Public Pension Reforms in Germany
— Major Post-War Reforms and Recent Decisions —[1]

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ドイツにおける年金改革

■ 要 約

年金改革は今日、先進国共通の課題である。中心的な問題の一つは年金政策における国の役割であり、特に賦課方式で運営されている公的年金の財政的安定性が大きな問題となっている。積立方式への移行を求める提案の多くは、少なくとも老齢年金の主要部分を民営化する案である。近年ドイツでも年金改革の議論が盛んになされているが、まだ結論を得るには至っていない。ドイツでは1998年9月の総選挙後に政権交替があり、97年に決められた改正法(1999年金改革法)の一部は新政権によって実施が延期された。

1999年金改革法の主な内容は(1)障害年金の早期受給にも減額を適用する(2)育児期間の納付とみなす給与水準を引き上げ、その分連邦補助金を引き上げる(3)45年加入の標準年金の手取り賃金代替率を、今後の65歳の平均余命の伸びに応じて今日の70％から2030年には64％に引き下げる(いわゆる「人口統計的要素」の年金算定式への導入)などであった。特に(3)は早期受給した場合に年金額が生活保護水準に接近し、公的年金に対する国民の支持が低下するとして当時の野党が強く反対していた。平均余命の伸びに対しては、年金算定式を変えずに退職年齢をさらに引き上げて対処する選択肢も考えられる。これは労働者に(a)より長く働いて今日と同じ水準の年金を今日と同じ期間受給するか、(b)就労期間を伸ばさず、より長い期間減額された年金を受給するか、の選択を迫るものである。

女性の年金問題や老齢年金の最低保証などのほかに、経済・社会政策上の最大の懸案は深刻な失業問題である。このため、新しい政府は労働組合、経営者団体、政府の間にいわゆる「雇用のための同盟」を作ろうとしている。この戦略の中で政府は若者の雇用を確保するため、再び早期退職政策を提案している。公的年金の水準が引き下げられれば、年金政策における第2の強制的要素(法律または労使協約による)に関する議論が活発になる。しかしこのことは、公的年金の分野でも、賦課方式からもっと積立方式を取り入れた財政運営に移行すべきかどうかの議論を巻き起こすことも意味している。

■ キーワード

年金改革、年金政策、人口統計的要素、早期受給、早期退職

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1. Introduction

Pension Reform at the end of this century is a world-wide debated topic. One of the central questions is the role of the state in pension policy. Especially pay-as-you-go financed public schemes are under severe political pressure in many industrialized countries. Often a radical shift towards capital funding is proposed, which mostly is linked to proposals for privatizing at least major parts of old-age security. In recent years also in Germany an intensive public debate on pension reform took place. This debate has not at all come to an end. In Germany after the election to the Federal Parliament (Bundestag) in September 1998 a change in government took place. The new political majority has suspended some of the reform measures the former government had decided upon.

There are many reasons for reform debates in Germany. Many are similar to other industrialized countries, namely demographic ageing, a changing structure of private households, intensified international competition after the breakdown of former socialist countries and their inclusion in international economic activities. Some challenges are different in its extent like the high unemployment rate, and at least one is specific for Germany: the economic consequences of German unification. In addition further steps for a closer European integration take place which also affect public pension policy.

To put the recent political discussion into a frame, some basic information concerning the structure of old-age protection arrangements in Germany will be given (2) as well as some information concerning the design and major objectives of Germany's public pension scheme (3). Then major pension reforms from 1957 to 1996 in West Germany (respectively in unified Germany) will be characterized in their basic elements[2] (4). Then the recent developments in Germany in 1997 and 1998 will be discussed more detailed (5) and (6). Finally, some remarks on possible future developments will be made (7). The focus of this article is on social insurance pensions, the major element of Germany's arrangements for social protection in general as well as specifically in old age.

2. The present structure of old-age protection in Germany

As in many other countries, in Germany a multi-pillar approach in pension policy (better to be characterized as multi-tiers or multi-layers) has existed for a long time.[3] The first tier consists of several mandatory pension schemes. The most important element of the first tier as well as of all old-age protection arrangements in Germany is the statutory pension scheme (social insurance) for blue- and white-collar workers. It is an earnings-related defined-benefit scheme, mostly financed by contributions (from employees and employers in equal parts). There exist several special schemes beside social insurance, e.g., for civil servants (also of the defined benefit type, but tax-financed) and for farmers. Supplementary occupational pension schemes in the private and public sector are the second tier. While in principle all white- and blue-collar workers of the public sector are covered by such an occupational scheme (based on collective agreement), only about 50% of employees in the private sector are covered by voluntary occupational pension schemes. Coverage is distributed very unequally according to size and branch of the firm.[4] The third tier consists of many different types of private saving for old age. The scientific and political debate was and is mainly focused on the social pension insurance. But especially since 1997 the specific pension scheme for civil servants (which is integrated within general public budgets) also has received public attention.[5]

Concerning the macro- and microeconomic impact of the different pension schemes, social (statutory) pension insurance is of overwhelming importance. It is paying nearly 70% of all expenditure for old-age security in Germany. Expenditure of social pension insurance is nearly 10% of GNP. More than 80% of the West German population is insured in this pension scheme; in East Germany the percentage is even higher.[6] For most retired people social insurance pensions are by far the most important source of income in old age. Therefore, discussion on social pension insurance is of great political and economic importance.

3. Some short remarks on the main elements and on the design of Germany's social insurance pension scheme

Looking at Germany's social security pension reforms in the period after the Second World War, some major reforms as well as some major topics of discussion have to be mentioned. The origins of the present social insurance pension scheme go back to the late 19th century, when Bismarck was chancellor of the newly founded German Reich. *Financing* was mainly based on employers' and employees' contributions. However, as an important element of financing (which was reflected also in the pension formula) a grant from the central public budget to pension insurance was introduced.

Since these days social pension insurance in Germany has been based on the idea of *insurance*, i.e., intertemporal redistribution and risk pooling, but also on *interpersonal redistribution.* The mix of different elements—namely equivalence and intertemporal redistribution on the one hand, interpersonal redistribution over the live cycle on the other—was and is a major topic of discussion. Also the organizational structure created in the founding period of the German social insurance has remained alive up to the present days.[7]

Bismarck's original idea for the type of pension scheme, however, was quite different from what was established in 1889: He originally aimed at a *tax-financed flat rate pension*; workers should become like "state pensioners". This idea—as a contrasting strategy to earnings-related pension insurance—often has been discussed in Germany up to the present days, especially when major reform steps in pension insurance became necessary because of changing conditions in economy, demography and society.[8]

Also the method of financing—*pay-as-you-go (PAYG) versus funding*—was discussed intensively in the late 19th century, taking e.g., into account effects on individual and national saving. And although public pension insurance in Germany originally was based in principle on fully funding, over time this became more and more a fiction because of inflation, war times, economic crises and by using accumulated funds for other purposes than pension financing.[9] But PAYG versus funding is still a topic of discussion, especially in the recent public (as well as scientific) debate in Germany.

4. Major pension reforms from 1957 to 1996

4.1 Introducing a dynamic pension in 1957

The first major pension reform in post-war Germany took place in 1957 by introducing the so-called "*dynamic pension*", linking pension calculation as well as pension adjustment to the development of gross wages (earnings). Also a major shift in the method of financing towards PAYG was realised: Only a limited reserve, covering pension expenditure for one year, was required.[10] This reserve requirement later was reduced, in 1969 to 3 months and finally in 1992 to one month only.

In the sixties, there was already a discussion on the future development of the pension scheme focusing especially on the *ageing* of the population. To cope with the expected financing problems it was proposed to accumulate some reserve by increasing the contribution rate to a higher level than necessary to balance the current budget and to use these reserves later in order to avoid a steep increase in contribution rates—the picture of "digging a tunnel into the pension mountain" was frequently used to illustrate this.[11] But contrary to this, in fact a reduction in reserve requirements was politically decided.

4.2 The Pension Reform of 1972: Flexible retirement age and increasing pension expenditure

Especially in the early seventies—based on optimistic projections of the future economic development for the next decades—huge future surplus in the pension scheme were calculated. This was in the years just before the first oil price crisis. Based on these calculations a political race between all political parties in proposing alternatives for *increasing pension expenditure* took place and resulted in several reform measures in 1972. That is the *flexibility of retirement ages* was introduced, allowing retirement before the former reference retirement age (for men, 63 instead of 65[12]) *without* introducing *actuarial* deductions from the pension.[13] A few years later the oil price development shocked the economy and several ad hoc measures were taken to reduce pension expenditure.

4.3 The '1992 Pension Reform Act' (of 1989): Net pension adjustment and a self-regulating mechanism

Especially demographic scenarios showing a rapid change in the age structure of the population and the consequences for public pension schemes were the main reason for a major pension reform decided upon on November 9, 1989 (the same day the Berlin Wall was opened in the evening). Most elements of this Pension Reform Act should be implemented in 1992 (therefore "1992 pension reform"). Nobody had expected that the introduction would take place not only in West Germany but after the German unification in East Germany, too. The reform measures were therefore aiming at influencing the future development of the pension insurance in *West* Germany (for a detailed discussion see Schmähl 1993b).

After several ad hoc interventions during the last about 15 years one aim was to establish again a set of clear rules, a self-regulating mechanism to stabilize the financing development over time and to reduce the financing burden for the working population in the future, while on the other hand an appropriate level of pensions compared to earnings should be maintained.

For a better understanding of the 1992 reform as well as of more recent reform measures and debates some basic information concerning the design of the social insurance pension scheme are given. As already mentioned, social pension insurance in Germany is a mix of a pure "insurance scheme" (aiming ex ante at intertemporal redistribution plus risk pooling) and a "tax-transfer scheme" (aiming at interpersonal redistribution, also over the life cycle). The "insurance approach" is dominating in Germany, resulting, e.g., in a (relatively) close link between individual contributions and later benefits, however, modified by measures of interpersonal income redistribution (e.g., by crediting years without gainful employment and without paying contributions during periods of schooling, illness, child care).[14] For many years, it has been a major political topic in Germany how benefits aiming at redistribution should be financed adequately. The result was higher transfers from the general public budget to social pension insurances based on decisions of the '1992 Pension Reform' and on decisions in 1997.

The German public pension scheme is earnings-related because:

- The individual pension benefit is linked to former own earnings of the pensioner.
- The absolute amount of the individual pension at time of retirement depends on the nation-wide average earnings close to the year of retirement.
- The development of the pension benefit during retirement is linked to the development of nation-wide average earnings.

The contributor acquires a pension claim according to the *relative* amount of his gross earnings (= wages or salaries): The individual gross earnings are compared year by year to average gross earnings of all employees. This ratio gives the amount of the pension points (Earnings points, EP) for this year. If for example individual gross earnings are equal to average gross earnings in one year, the result is one EP for this year. When claiming the pension, the sum of all EPs is taken (including also EPs credited according to special rules connected, e.g., to child care, schooling or times of unemployment).

To calculate the individual pension benefit the sum of individual EPs is multiplied by a factor (ARW; "actual pension value") representing the value (in German Marks) of one EP in a specific year. ARW is the dynamic factor of the German pension formula, because it changes year by year according to the growth rate of average earnings. Concerning the development of ARW over time, the 1992 Pension Reform Act introduced an important change, namely by linking ARW to the development of average *net* earnings instead of average gross earnings as in principle in previous years since the 1957 pension reform.[15]

The rate of change of ARW is also the factor for adjusting all pensions calculated in former years. This also means that all pensioners having the same sum of EP receive the same pension benefit irrespective of the year of retirement.

It was possible to claim a pension before the "reference retirement age" of 65 without reducing the pension benefit because of the extended period for receiving the pension. This was an incentive to retire early:[16] Since the introduction of "flexible retirement age" in 1972 a radical reduction of male labor force participation rates has taken place (e.g., of men at age 63 from 67% in 1972 to about 20% within less than 20 years). Although incentives in the pension scheme are not the only reason for this development, there are, however, clear indications that this was a major influencing factor.

The 1992 Reform Act was also aiming at postponing retirement. After a long controversial discussion, it was decided that beginning in the year 2001, over a period of more than 10 years some deductions from the pension should be introduced step by step, if retiring before age 65. Age 62 should become the earliest retirement age for starting an old-age pension, equal for men and women. The deductions were decided to be 3.6% (below an actuarial fair rate) per year of earlier retirement. Disability pensions, however, should not be burdened by a deduction. It was obvious, that also the rules for claiming disability pensions would have to be changed in the future in order to avoid that disability pensions became a loophole for early retirement.[17]

Another element of the 1992 reform package was a new formula for federal grants aiming at stabilizing the relative amount of this federal grant at about 20% of pension expenditure. Beside the development of average gross earnings, the formula for calculating the federal grant now also includes the development of the contribution rate to social pension insurance.

The changes of the adjustment procedure as well as the new formula for federal grants are elements of a self-regulating mechanism for the pension insurance scheme.[18] This seems to be an important decision from a political as well as an economic point of view; e.g., since 1992 no parliamentary decision about the pension adjustment rate or the contribution rate has been necessary. This is done automatically by the government according to clearly defined statistical data of the Federal Statistical Office. However, such a rule exists only as long as parliament does not change it.

A political objective concerning the level of pensions compared to earnings was decided upon in the 1992 Reform Act; for a so-called standard pension with 45 Earnings Points the pension shall be about 70% of present average net earnings of all employees.[19] Because pension adjustment rates are linked to the increase of average net earnings, the individual net pension level (individual net pension compared to average net earnings) remains constant over time.

The 1992 Pension Reform Act was based on a broad political consensus among the governing coalition parties and the major opposition party in the German Parliament and among employers' organizations and trade unions.[20] This consensus was in line with the experience from former major changes in pension policy in Germany. Looking for solutions on a broad political basis in this area that needs a long-term perspective could be interpreted as being an element of the "political culture" in Germany. Contrary to some other countries, the biggest political parties (Christian Democrats and Social Democrats) both were in favour of the "social state"[21] and shared many basic values.

4.4 1996: Breaking the trend of early retirement

For many years, a broad consensus among employers, trade unions and government also existed in aiming at a reduction of unemployment by early exit of older workers from the labor force as a socially accepted measure, because it would give younger people a better chance to become employed. A low youth unemployment rate in Germany compared to many other European countries seemed to confirm this. This consensus broke down. Since summer 1995 a political discussion was going on aiming at a reduction of early exit and the costs linked to this especially for unemployment insurance and social pension insurance, although unemployment remained on a high level.[22] Especially the effect on contribution rates and therefore also on non-wage labor costs was accused to be a negative factor in times of intensified international economic competition.

In February 1996 the federal government decided upon measures aiming at stopping the growing number of early retirees claiming an old-age pension at age 60 after a phase of unemployment: (1) The phase-in of the deductions from the full pension (3.6% per year) starts already in 1997 (and not in 2001) and will be much quicker compared to the rules in the 1992 Act: For pensions after periods of unemployment (age 60) the reference retirement age will be increased within 3 years (up to the end of 1999) by 3 years; thereafter for all types of old-age pensions[23] within the following 2 years up to 65. For the specific female retirement age (at 60) this process will (after strong resistance by several organizations) start in 2000 and the reference retirement age will become 65 at the end of 2004.[24]

For claiming a pension at age 60 beside unemployment an additional possibility was created: "part-time employment" of older workers after age 55, which—under special conditions—is supplemented by benefits from unemployment insurance. However, there is a lack of part-time jobs, especially for men.[25] Therefore, in reality this "part-time" employment means half of the period of full employment, thereafter employment with working hours of zero.[26]

Another starting point for reducing pension expenditure in the future was the reduction of the number of years of schooling credited without paying contributions.

The reduction of credited years of schooling as well as the introduction of deductions from the full pension in case of early retirement can be interpreted as elements of an underlying strategy to strengthen the contribution-benefit link—a strategy government seems to have become convinced of during the last years especially as a counteraction to proposals for shifting public pension policy to a flat-rate approach.[27]

5. The 1997 reform measures (the '1999 Pension Reform Act')

Although in the long-term perspective the financial outlook of social pension insurance in 1996 hardly differed from that in November 1989, when the '1992 Pension Reform Act' was decided, the discussion about its future development was brought up again into the political arena in summer 1996.[28] Several politicians and leading members of employers' organizations argued that more has to be done to avoid the consequences of the "demographic time bomb" and the expected future increase in contribution rates. The role of the mass media as reinforcing agent in the process of agenda-setting has increased during the last years.

While the development of calculated contribution rates based on assumptions of demographic and economic development hardly was new information, the climate obviously had changed. Coping with the economic and social consequences of the German unification—a process that lasted longer than expected in former rather optimistic political statements—high unemployment, the political will to meet the Maastricht convergence criteria leading into a policy of retrenchment in several areas, backed by mainstream economists as a supply side strategy as well as by pressure groups from industry, are some elements of the background for this new discussion in several areas of social policy, not only in pension policy. The climate between federal government and employers' organizations on one side, labor unions on the other became chilly especially after government (and the majority in parliament) decided to change the rules for continued wage payments in case of illness of employees—a highly sensitive topic for trade unions because the existing rule was the result of a severe strike in the past.

Mass media (especially newspapers and television) pushed the topic of a "collapse" of the pension scheme; banks and insurance companies argued in the same direction. As often in such periods of turbulences, radical proposals for abolishing the social pension scheme and introducing flat-rate pensions or at least reducing the pension level drastically were published. Although the argument often was to give people more space for "self-reliance", nevertheless these proposals were linked to obviously own interests for many advocates of radical changes from the business community.

Government in the beginning of this debate reacted only in a very passive way, promising that "pensions are secure". However, in summer 1996 because of the growing public debate the federal government decided to appoint an expert commission (chaired by the Minister of Labor) to propose additional measures for a new pension reform. At the same time another commission (chaired by the Minister of Finance) should develop proposals for a major income tax reform.[29] Both projects should be realised at the end of 1997 at the latest, i.e., near the end of the election period (the next parliamentary election was scheduled for September 1998).[30] While the government had a majority in the "Bundestag" (the federal parliament), the second chamber, the "Bundesrat" (representing the states, the "Länder") was and still is dominated by the Social Democratic Party.[31]

The debate in the commissions and the public debate concentrated on two main areas:

- Possibilities for a further reduction in the development of pension expenditure, aiming above all at a reduction of financing burden for "future generations" and
- a "fair" distribution of "burden" in financing of current pension expenditure, taking into consideration the different distributional targets (intertemporal versus interpersonal redistribution), and especially aiming at a reduction of non-wage labor costs because of labor market reasons.

The proposals of the expert commission aimed at maintaining the concept of earnings- and contribution-based (defined-benefit) pension scheme, while the concept of tax-financed flat-rate pensions was rejected. This was also backed by the majority in the political decision process. The main instruments to realise the above mentioned goals—as in principle proposed by the commissions[32] and finally politically decided—were the following:

In addition to already introduced changes in *retirement ages* for old-age pensions, deductions from the full pension were decided also for *disability* pensions. This was linked to some changes for old-age pensions once more: Starting in 2012, the earliest age to claim an old-age pension should become 62, but only for those having 35 years of insurance. The deductions would be 3 * 3.6% from the full pension. These 10.8% should also become effective for disability pensions in general.[33]

Additional pension expenditure, however, result from higher *crediting years for child care*—a measure that in general is an element of family policy (and resulting in interpersonal redistribution that should be financed from general public revenue and not from earnings-based contribution payments; this will be discussed below).

The most important change concerning expenditure was the decision to introduce a so-called *"demographic factor" as an element of the formula for calculating and adjusting (all) pensions*. The main argument was the following: Life expectancy increases; if the contribution rate shall not increase because of this development, a reduction in the pension level shall take place. The solution proposed by the majority of the expert commission of the government—and later decided by the federal parliament—was a compromise:

The development of ARW should be linked beside the rate of change of average net earnings[34] also by one half of the development of (further) life expectancy of people aged 65, however, with a time lag of 8 years. The parameters of this formula were chosen in such a way, that—in combination with other assumptions determinating the financing of the pension scheme—the so-called standard pension level up to the year 2030 should be reduced from today 70% to 64%.[35] How quick such a reduction of the standard pension level could take place according to this formula depends in reality, however, among other factors on the development of life expectancy.

The parliamentary decision to include such a factor—aiming at a reduction in the pension level—could have, at least in the long run, some very negative effects. Some arguments to explain this opinion are the following:

(1) Transparency of the pension formula is reduced, it becomes less understandable for the insured.[36] This may lower the acceptance of the scheme.
(2) The introduction of the additional factor is a (first) step to break the link of pension development and earnings development. This earnings-linked pension development has been a cornerstone of the German public pension scheme since 1957 (and it exists in principle also in the specific pension scheme for civil servants).
(3) The pension level becomes a variable; a specific number of Earnings Points does not anymore give the insured person an information about the relative amount of the pension compared to average net earnings. Planning for own additional old-age provision becomes more complicated.
(4) The reduction in the pension level has remarkable consequences for the income of the insured and
(5) the general reduction of the pension level can have the effect, that a great number of employees even after long periods of paying contributions to the scheme only receive a pension that is hardly higher than social assistance. This could undermine legitimacy and acceptance of the mandatory contributory scheme.

The last two points shall be illustrated by some numerical information: Based on the rules for calculating and adjusting pensions as decided in 1989 and explained above, the "standard pension" (45 EP) is about 70% of average net earnings (of all employees). Compared to this a full claim for social assistance (if no other income exists) is 40% of average net earnings. A contributor who was an "average earner" needs 26 years of insurance to receive a pension just as high as this social assistance level. Somebody who only earned 2/3 of average earnings even needs 40 insurance years. If the pension level is reduced generally as aimed at by the additional factor in the pension formula, more years of insurance are needed for a pension that is as high or even above the social assistance level.

Therefore, for the future it is decisive how many EP workers can accumulate during their working life. Here one has to take into consideration the following facts: (a) Today about 50% of male and 95% of female old-age pensioners have less than 45 EP. (b) Future working lives (and earnings development) may be less stable than in the past. This may reduce the possibility to accumulate pension claims (EPs). (c) There are already changes in rules for pension calculation that do not affect the (fictitious) standard pension (which always is based on 45 EP) but the individual EPs (an example is the reduction in years credited for schooling). (d) In the future a "full" pension without deductions will be paid at age 65. Those who retire earlier (e.g., at age 62) have a reduction of 10.8% in their pension amount.

Assuming a standard pension level of 64% (45 EP at age 65), when claiming the pension already at age 62, even the standard pensioner has a pension level of only 57.1% (of average net earnings). If a pensioner has 40 (instead of 45) EP, his pension level is less than 51% (while the social assistance level is 40%).

In the long run such a development could undermine the legitimacy of a scheme obliging employees to pay (high) contributions for a long time without giving pensions that are remarkably higher than social assistance.

However, there exist alternatives to a general reduction in the pension level to cope with the consequences of an increasing life expectancy, that is an extension of retirement ages. Reference retirement age could be linked to changes in life expectancy, while the pension formula itself remains constant (proposed in Schmähl 1997a). Such an increase in retirement ages could start, e.g., around 2010/2015, in a period when labor market projections show a change in labor market conditions, among other things because of the demographic development (resulting in a remarkable reduction in labor supply). This would show workers very clearly that they have to make a decision: Working longer and having the same pension level as today for about the same length of retirement or receiving the pension for a longer time, but at a reduced level (because of the deductions from the full pension).

Government could realise changes which affected the expenditure side of the social insurance budget by its majority in the Bundestag. The opposition parties were strongly against the changes for disability pensions as well as the new factor introduced into the pension formula. They promised that these reform measures would be cancelled if a change in government after the 1998 elections took place. Meanwhile this was realised (see below).

To avoid higher contribution rates in the pension scheme by unfavourable political conditions as well as to reduce the contribution rate and thereby (non-wage) labour costs government planned to give more money from the federal budget to the pension scheme to cover some of those expenditure aiming at (interpersonal) redistribution, but still financed by contribution revenue. An increase of the value added tax required the agreement of the second chamber, the Bundesrat, with its majority of the opposition party.[37] Although all political parties wanted such a change in the structure of financing (as well as employers' organizations and trade unions)[38] only after a process of many months the opposition agreed in increasing the value added tax.[39]

6. First decisions in pension policy after the election to the German Federal Parliament in September 1998

The coalition government of Christian Democratic and Liberal Party was replaced after the September election to the Bundestag by a coalition of the Social Democratic and the Green Party. As announced and proposed by Social Democrats prior to the election, they wanted to abolish some of the measures the old coalition had decided. However, the Green Party is in principle in favor of a general reduction of the pension level in combination with more redistribution within the scheme. Therefore, the new coalition only agreed upon a suspension of two major elements of the '1999 Pension Reform Act' namely the so called "demographic factor" of the pension formula and new rules for disability pensions: Up to the end of the year 2000 decisions shall be taken to replace these elements; if the government is not successful in doing so, the old rules shall be implemented. It is not clear up to now, which proposals will be launched. There exist conflicting views whether the pension scheme should be developed towards a closer contribution-benefit-link or towards (interpersonal) redistribution.

Some decisions were taken very quickly, namely to increase the transfers from the federal budget to cover expenditure for redistributive measures within the pension insurance, resulting from German unification as well as from crediting Earnings Points for child care. For the latter, in the future contributions will be paid by the federal budget to pension insurance to cover these pension claims. This is in line with already existing rules. For periods of unemployment the unemployment insurance pays contributions to the pension scheme as well as to the new long-term care insurance for caregivers (see Schmähl and Rothgang (1996)). This is—from my point of view—an approach, which results in a clear rule step by step: Pension claims are only granted, if an adequate contribution payment is existing (from gainful employment or from other public budgets which are responsible for the specific task). This will make the contribution-benefit link in social pension insurance even closer as it is today and may increase acceptance for the scheme.

These additional payments from the federal budget will make it possible to reduce the contribution rate from 20.3% (in 1998) to 19.5% (in April 1999). The money shall come from an energy tax (the exact rules have not been decided upon up to the end of 1998).

Additional decisions are aiming at increasing the number of contributors to the pension scheme, namely new types of self-employed as well as employees with earnings below a lower contribution limit. The existence of such a limit (about 1/7 of average gross earnings) without paying contributions gives an incentive for employers to offer such jobs as well as for employees to accept them (even in addition to another job which is covered by social insurance).[40] Here also details of the new rules still have to be decided.

7. Some topics for discussions and decisions in the near future

The "old" government already announced a second phase in pension reform after the 1998 election focusing on widow's and widower's pensions and old-age security of women.[41] This remains on the political agenda.

There are demands for introducing minimum elements for old-age protection. Two different approaches are discussed: to increase such minimum elements within the pension scheme or to modify existing rules for means-tested social assistance (i.e., outside the social insurance system). These demands are based among other things on expectations concerning the future development of individual working careers and especially the difficult problems for employment of people with low qualifications.

The most pressing problem in economic and social policy is the high and long lasting unemployment. Therefore, the new government tries to establish a so-called "alliance for work (employment)" of trade unions, employer and industry organizations and government. As an element of this strategy government proposes measures for further early retirement, hoping to offer additional jobs for young people by this. Although the experiences with such a strategy in the past were not promising at all, this is on the political agenda. Government wants trade unions and employer's organizations to decide on collective agreements for transferring part of the wages into collective funds. The money shall be used to compensate for reductions from the full pensions for those employees retiring before the reference retirement age. Additional money of these collective funds shall be used to establish capital-funded additional pension claims. These plans are up to now not well defined and are strongly disputed. It has also not been discussed up to now how this may affect occupational pension schemes. The present discussion is in my view, however, an indicator for a tendency clearly to be seen in international development: If the public pension scheme is reduced in its level, the discussion about additional mandatory elements in pension policy — either by law or by collective agreement—are stimulated.[42]

This very clearly shows, however, that, e.g., there will be further discussion about a shift from pay-as-you-go financing to more capital funding—even within the public sector. It is not possible to go here into the micro—and macroeconomic effects of such a strategy.[43] During the last months, however, the strong pressure especially from commercial banks and many economists in favour of capital funding, especially by investing in stocks, at present is modified a bit because of the recent experiences during capital market crises. There is also a debate in Germany on the rates of return in social pension insurance compared to other alternatives in provision for old age. However, the figures presented here often are rather biased, e.g., by not fully taking costs into account.

All these topics mentioned clearly show that the discussion in Germany about pension policy will remain lively during the next time. At the end of 1998, the pathway into the future is not fully clear.

Note

1 This paper was written at the end of December 1998.

2 It is beyond the scope of this paper to deal with the different development that took place after Second World War in the "German Democratic Republic" and the problems resulting from the different structures in East and West Germany of pension schemes in the process of integrating the population of East Germany since 1990 into the West German public pension scheme, see Schmähl (1992a).

3 An overview is given in Schmähl (1998).

4 A detailed analysis of occupational pension schemes and its link to social insurance is given in Schmähl (1997c).

5 A dominant feature of Germany's public pension schemes is that pensions are calculated according to former earnings, in social pension insurances taking into account the whole "earnings career", while civil servants' pensions are linked to last earnings. This specific scheme can be interpreted as a mix of first and second tier.—The social pension insurance as well as the civil servants pension scheme are dealing with old age, but also with the risk of disability and there are pension payments for the surviving spouse.

6 In East Germany occupational pensions in the private sector as well as life insurance expenditure are up to now hardly relevant. That means, that social pension insurance in East Germany is even more important as an element of old-age protection than in West Germany today. Some reasons for this difference are the following: In the former socialist German Democratic Republic social insurance covered nearly the whole population. There existed some special pension schemes (e.g. for military personnel). After the German unification schemes for special groups of the population were introduced only step by step and the number of people of these groups (like self-employed, civil servants) increases only slowly over time.

7 Different agencies for blue-collar workers on a regional basis, while for white-collar workers one central agency was established in 1911. Due to the changes in the structure of employment, there are less and less blue-collar workers. This shift to white-collar workers results only with a long time lag in a shift in pensioners of the two parts of the pension system. Methods of fiscal equalization became necessary, because financing as well as pension calculation are identical for both groups of insured employees. The fact that blue-collar pension agencies have less and less "clients" resulted in a discussion stimulated by the states (Länder) to reorganize pension agencies, to strengthen the agencies on the regional level and to cut down the central agency (on the federal level).

8 An overview on this discussion is given in Schmähl (1993a).

9 Mörschel (1990) is describing the development over time.

10 At the end of a 10-year period a reserve to cover pension expenditure for one year was required.

11 The focus therefore was not mainly on additional saving, investment and economic growth, but on intertemporal aspects of sharing the "burden" between generations.

12 To retire at age 63 became possible, if 35 years of insurance were fulfilled.

13 There existed already possibilities for women and unemployed (meeting several requirements) to retire at age 60 without deductions from the full pension. Later, also for handicapped, a further lowering of the retirement age was decided, see Jacobs and Schmähl (1989).

14 There exists no general minimum pension. To avoid poverty in old age a means-tested social assistance exists. But only less than 2% of all pensioners claim additional social assistance.

15 Net earnings is defined as gross earnings minus income tax on earnings and employee's part of social insurance contributions to statutory pension insurance, health insurance and unemployment insurance.

16 Retirement age, however, is not identical with exit from the labor force for older workers. There exist several other possibilities to end official gainful employment without claiming an old-age pension, namely a disability pension (the number of disability pensions is to a certain degree also linked to the labor market conditions), several pre-retirement agreements. A detailed discussion of existing possibilities as well as of the changes decided upon in the '1992 Reform Act' is given in Schmähl (1992b) and in Schmähl et al. (1995).

17 Another new element was the introduction of a partial pension. Mainly because of the unfavourable labor market conditions as well as of other possibilities to leave the labor force early, this possibility for a phased retirement up to now has been no success. Only a negligible number of pensioners claimed such a partial pension. It is possible to claim either one third, one half or two thirds of the pension and supplement earnings from part-time employment.—Viebrok (1997) analyses in a very differentiated manner the labor supply effects of the German social security scheme, theoretically (taking into account the institutional arrangements) as well as simulating effects based on a dynamic progamming approach.

18 For a more detailed analysis see Schmähl (1993a).

19 For employees with lower pension claims this percentage is lower and vice versa. That is for a pension based on 40 EP the target pension level is $40/45^{*}$ 0.7 (= 62.2%) instead of 70%.

20 The "social partners"—unions and employers' organizations

—also work together in the self-administration bodies of social insurance.

21 The term "social state" (*Sozialstaat)* (is used in Germany instead of "welfare state"; *Wohlfahrtsstaat* is the German literal translation. Wohlfahrtsstaat has in German a different meaning compared to "Sozialstaat".

22 A widely used measure for pre-retirement was and is the layoff of older workers and supplementing the unemployment benefit by a payment of the employer, so that the net income of the now unemployed person remains nearly the same as in the period of employment. After a period of unemployment, the old-age pension can be claimed at age 60. There was a sharp increase in taking up this type of pension. In 1994 about 20% of all male pensioners claiming a pension used this pathway into old-age pension; in East Germany this percentage was even much higher, more than 40%. This measure was used particularly by big companies.

23 This means that also the existing "flexible" pension, which can be claimed from age 63, will be "burdened" by deductions.

24 According to the 1996 decisions old-age pension could be claimed at its earliest at age 60, however with a deduction from the full pension by 18% (5^{*} 3.6%).

25 This is also the main reason, why the "partial pension" introduced already in 1992 has not become an effective instrument. E.g. in 1994 only 0.15% of all new pensions were partial pensions.

26 For a detailed discussion of early retirement see Gatter and Schmähl (1996).

27 For a detailed discussion of arguments in favour of such a strategy aiming at a closer contribution-benefit link see e.g. Schmähl (1985).

28 In 1989 it was calculated that the contribution rate would be about 27% in 2030 (including the 1992 reform measures), while in 1996 (taking into account the additional decisions up to 1996) the contribution rate was expected to become 25.5%—It should be taken into account when looking at these contribution rates that the rate is about 1 percentage point higher because of transfers from West to East Germany, about 2 percentage points are used to finance redistributive measures (instead of financing by taxes) and at least 1 percentage point is due to the fact that the pension scheme was used as an instrument of labor market policy.

29 In addition, e.g., the Christian Democratic (and Christian Social) Parties also established party commissions.

30 There was hardly any direct contact and coordination of the two reform commissions as well as the two reform projects, although there exist some direct links of tax policy and pension policy. For a discussion see Schmähl (1997b).

31 It is not possible to go here into the process of passing a law. But if the states are affected, they have to approve it, too. Even in all other cases a complicated, time-consuming process is necessary if there are different majorities in Parliament and Bundesrat.

32 See especially the proposals of the Expert Commission (1997).

33 There are some other technical changes not discussed here as well as changes for pensions for handicapped people.

34 Which reflects also increases in life expectancy as far as this increases the contribution rate of the pension scheme.

35 If a pensioner has 40 EP instead of 45 EP (standard pension) the present pension level is $40/45^{*}$ 0.7 = 0.62 and would decrease according to these plans to $40/45^{*}$ 0.64 = 0.53 for the full pension when claiming the pension at reference retirement age (i.e. in the future at age 65).

36 In my view it would be preferable not to make pension insurance directly dependent on the development of other variables (like the different contribution rates to social insurance and income tax), but on the contrary to limit the number of these variables: Linking ARW only to the growth rate of average gross earnings and the contribution rate to pension insurance. This is discussed in Schmähl (1997a).

37 Revenue of the value added tax is for the state as well as for the federal level.

38 A detailed discussion of the financing structure, its effects and the arguments for change is given in Schmähl (1997d).

39 The reason why they agreed, mainly was the fact that due to the unfavourable labor market situation (especially a downward development in the number of contributors and a slowdown of contribution revenue) the contribution rate in 1998 otherwise would have had to be increased from 20.3% to 21%.

40 If for social pension insurance the contribution-benefit link is very close, then the attractivity of not being covered will be reduced as well as the "tax wedge"—compared to the difference of labor costs and net earnings of employees (for a detailed discussion see Schmähl 1997d).

41 This is closely linked with the interaction of labor market development, family structure and family policy and old-age security. For an overview of proposals under discussion in Germany see Horstmann (1996).

42 This tendency was already documented by many examples in Schmähl (1991), pp. 47–50.

43 E.g., if the contribution rate shall be higher than necessary to balance the budget.

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