The Politics of Pension Reform in Germany

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1. Introduction

After a series of changes enacted between 1989 and 2001, at the end of 2003, the Red-Green government in Germany got involved in another enterprise of reforming pensions. Apart from closing a short-term deficit of the public pension scheme, the main rationale for the latest reform initiative is again *demographic aging*. It results from both below-replacement fertility and ever greater life expectancy and concerns those welfare programs disproportionately utilized by the elderly, as are health and long-term care services, but most heavily affected are old-age pension schemes. The combination of an ever more elderly-biased age structure and a shrinking population of what presently is defined as employable age pose severe problems for a welfare state which, in its expenditure orientation, is elderly-biased anyway, not the least since public pensions regularly represent the largest single item of total social spending.

Germany is among the Western countries where fertility has been very low since about the mid-1960s. This will — according to the median variant of the latest official projections — lead to a shrinking population size: from presently 82 million to 75 million in 2050 (see *Table 1*). Due to increasing longevity, a smaller population size goes along with a rising share of elderly. The percentage of elders (60+) already exceeds that of the young generation (<20) since the 1990s, and more than one third of the population will be 60 years of age and older in 2030 and thereafter.

If one starts from a continued *actual* retirement age of about 60 years, it is obvious that compelling an ever smaller working age population[1] to finance pension benefits for a growing percentage of the population for an ever longer period of their lives constitutes a serious political challenge. It will hardly be eased by a declining share of young people who are also dependent on income support as long as they are still children or involved in education. *Table 1* shows the interesting fact that, in case the projected figures come true, the *total dependency ratio* in 2050 will be almost the same as it was at the beginning of the 20th century when Germany was incomparably less wealthy. For one thing, many more youngsters below age 20 were actually in the labor force then and, almost regularly, older employees continued working until death or disability since public pensions were low and explicitly meant to *supplement* other resources. More important is, however, that spending on the young generation is mainly private, i.e. by sharing the family's resources. Compared to the elderly, per capita public spending on the young is *substantially* less although, in

[1] Whatever extreme assumptions about an increased participation rate of women and higher net migration are made, the potential labor force in Germany will definitely start to decline after 2010. According to the most realistic scenario between 2010 and 2040 it is going to decrease from 40.5 to 29.9 million persons what is about 25 per cent (Fuchs and Thon 1999).

cross-country comparison, the shares vary (Lynch 2001; Esping-Andersen and Sarasa 2002).

****** *Table 1* about here ******

Hence, population aging remains a challenge for matured welfare states, adding to other strains they are facing: lower growth rates as post-industrialism progresses, structural changes in the labor market (decline of the "standard employment relationship"), more diversity in private (family) households and, finally, *globalization*. Paul Pierson (2001) has questioned whether globalization indeed represents an *autonomous* cause of pressure on welfare states and a major threat to their central features. Notwithstanding the validity of this argument, globalization reinforces the pressure on political actors in the welfare state to tackle the aging problem through pension reforms, and it becomes effective in the reform discourse in at least in threefold manner.

First, besides a rapidly growing volume, intensity and speed of cross-border transactions regarding goods, (financial) services and capital investments, globalization means that *information* flows almost without a time difference. Epistemic communities are part of an increasingly transnational exchange of information. Their role in the political discourse on potential responses to demographic aging and the future of (public) pensions has increased, and it is further fuelled by interference of supranational organizations (like the World Bank, the International Monetary Fund or the OECD). This is so because the interest in "successful" or "innovative" pension reforms abroad and to adopt seemingly "best practices" has grown. The *Open Method of Coordination*, applied be the European Commission in the area of old-age pensions, is another attempt to put that interest into practice when national pension systems and reform strategies in EU member states become exposed to some kind of competition.

Second, recent pension reforms in developed nations regularly imply a larger role of (mostly private) funded schemes and thus, for the time being, more savings have to be invested most profitably. In view of largely liberalized (deregulated) financial markets, pension funds and other institutional investors have become global actors when they operate worldwide and on a still growing scale. These multinational corporations and/or corresponding interest associations are attempting to gain a stake in national discourses on pension reform and to influence the direction of the reform process with regard to state regulation of their activities and the potential volume of their business.

The third relationship between globalization and population aging *viz.* pension reform is particularly relevant for Germany as *the* "social insurance state" *par excellence*: in no other OECD country, contributions to social insurance schemes make up such a large share of GDP as in Germany, namely, 18.6 per cent in 2001 which is about 43 per cent of total public revenues (Bach et al. 2002, p. 662; see also below, *Table 2*, col. 2). High proportional taxes on employing labor (up to an earnings ceiling) are presumed to have two effects: *(a)* Particularly jobs yielding low productivity are endangered to be substituted for by capital, and in the labor-intensive service sector the creation of corresponding jobs is impeded. That problem will aggravate when, due to population aging, contribution rates to the public pension scheme as well as to statutory sickness funds and long-term care insurance have to be raised. Fewer jobs for low-skilled workers would shrink the contributory base, increase outlays (unemployment benefits) and, thus propel a vicious cycle. *(b)* Since social insurance contributions are partly shifted forward into labor costs, a country like Germany is prone to lose out on "locational competition", i.e. to be no place of profitable investment and production anymore. In a globalized economy high total wage costs may not only scare off investors of capital, but also employees due to the tax wedge: it could cause a "brain drain" of domestic workers with a high earnings potential and, *vice versa*, make Germany a comparatively less attractive place for potential immigrants. The influx of preferably young and well-educated migrants is a most important option to *moderate* the effects of demographic aging. Framing the aging issue in the globalization context thus urgently calls for pension reforms containing the combined contribution rate to the social insurance schemes as a "no alternative" policy.

A major obstacle to cope with this seemingly irrefutable demand is that of all welfare state programs a pension scheme organized as a social insurance turns out to be the one most resistant to change. According to Titmuss (1976, p. 60), 'contributory "rights" and privileges, spanning perhaps fifty years, become sacrosanct'. This is so because entitlements are "earned" through prior contributions and are regarded as "quasi-property rights". Moreover, the opportunities of workers to adjust to policy changes decline to zero as they approach retirement age. The metaphor of the "generational compact" is thus a conceptual arrangement meant to bridge the temporal cleavage between the stages of a complete adult life, ranging from first covered employment to the last pension benefit paid. Maintaining *confidence* in the scheme's continuity and stability is thus an essential requirement. Additionally, the "generational compact" signifies a self-reproducing cooperative solution for income redistribution: based upon serial reciprocity it ties together the elderly, being interested in fair as well as sufficient pensions, and contributing members of the working age generation who want to see their parents and, after all, themselves well provided with public pensions. Therefore, these schemes regularly enjoy high esteem and support among citizens of all ages, adding up to a *broad constituency*. Living up to current and future beneficiaries' expectations of reliable income security nonetheless poses a difficult challenge for public policy. In order to overcome *inertia* as an institutional feature of pension schemes, reform considerations of policy-makers in this area of social policy are typically shaped by a very long time frame, stretching well beyond one parliamentary period. It entails a specific pension *politics*, among others, regularly resulting in attempts to spread the consequences of adjustments into the future in Generous phasing-in or phasing-out clauses avoid immediate hardships, but timely responses to imminent problems are essential.

Germany started early to meet the challenge of an aging population and passed the Pension Reform Act 1992 (hereafter: *PRA92*) in 1989. After enacting the *PRA92* the assessment prevailed among all relevant political actors that no substantial legislative change had to be considered much before the year 2010. Actually, already when the *PRA92* was going into effect a changed interpretation of the scheme's financial viability in the short and long run began to spread. It became the starting point of further so called "structural" reforms which, however, remained within the realm of *parametric* changes, but led the way to a *paradigmatic* shift in 2001. The reform process until the 2001 legislation is dealt with in section 2. which, in order to show the subsequent paradigm shift more clearly, begins with a short review of the pension reform of 1957. Section 3. describes the emergence and elements of an old-age security system that, with regard to goals, principles, actor constellations and possibilities for further development, substantially differs from the traditional one-pillar approach. Thereafter it is analyzed *how* such a path-departing turn towards a multi-pillar pension system came about, and special attention is given to policy-*makers*' strategies vis-à-vis the perceptions of policy-*takers* since issues like institutional trust (reliable income security) and the legitimacy of the pension system were most important. Besides looking into the political and socioeconomic constellations — or: the changing *politics* — facilitating or even demanding a break in continuity, in section 4. the most recent reform attempts are described and evaluated as well. Starting from the German case, the concluding section discusses the '"frozen" welfare state landscape' argument (Esping-Andersen 1996, p. 24).

2. Public pension policy in Germany, 1989 — 1997

2.1. The starting-point

Until 1957, central traits of the German public pension scheme[2] which are assumed to be

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[2] Nowadays, the "public pension scheme" compulsorily covers all white-collar and blue-collar workers above a certain earnings threshold and, additionally, the artisans (other self-employed may join voluntarily). Civil servants (nearly 6 per cent of all employed persons) are provided for through a uniform, tax-financed program without own contributions. Farmers are included in a special scheme, and the professionals (doctors, lawyers etc.) have to join non-public pension funds.

generically "Bismarckian" — particularly the equivalence principle and status maintenance — were merely embrionic. Although benefits were linked to preceding contribution payments right from the beginning, elements of basic security, representing remnants of Bismarck's original plan of a tax-financed flat-rate pension, still played a role after World War II. Nevertheless, benefits emanating from this static scheme were low and, conceptually being part of a "multi-pillar approach" (as would be today's terminology), meant to simply *contribute* to other sources securing livelihood in old age, like private provision, family support, (reduced) earnings from continued work or (selective) occupational pensions. Despite an incremental expansion of the scheme since 1889 and several *ad hoc* benefit increases after 1951, in 1956 the *average* pension amounted to no more than 25 per cent of net earnings for blue-collar workers so that, for almost all low-skilled, "being old" was synonymous with "being poor". White-collar workers who attained an average replacement ratio of about 40 per cent were somewhat better off (Alber 1989, p. 183; Döring 2000).

****** *Table 2* <u>about here</u> ******

The pension reform of 1957 had an *immediate* impact on the economic well-being of current retirees when the benefit formula and the post-retirement adjustment of benefits were made *dynamic* (Hinrichs 1998): taking into account individual, lifetime earnings in relation to average earnings of all insured (thereby granting credits for military service, spells of unemployment and education) when calculating the pension amount and annually upgrading it according to *gross* wage growth made the retirees participating in economic progress. The benefit increase of almost 70 per cent in spring of 1957 transformed public pensions as a floor of retirement income into an actual wage replacement that went up to a higher ratio subsequently (see *Table 2*, col. 4). Although basic security elements were abolished completely, the number and rate of elderly people being dependent on (additional) social assistance payments declined.[3]

Providing (future) pensioners a stake in the "economic miracle" substantially contributed to the support for the new *economic order* ("social market economy"). At the same time, the reform helped to further consolidate the legitimacy of the restored *democratic*

[3] The reduction of old-age poverty was enhanced as a result of the expansionary 1972 reform: a revaluation of covered earnings below 75 per cent of average favored low-paid workers with long employment careers (and their surviving widows). Internal redistribution was further enlarged when a flexible retirement option (at age 63; for seriously handicapped persons at age 60) without permanent benefit deductions was created. Moreover, self-employed and other non-covered groups were offered the opportunity to enter the public scheme on extremely favorable terms by paying low retroactive contributions (Baldwin 1990, pp. 281-3).

system as it effectively demonstrated its ability to deliver "social security". Albeit the 1957 legislation established the pattern of consensual pension policy (lasting until the 1990s; see below) when it eventually passed parliament with the votes of both Christian Democrats and Social Democrats, competitive party politics was central: the Social Democrats came forward with a reform bill first and "pushed" the government to present a more generous proposal than it originally planned. However, only the incumbent Christian Democrats were given credit for this most popular post-war social policy reform when, for the first and only time, they attained an absolute majority in parliament after the federal elections in September 1957.

Assessments as to whether features of institutional continuity prevailed in the 1957 reform (Conrad 1998) or it factually meant a *path shift* (Döring 2000) differ. Supporting the latter position, Mätzke (2002) argues that a conversion had happened which manifested itself as a 'conservative innovation'. Within this combination *conservative* relates primarily to 'organizational form', i.e. preserving occupationally segregated schemes with still no universal coverage or the continuing role of social partners in the schemes' administration. *Innovation* mainly concerns 'institutional form' and refers to the goal shift that occurred on the benefit side of the scheme when this institution was assigned a new mission, namely to provide *wage replacement* according to the equivalence principle at a level that maintains pre-retirement living standards after a full occupational career *and* all through retirement. Hence, not earlier than 1957 the old-age income system attained its specific shape that is usually associated with Germany as the prototype of a conservative welfare state regime.

Moreover, the 1957 reform meant the "birth" of the *one-pillar approach* in Germany because a *net* replacement ratio hovering around 70 per cent even for employees with earnings up to about 1.7 to 1.9 times the average[4] (see *Table 2*, col. 4 and 5) reduced the need to strive after further income for an extended and from now on virtually work-free period of life. Whereas elderly people's resource mix during the late 19th century and beyond most often signaled straitened circumstances, after 1957 a more varied public/private mix of retirement income, almost regularly, became an indicator of affluence: due to the relatively high level of public benefits, occupational pension coverage remained low. Like additional private provision for old age (financial assets or home equity) of some significance it was largely confined to the more prosperous parts of the work force. Despite much rhetoric about the "three-pillar model", due to the "crowding-out" effect of quite generous public pensions still about 80 per cent of total retirement income stems from unfunded public sources (when

[4] The "target" or "standard replacement ratio" is defined as *net* benefit level for a *fictitious* pensioner after spending 45 years in covered employment and constantly receiving an average wage as percentage of former *net* earnings. Due to the strict equivalence principle it would also apply to pensioners whose earnings had been always below or above the average, but progressive income tax factually implies a higher net wage replacement for former employees with above-average wages.

the civil servants' pensions are included – Deutscher Bundestag 2002, pp. 317-21).

2.2. *Containing the future rise of the contribution rate: general and selective retrenchments*

Increasing outlays and declining contribution revenues out of actual earnings beleaguered all social insurance schemes in Germany after the "sudden death" of full employment in 1974. In the public pension scheme, additionally burdened with the costly consequences of the expansion concluded in 1972 (see above, **n. 3**), this pressure implied a series of discretionary interventions into the indexing formula so that instead of steady gross wage adjustments a *factual* net wage development of pensions occurred after 1977. Moreover, the contribution rate was increased several times. Apart from "dutiful" protests of the respective opposition parties, these "first-order changes" (Hall 1993) were largely undisputed due to the 'grand coalition of path dependants' (Conrad 1998, p. 112) that had been established in 1957. It was a policy network with a shared belief system regarding the techniques and principles of social insurance, and it included the social policy experts of both *Volksparteien* (CDU/CSU and SPD), representatives of the social partners, the administrators of the public pension scheme as well as the academic advisers. Thanks to its interpretative hegemony that policy network was able to fend off attacks on the prevailing policy paradigm and to successfully push through reforms *within* the system as against system shifts (e.g. moving towards capital funding or a tax-financed basic pension scheme). Commitment to now consolidated institutional features meant a preference for technical solutions which, after a joint learning process, usually resulted in compromises acceptable for all actors involved.[5]

Therefore, the preparation of the *PRA92* was a highly depoliticized and deparlamentarized course of events. There was almost no controversy on the implications of demographic aging and the need for timely action when, at that time, the equally non-acceptable alternatives either were to exempt retirees from any benefit cuts, and then gradually have to increase the contribution rate from about 18.7 to 36.4 percent by 2030, or to cut benefit levels by half while maintaining a stable contribution rate. The final reform bill was a compromise between the government parties (CDU/CSU and Liberal Party) and the

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[5] It almost looks as if Peter Hall (1993, p. 291) has had in mind the German public pension scheme when he argued that '(policy) paradigms are most likely to be found in fields where policymaking involves some highly technical issues and a body of specialized knowledge pertaining to them (and) ... are likely to have greatest impact in institutional settings where policy is superintended by experts or by administrators with long tenures in office.'

Social Democrats, and both social partners had agreed to it as well. The cumulative effect of the altogether incremental reform elements should reduce the increase of the expected contribution rate by almost 10 percentage points (Schmähl 1993; Sozialbeirat 1998, p. 242).

The difference to the pre-reform projections mainly stemmed from the three changes mentioned first in *Figure 1*, i.e. an increased and in future constant share of federal subsidies, introducing permanent deductions if pensions are claimed before age 65[6], and the shift to net wage adjustment. The central idea of the new indexing formula was the 'fixed relative position' (Myles 2002, p. 141, referring to Musgrave), i.e. to ensure a *stable target replacement ratio of 70 per cent* and to make pensioners participating in demographically (or otherwise) induced alterations of social insurance contributions and income tax codes that would change employees' *net* wages.

****** *Figure 1* <u>about here</u> ******

When the *PRA92* that passed the legislative bodies in November 1989 became effective in 1992, the "unification boom" was almost over in West Germany and employment in East Germany was still in steep decline. As a result of the deteriorating labor market situation the number of elderly unemployed who claimed an early retirement pension (starting at age 60) nearly exploded. The concomitant rise in social spending and the increased contribution rates to the social insurance schemes can be read off from *Table 2* (col. 2 and 5). This development contributed to another round of retrenchments of the public pension scheme being included in an omnibus bill enacted in 1996 (*WBG* – see *Figure 1* for the main elements). The *WBG* enhanced the effects of the *PRA92* when it accelerated the phasing-out of early retirement options without permanent benefit deductions and further reduced various non-contributory entitlements. The Social Democrats and the unions vehemently opposed these changes (and further elements of the omnibus bill, e.g. waiting days for sickness benefits). The passing of the *WBG* in parliament and the subsequent preparations for another major reform (*PRA99*) by the Christian-Liberal government marked the end of the traditional "pension consensus" between the two large parties (and also created less unanimity among the social partners) — although there was no principled dissent on all changes included in the reform bill enacted in 1997.

For example, higher federal subsidies, financed out of an increased VAT rate (already

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[6] At first glance, a permanent deduction of 3.6 per cent for each year of premature retirement seems not much of a disincentive for not working until age 65. However, no credits are earned for those years (or months) not spent in covered employment anymore which amount to a reduction of about 2 per cent per year. It is nevertheless contested whether the deduction is actuarial or not (Börsch-Supan and Schnabel 1999; Ohsmann et al. 2003; Salthammer 2003).

beginning in April 1998) and meant to cover non-contributory components of the benefit package more completely, were not contested as was a further improvement of child care credits (see below). However, the two most momentous reform elements of *PRA99* were, at the same time, the most controversial ones: *(a)* In order to push through a higher *actual* retirement age, individual efforts to evade permanent benefit deductions by resorting to *disability pensions* were made unattractive, and access to them was rendered more difficult. *(b)* The core piece of the *PRA99* was the "demographic factor" by which, beginning in 1999, the hidden expansion of the scheme due to decreasing mortality rates at higher ages should be halted when lower benefits were stretched over a prolonged period of retirement. Further life expectancy at age 65 was integrated into the formula that determines the *initial benefit level* as well as the *annual adjustment*. Rising longevity assumed, the "demographic factor" would gradually lower the *net* standard pension level from nearly 70 to 64 percent (but not below).

Contrary to the expectations that after implementing the *PRA99* no further adjustments would be necessary until about 2010, the legislation of the *WBG* and *PRA99* already in 1996 and 1997 and the end of the "pension consensus" between the CDU/CSU and the SPD accompanying their passage demonstrate a changed, but not yet universally shared interpretation of aging and globalization issues. When the *PRA99* was read in the *Bundestag*, the spokeswomen of the Liberal Party, Gisela Babel, expressed the difference to the 1989 situation most clearly: 'At that time no discontent with a contribution rate to the pension scheme of 26 per cent or 28 per cent was discernible. That was flatly considered acceptable then. Today we do not consider it acceptable anymore' (Deutscher Bundestag 1997).

Including the effects of the *PRA99* now a contribution rate of 23.5 per cent in 2030 was estimated. It was substantially lower than the 36.4 per cent that had been projected *before* the *PRA92* became law (Sozialbeirat 1998, p. 242). Although the reforms enacted between 1989 and 1997 were clearly *parametric*, the moderation of the expected rise of the contribution rate by about 13 percentage points will inevitably leave grave "traces" in the future structure of benefits and the actual level of pensions — even if the lower figure is partly due to more funding out of general (and partly earmarked) revenues and to savings from making early retirement more costly for pensioners. The scheduled decrease of the target replacement ratio (from 70 to 64 per cent), a widely used indicator of benefit generosity, only partly displays the most serious consequences on the *level* and overall *distribution* of benefits. The cumulative effect is much larger and not immediately visible. It mainly stems from a strengthened insurance principle (Prognos 1999). The full impact hinges upon future pensioners' improved or diminished chances to realize a standard employment career and thus to earn credits sufficient for attaining the (lower) target replacement ratio. If ongoing changes in the labor market indeed diminish these chances it is most decisive for the individual pensioner whether those developments are compensated for by corresponding adaptations of the entitlement rules or are aggravated when exactly those provisions aiming at social adequacy of benefits are removed.[7]

For these reasons it is clear that stabilizing the contribution rate *and* status maintenance increasingly become contradictory goals. Albeit the latter goal had not been officially abandoned by the Christian-Liberal government and thus the 'basic model' of 1957 remained unchanged (Döring 2000, p. 180), it is obvious that after this series of reforms in future fewer employees can expect a factual wage replacement well above the social assistance level. This is exactly what the term 'creeping disentitlement' (van Kersbergen 2000, pp. 28-9) means when several incremental adjustments are evaluated according to their cumulative impact — namely, a *tacit system shift* in the long run (Hinrichs and Kangas 2003). To the majority of insured a number of single changes were intangible, and in particular the combined impact for oneself remained obscure. Therefore, these non-transparent adjustments failed to produce the effect the government had hoped for: in future lower pensions were not regarded as "more secure", and lost confidence in the reliability of the public pension scheme could not be regained. Additionally — and not the least as a result of a transnational discourse diffusion — a new interpretative frame emerged when social insurances were no longer regarded as a solution to workers' typical risks, but rather as a central *problem* for international competitiveness and employment growth. It linked to amplified fears of indeed unprecedented population aging and, for the first time, notions of *intergenerational equity* emerged as an imperative. As a result of the failure to reestablish confidence and of changes in the cognitive map of political actors, at the end of the 1990s the German pension system arrived at a "critical juncture" when a learning process was triggered which finally led (in 2001) to a "path dynamics" that is tantamount to a *paradigm shift*.[8]

3. From public pension reform to retirement income policy: the "Riester-Reform" of 2001

During the 1998 election campaign the Social Democrats created difficulties for themselves

[7] Shifting risk constellations that lead to an effective decline in protection are more frequent and longer spells of unemployment within the career of younger cohorts when no or reduced pension credits are earned (Kortmann and Schatz 2000, pp. 160-3) or result from rising earnings inequality. For example, more all-year-round full-time employees earn precarious wages (below 75 per cent of the average) and have less chances to obtain sufficient pension benefits (Schäfer 2003).

[8] On "path dynamics" see Goul Andersen (2001) who refers to March and Olsen's "policy martingales".

when they announced to revoke the "demographic factor" which had been denounced as a "pension cut" before. After coming into office these difficulties were enlarged when the Red-Green government actually kept that promise.[9] In addition, the government got under time pressure because it merely *suspended* this element of the *PRA99* as well as the impairments for future disability pensioners until end of the year 2000.

The first draft of reform proposals was presented in June 1999, and it was not earlier than May 2001 when the *Bundesrat* passed final pieces of the reform package (hereafter: *PRA2001*). This lengthy process was due to numerous and sometimes very detailed changes in response to objections from various actors as well as to attempts to revive the inter-party "pension consensus" that had lasted until the mid-1990s.[10] Parallel to the reform project *PRA2001* the government enacted several changes concerning the public pension scheme: it introduced a gradually increasing energy tax (*Ökosteuer*). The revenues are earmarked as a supplementary federal grant to the public pension scheme in order to further cover non-contributory benefits and to facilitate a lower contribution rate.[11] Furthermore, pension credits on behalf of recipients of unemployment assistance were reduced. Instead of wage indexing, pensions were arbitrarily adjusted according to consumer prices only in 2000, and in 2001 a moderated version (compared to the *PRA99* provisions) of disability pension reform went into effect. Three innovations included in the *PRA2001* (see *Figure 1*) justify to speak of a *paradigmatic change* (see also Michaelis and Thiede 2000) towards a retirement income policy that has happened and which supersedes the institutionally confined public pension policy.

[9] The influence of the pension and health care issue on the election result cannot be ascertained exactly. However, exit polls show that the SPD gained disproportionately among voters of retirement age (60 years and older) or approaching retirement (between 45 and 59 years of age) which in turn are the age groups where the decline for the CDU/CSU was largest. In particular, elderly women, traditionally its most loyal followers, turned away from the CDU/CSU. Moreover, there is a further indicator demonstrating the salience of the pension issue at the 1998 federal elections: compared to other themes it ranked high among the electorate, and the Social Democrats were believed of being capable of "securing pensions" much more frequently than the Christian Democrats (Emmert et al. 2001).

[10] Lamping and Rüb (2001, pp. 20-1) accurately speak of 'experimental law-making' to characterize the mode how the government pushed ahead the reform process. For a chronology of the course of events see Dünn and Fasshauer 2001.

[11] It is questionable whether at all in a *social* insurance scheme there can be (non-contributory) benefits which indeed would be "alien" to a *private* insurance. However, it can be considered a substantial shift when in the basically *contribution*-financed pension scheme nowadays about *39 per cent* of its expenditure stem from tax revenues which are transferred to cover certain benefit components (not based on individual contributions) and other expenses (Sachverständigenrat 2003, para. 333).

(a) Hitherto, like in many other pay-as-you-go, defined-benefit public pension schemes, in Germany the contribution rate functioned as the dependent variable of all parameter changes affecting revenues and expenditures, e.g. it was increased when the available funds fell below a certain contingency reserve. In future, this practice will be reversed because *upper limits* were fixed: the contribution rate *must not* exceed 20 per cent until 2020 and 22 per cent until 2030. In order to realize this transition to a "revenue-oriented expenditure policy", apart from funding a higher share out of general taxation, only savings on the benefit side remain as an option. A new benefit (adjustment) formula comprising a complicated "brake mechanism", replacing the suspended "demographic factor", was expected to deliver most of the required savings (Schmähl 2003). It should lead to roughly the same result in the long run, namely a standard replacement ratio of 64 per cent although, due to a redefinition of "net wage", the factual decline appears to be less large: the officially projected figure for 2030 is about 67 per cent. In case higher contribution rates than those mentioned before *or* a replacement ratio lower than 67 per cent come into reach, it is stipulated that the government has to take "appropriate" action. The expectation to actually live up to *both* targets was based on overly optimistic assumptions (about declining unemployment, demographic development etc.), and very soon it became foreseeable that if a conflict will arise such a trade-off would be decided in favor of containing the contribution rate at the expense of the pension level (see section 4.2.).

(b) Among the 18 traditional OECD member countries, so far, only Germany has had no special minimum protection scheme for the elderly. Persons without sufficient insurance claims were referred to the general social assistance scheme. At the beginning of this decade only about 1.3 per cent of retirement age people received those means-tested benefits. The new basic security scheme for old-age and disability pensioners is still means-tested, but the legal obligation of adult children to support their elderly parents is virtually lifted since 2003. The official justification for introducing this scheme was to increase the take-up rate, and that will indeed be the immediate consequence. In its explanation to the reform bill the government also admitted that changing (un-)employment careers may lead to more pensioners receiving benefits lower than the social assistance level (Bundesregierung 2000, p. 43).[12] Therefore, the major role of this "social assistance *de luxe*" for the elderly will make "new risks" in the labor market and the consequences of *past* and *future* pension

[12] After sorting out the pensioners, the bulk of social assistance recipients are people of employable age and their minor children. Therefore, the fusion of earnings-related, albeit means-tested unemployment assistance (which is financed by the federal government) and social assistance (as yet within the municipalities' responsibility) is eased. Corresponding measures have passed parliament in December 2003. It includes stronger work incentives and measures to better "activate" the largely overlapping clientele of the hitherto two schemes.

retrenchments socially more bearable when there is an increasing number of newly retired persons whose insurance entitlements prove to be insufficient.

(c) Core element of the *PRA2001* are incentives for a new type of *voluntary* private pension savings which is named after the then Minister of Social Affairs, Walter Riester (*Riester-Rente*). Although officially called *supplementary* provision for old age, this component of future retirement income is in fact meant to *compensate* for the declining target replacement ratio and to ensure income security: after the various measures taken in order to contain the contribution rate have created 'a "social protection gap"' it is now 'filled by private provision' (Bonoli et al. 2000, p. 46). When institutionalizing private pensions, the Red-Green government has not only made up for the "forgotten" compensation in the *PRA99* of its predecessor. Moreover, the extension towards *retirement income policy* has irrevocably converted the German pension system into a multi-pillar approach again after it had been tantamount to *public pension policy* and a one-pillar approach since 1957 (see section 2.1.). The *Riester-Rente* started in 2002. Contributions to certified savings plans, gradually increasing to 4 per cent of gross earnings in 2008, benefit from direct subsidies or tax privileges with a bias in favor of families raising children and high-income earners.

Different from the public pension scheme employers do not financially participate the *Riester-Rente* so that their compulsory contribution payments will be limited to 11 per cent of covered wages at maximum. Sparing employers from joint financing may be regarded as a further innovation. For the trade unions and the traditional Left it was of high symbolic value although economically it is irrelevant because employers' social security contributions always added to total wage costs, and increases were considered in subsequent wage bargaining. In any case, for those employees who voluntarily engage in supplementary provision their total contribution rate is higher than before. It is the inevitable consequence if one moves from a complete PAYG system to partial capital funding and represents the well-known "double payment problem" that goes along with it. Therefore, the shift away from the one-pillar approach will proceed very slowly. If employees save for the *Riester-Rente* as recommended and these savings were to yield a constant interest rate of 4 per cent, according to government estimations (Deutscher Bundestag 2001, p. 7), the personal pension accrual would amount to no more than 10.5 per cent of the combined pension benefits for a worker retiring in 2030. While the 1957 pension reform within the PAYG framework immediately produced a large improvement (see section 2.1.), as a result of asymmetrical reversibility, the full effect of this element of *PRA2001* evolves gradually.

So far, employees have not embraced the *Riester-Rente* enthusiastically. After 18 months the take-up rate has remained low (about 12 per cent - BMGS 2003; Dünn and

Fasshauer 2003).[13] One has to take into account, however, that there is also the option to benefit from corresponding tax privileges when it is provided as an occupational pension. Converting parts of the salary (up to 4 per cent right from the start in 2001) into savings to single-employer plans or those set up by industry-wide collective agreements can be advantageous due to cost efficiency,[14] and the individual employee has not to invest much in "financial literacy". Understandably, occupational pension coverage has mushroomed since 2001 (April 2001: 29 per cent; March 2003: 57 per cent – BMGS 2003) whereas it was comparatively low before and even on the decline for about 25 years. Moreover, outside the public sector, almost nowhere occupational pensions had been an element of collective bargaining until 2001. Within the new architecture of the German pension system, occupational pensions will change their character: up to now they were first of all an instrument of firms' human resource policy in order to recruit, motivate and tie personnel and thus *supplemented* (sufficient) first-pillar pensions. This function (and employers' financial responsibility) will fade in importance as against a new role, namely to become a genuine element of social policy, providing status maintenance for a substantially larger share of employees when public pension benefits alone do no longer perform that role.

Whether employees take out savings contracts for the *Riester-Rente* on their own or convert a part of their earnings into occupational pension plans, in any case, on a *voluntary* basis the take-up rate will remain incomplete. This will, in addition to the fact that these "defined-contribution type" pensions contain no redistributive elements, lead to enlarged economic inequality in old age because only employees who can afford to forego present consumption will additionally provide for retirement, and only those who actually do may take advantage of the tax privileges in addition to their own savings efforts (or when they divert savings correspondingly). Thus, mainly employees with medium and high wages will benefit from the transition towards the multi-pillar approach (Bulmahn 2003; Schmähl 2003). Another criticism relates to the legitimacy of contribution payments: compared to tax payments, social insurance contributions are usually less resisted because they "earn" benefits which in most cases exceed the social assistance level by a considerable margin. If selective curtailments and the declining replacement ratio result in public pensions below or close to what one would receive as means-tested basic security anyway, from the individual

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[13] One reason may be that employees systematically overestimate their public pension entitlement (Deutsches Institut für Altersvorsorge 1999). Furthermore, the majority of Germans is not very knowledgeable about individual pension planning, and the *Riester-Rente* is a completely new and, so far, a rather complicated product. Lack of trust in welfare markets may be another impediment (Taylor-Gooby 1999).

[14] This type of occupational pension resembles the "401(k) plans" in the United States (see e.g. Springstead and Wilson 2000).

perspective, contributions to the public pension scheme were paid for virtually nothing in return. Schmähl (2003), who is particularly concerned about the delegitimation of the contributory scheme, therefore favors a an index-linked increase in retirement age (that entitles to full benefits) instead of lowering benefits (see Schmähl and Viebrok 2000).

When considering the *PRA2001* as a clear *paradigm shift* three conclusions may be highlighted. First, its central parts cannot be simply interpreted in categories of "more" or "less". Rather, the term 'recalibration' (Pierson 2001, pp. 425-6) is appropriate. The new goals assigned to the different components of old-age security and the *new components* itself (the certified savings plans entitling to subsidies or tax privileges as well as the means-tested basic security scheme) will lead to a substantially changed public/private mix of retirement income — albeit not to an identical composition across income classes.

Second, the transition towards retirement income policy cannot be simply treated as equivalent to (partial) *privatization* or less state responsibility. Fiscal expenditure increases due to subsidies covering non-contributory benefit components within the public pension scheme. Furthermore, a growing number of elderly will claim benefits from the means-tested basic security scheme, and tax expenditures to induce voluntary savings efforts for the *Riester-Rente* are on the increase. At the same time efforts to (re-)regulate the non-public components of the income mix (personal pensions, occupational pensions) have to be intensified since they are no longer supplementing actually sufficient public benefits, but rather compensate for exactly the loss of their status maintaining function.

Finally, the institutional dynamics has brought new actors, themes, conflicts and modes of conflict resolution into play which, as yet, have not fully consolidated (Hinrichs 2000b; Nullmeier 2001). For example, in the *new politics* of retirement income policy those actors have gained a stake who occupied a more or less marginal position so far, as there are the various branches of the financial service industry offering the certified defined-contribution schemes, the Ministry of Finance which is involved with considerably more tax money than before, authorities regulating the emerging "welfare market" and its products, organizations protecting consumers' interests, and the social partners in a new role as they enter collective agreements on occupational pensions. Moreover, it is foreseeable that after the interpretative hegemony of the "old" pension policy network, rallying behind the pay-as-you-go public pension scheme and its established principles, has gone the new retirement income policy will take place in different, partly parallel arenas with possibly more conflictuous relationships among each other and within.

4. After the paradigm shift

4.1. How could it happen?

Bridging long time spans is a central feature of all pension systems (see section 1.). An *immediate* and *substantial* reduction of public pension expenditures is thus most unlikely. Changes of pension programs aiming at such goal usually comprise "grandfather clauses" or provisions that cut back on entitlements are phased in. Consequently, the pension reforms enacted between 1989 and 1997 *largely* spared current pensioners and employees close to retirement age — not the least because they represent a significant group within the electorate. The *PRA2001* factually implied no curtailments over and above the *PRA99*, but merely lower increments which are perceived differently than direct cuts (although present and future pensioners' benefits are partly decoupled from net wage development during their retirement). Moreover, by introducing the *Riester-Rente* the government went beyond a *synchronous* redistribution between covered employees and pensioners and the consequences arising from their shifting numerical ratio. Thereby, it enabled current employees to take an intertemporal (or: *diachronic*) perspective, i.e. to pursue an "investment strategy" which demands to (additionally) sacrifice consumption now for not being worse off (than the present generation of pensioners) later when a declining replacement ratio of public pensions is offset by a parallel increase of the *Riester-Rente* (see also Jacobs 2002).

In order to understand why it mainly were the Social Democrats who realized this "investment strategy" one has to recall the problem they faced after returning to office: successful social policy institutions perform a socializing function when by way of their lasting and well-known operation they create their own basis of support — a *culture of solidarity* as a fundament (Hinrichs 2002). These formative effects largely preclude positive answers to questions of how *could* or *should* it be different and foster expectations of stability and continuity. Today, the existence of the public pension scheme for more than hundred years no longer generates confidence automatically, and the working of the generational compact in the past is no guarantee for the continuance of rules and levels in future. Official assertions that there is no reason to be afraid of challenges lying ahead contrast with questions by the (younger) insured *how* it will go on.[15] After recurrent policy adjustments and still uncertain prospects regarding security in old age, at the end of the 1990s, one was not simply 'running out of options', as Lamping and Rüb (2001, p. 16) argue, but rather, public pension policy had lost its *credibility* and the institution as such had used up *plausibility*. Parametric reforms of the public pension scheme have not come to an end yet and will

[15] The long-standing Minister of Social Affairs, Norbert Blüm (1982 to 1998), again and again maintained that public pensions are secure ("*Die Rente ist sicher!*"). Increasingly, the public cynically interpreted this message as a joke.

continue in order to attain defined upper limits of the contribution rate (see section 4.2.). However, merely confining oneself to again turning those well-known "adjustment screws" and afterwards declaring "less" as more "secure" would have been absolutely pointless for restoring confidence. On the contrary, it had again betrayed expectations of reliability. Insofar, the situation in Germany was similar to that in Sweden where only a fundamental reform was suitable for reconstituting credibility (Scherman 1999, pp. 44-7). Instead of asking higher contributions to a *collective* security scheme from the insured[16], they were given the opportunity to put subsidized savings into pension plans which offer true *property rights* and *freedom of choice*. Moreover, the government pointed out that public pensions plus *Riester-Rente* were going to amount to an *higher* retirement income level than at present (Deutscher Bundestag 2001, p. 7). In this way a strategy of "blame avoidance" was combined with the one of "credit claiming" (Weaver 1986; Pierson 1994, pp. 13-26).[17]

Opting for *individualistic* solutions to securing a sufficient level of pensions in view of *individualization* as a societal "mega-trend" clearly matched the credo of a modernized ("New") Social Democracy that places self-responsibility and efficiency on an equal footing with (inter-generational) solidarity and social justice (see e.g. Clasen 2002). Out of numerous similar quotations from leading Social Democrats in Germany only one may suffice to prove the frame shift that occurred. Gabriele Behler (1999, p. 85), a former Minister in North Rhine-Westphalia, asked the population to say farewell to the desire for a welfare state which in a paternalistic way takes away individual responsibility for providing against risks.

The attempt to gain *reputation* by making up for the "forgotten" compensation of the preceding government and pushing the transition to the multi-pillar approach nonetheless implied that the Social Democrats (much more than their coalition partner, the Green Party) got involved in a very risky enterprise. This was so because important criteria for a smooth implementation of loss-imposing changes were not met. In order to ensure acquiescence and to minimize the threat of electoral retribution, in discoursive manner, any government should

[16] That is exactly the "Achilles heel" of a pay-as-you-go pension scheme as was pointed out by Martin Feldstein (1975, p. 78): 'future tax rates can be set so that tax revenues are sufficient to meet the claims of the beneficiaries … *as long as the voters support the social security system*' (italics in original).

[17] The only benefit improvements included in the *PRA2001* again concerns persons who raised children (see *Figure 1*). That development started in 1986 and, subsequently, it was strongly pushed by several rulings of the Federal Constitutional Court demanding to compensate families raising (or having raised) children for the positive externalities they produce. Due to its far-reaching rights to actually *stipulate* concrete legislative action, the Court has become a major actor in this policy domain when it comes to family-related benefits like child care credits. By another judgement in 2002 regarding the taxation of (public) pension benefits the Court has again obliged the legislator to take action (see section 4.2.).

bring home to the public that the reform is *small*, *necessary*, burdens are *fairly distributed*, can be regarded as a *coherent redesign* of the policy which was *broadly consented* (Hinrichs 2000b; Schmidt 2002). Concretely, the immediate impact of the reform package was indeed *small*, but inevitably growing over time. In addition, there were the phasing-in effects of all reforms prior to the *PRA2001*. When the *PRA99* was at stake the Social Democrats had outright denied its *necessity*, but proclaimed own reform plans as indispensable after the federal elections of 1998. It remained contested whether the overall burdens of the *PRA2001* were distributed in a *socially fair* manner and therefore satisfied established values of social policy. Much emphasis was put on convincing the public that the reform meant a *coherent redesign* of the pension system in response to well-known challenges, ensuring sustainability *and* sufficient retirement income. However, the corresponding attempts have not proved very successful (Bulmahn 2003; Leinert 2003). In any case, the *PRA2001* was not broadly *consented* among the relevant political actors.

In view of the credibility problem and own ambitions to modernization ("strengthening self-responsibility"), the government — and that was much more the Federal Chancellery than the Ministry of Social Affairs that had been most decisive in the process of all former reforms — proved extremely capable of learning when it integrated initially vague reform conceptions and a conflicting paradigm. Although one should always be cautious towards conspiracy theories, but it can hardly be avoided to concede that the financial services industry (assisted by economists advocating of "pension funding" and who had not conquered a voice in the pension policy arena until the 1990s) has successfully contributed to the destruction of confidence in the public pension scheme and, moreover, exerted substantial influence on the reform discourse. Following Peter Hall (1993, p. 290), it shows the power of interest groups to change interpretative frames. Inasmuch as the social (re-)construction of a *policy* problem and the responses it suggests was successful, the established policy network lost ground and was no longer capable of unassailably defining the problem and a solution that would match traditional goals of public pension policy.[18]

The Left among the Social Democrats ("traditionalists") could hardly be convinced to abandon the quasi-monopoly of the public pension scheme and, likewise, the trade unions

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[18] An indicator of the approaching change of course was that Walter Riester, deputy president of the Metal Union and renowned as a "modernizer", was appointed Minister of Social Affairs instead of Rudolf Dreßler, a dyed-in-the-wool protagonist of the social insurance approach and experienced social policy spokesman of the Social Democrats in the *Bundestag*. The intention of the government to execute the transition towards retirement income policy became also obvious when in 2000 the long-standing chairperson of the advisory council (*Sozialbeirat*), Winfried Schmähl, was not reappointed, but rather replaced with the more "flexible" multi-purpose advisor Bert Rürup, also a Professor of Public Finance.

only reluctantly accepted the *PRA2001*. Eventually, they were appeased by the stipulation that the replacement ratio must not fall below the 67 per cent level (see above). The special (tax) privilege of occupational pensions also accommodated their interests since it benefits the unions' core membership and opened up an attractive terrain for collective agreements on pension funds (and for participating in their administration then). Finally, it is hard to prove whether there was a tacit deal, trading compliance with the *PRA2001* for an extension of works councils' rights that was firmly demanded by the trade unions and actually legislated later in 2001.

Until the end of the parliamentary process the government attempted to win over the Christian Democrats for a consensus. In principle, the party supported the system shift, but continuously caviled at the concrete form. Eventually, it shied away from thwarting the *Riester-Rente* in the *Bundesrat* which had to agree on this element of the *PRA2001*. Utilizing their majority in the *Bundesrat* would have meant that the CDU/CSU had denied future pensioners attractive opportunities to attain a higher retirement income. Despite considerable concessions to the CDU/CSU (particularly on family-related benefits) it refused an overall compromise with the government. One reason may be the lasting disgruntlement about the SPD's successful strategy to blame the Kohl government for the "pension cuts" during the 1998 election campaign. More important was that the Christian Democrats were very much on the defensive after a financial scandal (about "soft money" and other unlawful deeds) was uncovered in November 1999. In such a situation it was hardly opportune to simply give away a potentially mobilizing theme for the next election campaign by striking an agreement with the political opponent. Thus, the government learned that in order to reach a compromise it needed a strong negotiating party on the other side of the table.

Paradigm shift in a policy area does not imply that basic programmatic structures are completely thrown out. Central elements of the German pension scheme, like employment-relatedness or contribution financing, are maintained ever since 1889 as it is also true for countries that realized an alternative starting point (based on citizenship) for their pension system. Nor is it required that, in order to claim a paradigm shift, all political actors involved have already adopted the new interpretative frame in full. Finally, such a claim may be made even if the impact of the corresponding policy changes has not yet fully materialized. Substantiating the path departure as being irreversible would suffice, and such further drifting away from the one-pillar approach will be shown next.

4.2. How will it go on?

Contrary to expectations in 2001, the contribution rate had to be increased to 19.5 per cent in

2003, and a rise to 20.4 per cent already in 2004 would have been inevitable without "emergency" measures. Such development was caused by a declining employment level and was partly self-inflicted due to reduced fictitious contributions on behalf of unemployment assistance recipients and revenue losses as a growing number of workers converted parts of their earnings into occupational pension plans (see also Schmähl 2003). Moreover, the long-run targets fixed in the *PRA2001* are in jeopardy as well: projections included in the report of the so called *Rürup-Kommission* (Kommission 2003, p. 101) arrive at a rate of 21.5 percent in 2020 and of 24.2 per cent in 2030. They are based on less optimistic assumptions than the government employed in its calculations when the *PRA2001* was prepared. The commission's central proposals to nonetheless achieve the 20/22 per cent target are *(a)* gradually increasing the age at which "full benefits" can be claimed from 65 to 67 (starting in 2011) and *(b)* including a "sustainability factor" in the benefit (adjustment) formula. By this factor the changing *worker/pensioner ratio* will determine the replacement rate of newly and already retired persons (whereas the "demographic factor" of the *PRA99* took into account further life expectancy at age 65). A variable factor will adjust the weight of this standardized dependency ratio so that "sustainability" is ensured, the 20/22 per cent target is always met.

In view of the unpleasant prospects in the short as well as long run, the government disregarded the doctrine to reform the pension system only occasionally. In 2003 it came forward with two reform packages and a third one that will translate the Constitutional Court's demand for equal tax treatment of all retirement income recipients. The "emergency" package that will ensure a contribution rate at the 2003 level has already passed parliament. It includes a suspension of benefit adjustment in 2004, and the pension scheme will no longer pay the "quasi-employers' share" of contributions to the long-term care insurance, so that pensioners have to bear the full rate (1.7 per cent). Beside this understandably unpopular benefit cut there will be a further (temporary) reduction of the scheme's contingency reserve and some minor changes.

In its second reform package the government has adopted all proposals of the *Rürup-Kommission* with the only exception that the decision on whether to raise retirement age will be postponed until 2008 when the labor market situation might have improved. Moreover, the reform bill provides for a complete abolition of non-contributory pension credits for periods spent in school or university education (and which had been reduced to a maximum of three years already).

In 2002, the Constitutional Court has again (see above, **n. 17**) proved to be a powerful veto-player in German pension politics when it ruled the unequal treatment of civil servants (whose pensions are fully taxable) and beneficiaries of the public pension scheme unconstitutional. Hitherto, white and blue-collar workers pay contributions largely out of post-tax income, and the accruing benefit is regularly tax-free if the retiree has no substantial income (like occupational pensions) in addition. Beside provisions that will simplify the *Riester-Rente* the third reform package aims at realizing the "EET principle", i.e. up to a certain limit contributions to public as well as private pension plans are *exempted* from taxation as are the funds' earnings (capital income), but benefits paid are liable to income *taxation*. Due to the tax revenue losses it implies (and which can only be recouped later) such a transition has to occur gradually and therefore will last from 2005 until 2040.

The government argues that the increasing tax relief will enlarge the scope for additional pension savings (but obviously most for employees with higher earnings). Those savings become all the more necessary since the "sustainability factor" will aggravate the decrease of the benefit level. While the *Riester-Rente* more or less filled the "social protection gap" that had arisen (see above), it is created again when the *gross* replacement ratio[19] for the standard pensioner will decline from presently 48 to 40 per cent in 2030 (Kommission 2003, p. 107), i.e. by one sixth (if she does not earn extra pension credits by working beyond age 65). It has been estimated (Schnabel 2003, p. 13) that an average employee who is going to retire in 2030 should have started already in 2000 to save 7 per cent of her income in order to end up with the same disposable income as present cohorts of pensioners. These figures point to a problem of savings incentives for voluntary (tax-privileged) pension plans (Disney 2000): if the emerging income security gap appears to be small no such savings are deemed necessary. In contrast, if the gap is large individual efforts are likewise discouraged because, in view of one's disposable income, it seems hopeless (or no longer worthwhile) to strive for adequate retirement income. In view of the standard replacement ratio having lost a "ratchet", even the Council of Economic Advisers, ideologically most committed to market liberalism, is concerned about incalculable public pensions and the legitimacy of the contributory scheme (Sachverständigenrat 2003, para. 346, 348 and 353).

Have these reform plans caused conflicts among relevant political actors? Obviously, there is less resistance than when the *PRA2001* was at stake because the dominance of political parties has been strengthened, particularly as against organized labor. The Christian Democrats have appointed their own commission chaired by the former Federal President Roman Herzog (Christlich Demokratische Union 2003). Its proposals *largely* overlap with the government's plan and also include an identical "sustainability factor" (BMGS 2003). It remains to be seen whether there will be a return to an inter-party "pension consensus" this time. However, apart from the largely "technical" taxation package, the government is not dependent on an approval of the *Bundesrat*. The trade unions which had forced the government to moderate the *PRA2001* are in a weak position after the Metal Union, the usual

[19] Due to the change in taxing pension benefits, *net* figures (see **n. 4**) can no more be applied.

spearhead, has lost a labor dispute on working hours reduction in East Germany in May 2003 and, moreover, the trade unions were unable to massively mobilize against the *Agenda 2001*, a comprehensive program for a far-reaching overhaul of the German welfare state and of which the current pension reform is an element. Likewise, the Left among the Social Democrats fought in vain against the *Agenda 2010*. At an extra party congress convened at their initiative in June 2003 they were clearly defeated. Therefore, in December 2003 it seems most likely that the second and third package of the current reform will pass without major changes whereas it is hardly foreseeable how the electorate will respond to the retrenchments which are not confined to pensions, but effect other areas of social policy as well.

5. Conclusion: pensions still frozen?

In comparative welfare state research explaining obvious institutional resilience against varied pressures and path-dependent development as dominant pattern have become central topics. Since Pierson's (1994) seminal work institutionalist approaches prevail, not the least, because quantitative methods are hardly capable of proving or disproving notions of a '"frozen" welfare state landscape' argument (Esping-Andersen 1996, p. 24). Predominantly, case studies on single welfare states or cross-country comparisons of certain programs are suitable to show whether there are changes 'beyond incrementalism' (Wiesenthal 2003) and, if so, why. In view of major reforms that occurred at accelerating speed during the 1990s and when welfare states became increasingly "defrosted" (Palier 2000), discontent with deterministic notions of almost static institutions has engendered concepts of large, path-breaking changes or "path creation" and how they came about (Crouch and Farrell 2002). Starting from the premise that "history matters", institutionalist approaches are not necessarily tied to a strict path dependence theorem although they can more easily explain immobility and inertia than fundamental policy changes. If the latter are not *a priori* denied, "critical junctures" are important when during periods of reorientation different routes are conceivable and the course for future development is set.

At the end of the 1990s, Germany's public pension policy had reached such a "critical juncture". Despite the difficulties to define and, subsequently, to measure whether a policy change is incremental or paradigmatic, particularly in the pension area (Hinrichs 2000a; Hinrichs and Kangas 2003), clearly a change of the latter type happened in 2001 and that will be reinforced in 2003/4. It has been demonstrated that a once 'coherent policy paradigm' (Hall 1993, p. 290) concentrating on truly earnings-replacing public pensions has been shaken and was replaced with a "multi-pillar approach". The current reform legislation will further enforce this transition as the 'hard budget line', following from the shift towards a 'fixed contribution rate' principle has maintained absolute priority. It supersedes the alternative of a 'fixed relative position' (Myles 2002, pp. 140-5), the core of the *PRA92*, when the financial consequences of aging should be shared between pensioners (constant ratio of net earnings), the insured (somewhat higher contributions) and the state (increased subsidies out of general revenues).

Nevertheless, it is remarkable that the paradigmatic shift from public pension policy towards retirement income policy occurred within a short period of time and concerned a policy domain prototypical for path-dependent development (Pierson 1994; Haverland 2001). Theoretically assumed "lock-in effects" of a mature pay-as-you-go scheme obviously dissolve with accelerating speed and contradict notions of a most immovable object. It is furthermore astonishing that the break with institutional inheritance happened in a country which is characterized by lacking power concentration and numerous veto-players. Finally, one would hardly expect that it was exactly a Social Democratic party departing from an established welfare state consensus and the routine of incremental adjustments as a technology of securing social policy institutions and instead realizing an almost bottomless decline of benefit levels and self-responsibility as a dogma.

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Table 1: **Population (Structure) in Germany: Development 1900—2000 and Projections 2010—2050 (Variant 5)**

Year	Population in million **(1)**	< 20 yrs. in percent **(2)**	≥ 60 yrs. in percent **(3)**	old-age dependency ratio[1)] **(4)**	total dependency ratio[2)] **(5)**
1900	56.4	44.2	7.8	16.3	108.5
1910	64.9	43.7	7.9	16.3	106.7
1939	69.3	32.0	12.3	22.0	79.6
1950	69.3	30.8	14.0	26.8	83.3
1961	73.7	28.1	17.8	33.0	84.9
1970	78.1	30.0	19.9	39.8	99.7
1980	78.4	26.8	19.4	35.9	85.6
1990	79.1	21.8	20.3	35.1	72.8
2001	82.4	20.9	24.1	43.9	81.9
2010	83.1	18.7	25.6	46.0	79.5
2020	82.8	17.6	29.2	54.8	87.7
2030	81.2	17.1	34.4	70.9	106.2
2040	78.5	16.4	35.2	72.8	106.6
2050	75.1	16.1	36.7	77.8	112.0

[1)] elderly ratio = (population ≥60 × 100) **:** population 20 to <60
[2)] total dependency ratio = [(population <20 + ≥60) × 100] **:** population 20 to <60

Sources: BMFS 1993: 257; Statistisches Bundesamt 2003: 42

Table 2: **Social Expenditure and Public Pension Financing in Germany**

Year	Social Expenditure in Percent of GDP **(1)**	Combined Contribution Rate to Social Insurance Schemes **(2)**	Public Pension Expenditure in Percent of GDP **(3)**	Net Standard Pension in 1995 EURO/*in % of Real Net Average Earnings* **(4)**	Contribution Rate to the Public Pension Scheme (*Earnings Ceiling in % of Gross Average Earnings*) **(5)**
1957		21.6			14.0 (*178.5*)
1960	21.1	22.4	6.4	5,517/*66.8*	14.0 (*167.2*)
1970	25.1	26.5	7.7	8,398/*65.0*	17.0 (*161.9*)
1975	31.6	30.5	9.8	9,995/*66.8*	18.0 (*154.1*)
1980	30.6	32.4	9.6	11,527/*71.1*	18.0 (*170.9*)
1985	30.0	35.1	9.5	11,171/*72.4*	19.0 (*183.6*)
1990	27.8	35.8	8.8	11,849/*68.0*	18,7 (*180.2*)
1991	28.4	36.7	8.9	11,902/*67.8*	17.7 (*175.6*)
1995	31.2	39.3	10.3	11,822/*69.9*	18.6 (*184.7*)
1996	32.1	40.8	10.5	11,733/*70.1*	19.2 (*185.8*)
1997	31.6	41.8	10.5	11,594/*71.0*	20.3 (*188.7*)
1998	31.5	42.1	10.6	11,552/*70.1*	20.3 (*190.5*)
1999	31.9	41.2	10.6	11,619/*69.9*	19.5 (*190.6*)
2000	31.9	41.0	10.7	11,537/*69.1*	19.3 (*190.2*)
2001	32.1	40.8	10.9	11,375/*67.7*	19.1 (*190.9*)
2002		41.3		11,440/*68.4*	19.1 (*189.4*)
2003		42.1			19.5 (*209.4*)

Sources: **(1)** = BMAS 2002: 19 and 22 [figures not comparable to OECD calculations; figures 1991 and after relate to united Germany]; **(2)** = VDR 2003: 243; **(3)** = BMAS 2002: 35 and 38; **(4)** = VDR 2003: 240 [for the definition of "standard pension" see **n. 4**; all figures relate to West Germany]; **(5)** = VDR 2003: 239 and 245 [1992 and after: contribution assessment ceiling valid in West Germany].

Figure 1: **Central Elements of Pension Reform Acts Legislated in Germany between 1989 and 2001**

Pension Reform Act 1992 (PRA92) – legislated: 1989; effective: 1992 + subsequently
- benefit adjustment according to preceding year's *net* wage development
- federal subsidies increased to 20% of the scheme's annual expenditure (permanently)
- all provisions to retire before age 65 without benefit reduction phased out in 2012 (exception: seriously handicapped workers); permanent deduction: 0.3% per month
- credits for periods of schooling and tertiary education reduced: from max. 13 yrs. to 7 yrs. at max. 75% of average wages
- 4 instead of 5 first yrs. of covered employment revalued at 90% of average wages
- child-care credits for births after 1991 increased from 1 to 3 yrs. at 75% of average wage)

Growth and Employment Promotion Act 1996 (WBG) – legislated: 1996; effective: 1997 + subsequently
- phasing out of first benefit receipt without permanent deduction before age 65 accelerated (completion: December 2004 instead of December 2012)
- credits for periods of schooling and tertiary education after age 17 reduced: from max. 7 yrs. to 3 yrs.
- 3 instead of 4 first yrs. of covered employment revalued at max. 75% of average wages (formerly: 90%)
- no credits for periods of unemployment and sickness if no benefits from respective social insurance scheme; credits reduced for recipients of unemployment assistance

Pension Reform Act 1999 (PRA99) – legislated: 1997; effectiveness *scheduled* for 1999 and subsequently
- retirement age for seriously handicapped persons lifted from 60 to 63 yrs. (benefits deducted if claimed between 60 and 63 yrs. of age)
- benefit calculation of disability pensions changed to the disadvantage of claimant and requirements for claiming disability pensions as such strengthened
- increase of life expectancy at age 65 taken into account when calculating initial benefit and adjusting current pensions ("demographic factor")
- credits from simultaneous covered employment can be added to child-care credits whose value is increased from 75 to 100% of average wages

Pension Reform Act 2001 (PRA2001) – legislated: 2001; effective 2002 and later
- benefit adjustment formula incorporates changes of the contribution rate to public pension scheme and to certified private pensions (effect: decreasing replacement ratio)
- survivors' pensions: more comprehensive income test; supplements for children born
- revaluation of low earnings for parents when child is between 3 and 10 yrs. or additional credits if non-employed while raising 2 or more children below age 10
- special, tax-financed means-tested basic security scheme for old-age and disability pensioners without reverting to children's income support
- tax-subsidized contribution to certified supplementary provision (starting in 2002, gradually increasing to 4% of maximally covered earnings in 2008)
- political action triggered if foreseeable that contribution rate will exceed 20% before 2020 or 22% before 2030 or target replacement ratio falls below 67%