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## On the marriage of flexibility and security: Lessons from the Hartz-reforms in Germany

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**On the Marriage of Flexibility and Security:  
Lessons from the Hartz-reforms  
in Germany**

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## **ABSTRACT**

In the context of the ongoing reforms on European labour markets the keyword 'flexicurity' is presently gaining prominence. We therefore want to explore the importance of the flexicurity-concept on the example of the German Hartz-reforms. Starting from the frequently used definition as a trade-off between employers' demands for flexibility and employees' needs for security, different conceptualisations of flexicurity are considered, and criteria for an efficient and equitable flexicurity-nexus are developed. The German debate on flexicurity is briefly looked at. The main part of the paper is devoted to analysing four policy measures which were implemented within the Hartz-reforms: 'Ich-AG' allowance for newly founded businesses, 'personnel service agencies' ('PSA') to place unemployed into regular employment, 'Mini-Jobs' and the introduction of 'Midi-Jobs' which were supposed to serve as stepping stones into employment subject to social insurance contributions and 'wage insurance' for elderly workers. It is assessed whether the measures contribute to enhancing the components of flexibility and security and whether the measures are appropriately balanced. The analysis reveals that the measures' quality could be improved by strengthening different components of the security dimension.

## **ZUSAMMENFASSUNG**

Das Schlagwort „Flexicurity“ gewinnt im Rahmen der aktuellen Reformen auf den europäischen Arbeitsmärkten an Bedeutung. Die Tragweite des Flexicurity-Konzepts soll hier am Beispiel der Hartz-Reformen in Deutschland untersucht werden. Ausgehend von der Definition als Zielkonflikt zwischen dem Bedürfnis der Arbeitgeber nach Flexibilität und dem Bedürfnis der Arbeitnehmer nach Sicherheit werden weitere Konzeptualisierungen des Terms erörtert. Darauf aufbauend werden Kriterien für einen sowohl effizienten als auch gerechten Flexicurity-Nexus entwickelt. Nach einem kurzen Überblick über den Verlauf der Flexicurity-Debatte in Deutschland werden vier Instrumente, die im Rahmen der Hartz-Gesetzgebung eingeführt wurden, vorgestellt: Die „Ich-AG“-Unterstützung für den Übergang in die Selbständigkeit, die „Personal Service Agenturen“ (PSA) für die Vermittlung ehemals Arbeitsloser in reguläre Beschäftigungsverhältnisse, „Mini-Jobs“ und die Einführung von „Midi-Jobs“, intendiert als Brücke in sozialversicherungspflichtige Beschäftigung, sowie die „Entgeltsicherung für ältere Arbeitnehmer“. An Hand der im Theorieteil entwickelten Kriterien wird gefragt, inwieweit die einzelnen Komponenten von Flexibilität und Sicherheit gestärkt werden und inwieweit die Maßnahmen ausgewogen sind. Die Analyse zeigt dabei auf, dass die Qualität der Maßnahmen durch die Stärkung unterschiedlicher Komponenten der Sicherheitsdimension gesteigert werden könnte.



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## 1. Introduction<sup>1</sup>

‘There is no more paradox in this [*in intellectual property protection – the authors*] than there is in saying that motorcars are travelling faster than they otherwise would *because* they are provided with brakes.’  
(Schumpeter 1976: 88)

The argument we would like to bring forward is captured in Schumpeter’s famous quotation, which can be reformulated in the following way: ‘There is no more paradox in ‘flexicurity’ than there is in saying that workers are more flexible and creative than they otherwise would *because* they are provided with securities.’

This paradoxical marriage of flexibility and security has been strongly promoted by the European Employment Taskforce headed by Wim Kok, which published its report ‘*Jobs, Jobs, Jobs. Creating More Employment in Europe*’ in November 2003. The title of this report was contested – and in some countries even badly accepted – for many people in Germany, for example, the term ‘job’ carries the connotation of non-standard low quality employment. However, within the report, security is clearly regarded as a prerequisite for the acceptance of flexibility, albeit in a new sense.

First, job security as a matter of preserving a job for life is abandoned. In return, employability, security, and decent pay as well as good working conditions are emphasised. Second, individualised assistance in finding a job and transferable social rights to foster mobility are brought up. Third, people should be encouraged to take risks (compare also Schmid 2006). Social security institutions, especially pension systems, should therefore be designed in such a way that they reward instead of punish people for taking up flexible jobs. Denmark and the Netherlands are reported as good practice cases. However, both countries follow quite different concepts of *flexicurity*: Denmark combines low employment protection with generous unemployment benefits, the Netherlands, on the other hand, combine high employment protection with high variability of employment contracts. The message the Employment Taskforce wanted to bring forward was that the EU-Member States should be encouraged to develop their own strategy to reconcile flexibility and security.

How has Germany responded to this challenge of finding its own ideal flexibility-security nexus? This paper will try to answer this question in four steps: First, definitions and criteria for a successful ‘marriage’ between flexibility and security will be developed, followed, second, by a brief overview of the German debate on *flexicurity*. In the third and main section, we assess the experiences with some

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1 We are grateful to Silke Gülker and Petra Kaps for comments on an earlier version.

specific German *flexicurity* measures introduced through the Hartz-reforms. We conclude by drawing some lessons from these experiences for the European Employment Strategy.

## 2. Flexibility and security: definitions and criteria

According to Tangian (2005) the flexibility-security nexus can be regarded from two different perspectives: First, as a trade-off to be optimized between social partners, and second as a kind of social insurance for the flexibly employed. Whereas the first perspective is predominant in the present debate, we will also strongly emphasise the second perspective.

Wilthagen and Tros (2004) suggest analysing *flexicurity* policies as trade-offs. They propose a trade-off matrix that contrasts four forms of flexibility and four types of security. Flexibility that mainly caters to employers' demands can take the form of external numerical, internal numerical, functional flexibility and variable pay. Security, in this trade-off matrix, is subdivided into job security, employment security/employability security, income security and combination security. Whereas the first three types of security are to be expanded to satisfy the needs of labour market outsiders or atypically employed, combination security adds the possibility to combine paid work with private responsibilities (Wilthagen et al. 2003).

For the sake of terminological consistency, we slightly modify this typology by subdividing 'functional flexibility' into 'internal' and 'external functional flexibility'. On the pay level, internal functional flexibility is thought of as going hand in hand with result oriented or 'variable pay' whereas on the macro level external functional flexibility is supposed to generally enhance wage flexibility. On the security side, we slightly change the terminology by coining 'combination security' as 'option security' in order to give this security aspect a broader meaning.

From an employers' point of view, four types of flexibility can therefore be distinguished:

- *External numerical flexibility* to hire and fire, or to use temporary layoff, fixed-term contracts, temp-agency work, casual work or marginal employment (in Germany, recently coined '*Mini-Jobs*' and '*Midi-Jobs*')<sup>2</sup>
- *Internal numerical flexibility* in the form of overtime or short-time work, part-time work, marginal employment or time banking (short- or long-term working time accounts)

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2 Although in Germany employment protection also holds for marginal employed workers, marginal employment is also often used to cope with work peaks.

- *Internal functional flexibility* as provided by multiple skills of the employees, flexible work organization, on-the-job learning and variable pay (for instance according to results or individual effort)
- *External functional flexibility* achieved through off-the-job learning, outsourcing, wage flexibility, and also through high-quality temp-agency work.

From the point of view of the employees, we distinguish four forms of security:

- *Job security* as the certainty of retaining a specific job with a specific employer
- *Employment or employability security* as the certainty of remaining in work, not necessarily with the same employer
- *Income security* as income protection in case that paid work ceases, for instance, through dismissal or mass unemployment, or through chronic illness, disability or retirement
- *Option security* as the certainty of having various employment options, for instance the possibility to combine paid work with unpaid work (for example caring or civic engagement), the entitlement to continuous education or training, or the right for intermediate working time reduction.

The nexus between these types of flexibility and security is more complicated than commonly thought (table 1). First, there is not only a trade-off between flexibility and security. The flexibility gains of employers do not necessarily mean a loss of security among employees; similarly, security gains of employees do not necessarily have to go along with flexibility losses among employers. Therefore, the talk about a balance between flexibility and security – usually thought of as a compromise between employers and employees – does unduly simplify the nexus.

As in marriage, it depends on how both partners act together. Apart from trade-offs, the flexibility-security nexus can also reflect a mutual supportive or complementary relationship. Job security, for instance, can induce employees to be loyal to the employer and to invest in firm specific human capital, thereby increasing internal functional flexibility.

The nexus, however, can also be deadly vicious, for instance when hire and fire policies lead to an overall insecurity, thereby lowering not only effective demand, but also fertility. While in the short run, the willingness to invest in human capital and, therefore, the availability of highly skilled workers would decline, in the long-term the size of the whole workforce could decrease.

Table 1: *The flexibility-security nexus: trade-off (t), complementary (c) or vicious relationship (v)*

Flexibility	Security			
	Job Security	Employment/ Employability Security	Income Security	Option Security
<i>External Numerical</i>	t	t / c / v	t / c / v	t
<i>Internal Numerical</i>	c	c	(t) / c	t / c
<i>Internal Functional</i>	c	c	t / c	(t) / c
<i>External Functional</i>	c	t / c / v	t / c	t / c

The flexibility-security matrix – as it is presented here – is static. It does not reflect the possible interrelationships between the different types of flexibility and security. Here, the dynamic perspective of transitional labour markets (tlm)<sup>3</sup> provides criteria whether flexible (or ‘non-standard’) forms of employment serve as

- stepping stones leading to labour market integration,
- maintain or enhance employment or employability through, for instance, combining part-time work with education or training,
- or finally lead to poverty or social exclusion if non-standard jobs do not provide the necessary capabilities to make people independent.

Thus, whether the flexibility-security nexus is a trade-off, a complementary or even a vicious relationship depends on the circumstances: especially on people’s position in the course of their life, but also on policies and on labour market regulations shaping this nexus.

The tlm-framework aims especially at critical events in people’s lives, in which work capacity or productivity is reduced due to unemployment, illness, old age, disability and social obligations such as care for children or other dependent persons. The bridging function that is to be supported by tlm-measures such as provision of income security, training and counselling thereby differs depending on specific target groups.

When it comes, for instance, to reduced productivity due to old age or disability, the provision of income security is advocated. Concerning workers whose work

3 The concept of transitional labour market was developed by a network of researchers in Europe sponsored by the fourth and fifth framework research programme of the European Commission under the acronyms TRANSLAM and TLM.NET. The theoretical background, illustrated by applications and good practices, is best represented in Schmid (2002) and Schmid and Gazier (2002). For further publications and current research, the reader is advised to visit the website: [www.siswo.uva.nl/tlm](http://www.siswo.uva.nl/tlm).

capacity is temporarily reduced due to social responsibilities or illness, the enabling of transitions back into the labour market or between full-time and part-time employment is called for. The German flexibility-security nexus faces the additional challenge not to serve as an incentive to reproduce the traditional role-division between men and women. Furthermore, technical progress, international division of labour but also changing individual preferences might require a change of occupation or the acquisition of new qualifications. In this case, transitions from unemployment to employment, between dependent employment and self-employment, and between high and low wage jobs are on the agenda.

We have now a proper framework to assess some of the German Hartz-reforms in terms of efficient and equitable *flexicurity* criteria. First, we ask to what extent flexibility, especially internal and external numerical flexibility has been strengthened by the latest labour market reforms. To assess the security dimension, we ask whether the measures provide minimum income security to the atypically employed. As state-run labour market policies do not aim anymore at improving job security, we further concentrate on the question if the measures enable transitions into standard employment, as an expression of enhanced employability. Lastly, we try to assess if option security among the atypically employed is improved. Thereby the particular needs of the schemes' target groups are taken into account. Concerning unemployment, we adopt a broad definition which includes illegal employment and discouraged workers.

### **3. How did Germany react to the 'flexicurity' challenge?**

Overall, it is fair to say that the flexibility-security nexus has not yet gained prominence in Germany. The neologism of *flexicurity* is rarely used, and the main actors have a quite different stance on this issue. In its 2005 National Reform Programme, which is part of the European Employment Strategy, the government took up *flexicurity* in a rather lukewarm way. As in 2004, it points out that the national economy has to substantiate itself in a competitive environment through flexibility which has to be compatible with employees' legitimate interest in security. The need of a fair balance of both elements is emphasised. We are therefore going to ask whether the Hartz-reforms succeed in fairly balancing the two antipodes.

Concerning *flexicurity*, the trade unions still emphasise the importance of job security during economic downturns. In order to meet employers' demands for flexibility, trade unions clearly favour internal functional flexibility. A second strategy is to claim the optimal realisation of win-win-situations within the *flexicurity*-matrix. Among parts of the trade unions, the flexibility-security nexus is very popular. The *trade union foundation* ('Hans-Böckler-Stiftung'), for example, focused on this issue by sponsoring research. By catering to various transitions in people's life

span, the approach held by the trade union foundation is strongly related to the tlm-framework. However, the operative branches of the trade unions are faced with a certain dilemma: Although it is accepted that social insurance schemes have to reflect the ongoing social and economic changes, the standard employment biography as a normative guideline is not being questioned: Derived rights for non-working partners within health and pension insurance are usually not challenged but confirmed (compare for example DGB 2003).

Among employers' representatives, the *flexicurity* concept and corresponding policy proposals are not explicitly on the agenda. Instead, the need for further flexibility, for instance through retrenching employment protection without considering complementary security as in the Danish case, is strongly emphasised. In exchange for giving up employment protection, employees might get the option of severance payments. On the firm-level, strong emphasis is also given to flexible wages. In this respect, the flexibility-security nexus is mainly discussed as an exchange of wage restraints and job security through so called 'Bündnisse für Arbeit' (pacts for work). Pointing to the already high unemployment-rate, employers identify disincentives in social protection. Granting security to outsiders, particularly to the low skilled, is understood as a genuine public duty and envisaged as a (minimum) income security provided by the state encouraging them to accept flexible jobs.

Recent German labour market reforms incorporate elements of *flexicurity* using different labels. The slogan 'Fördern and Fordern' (actively supporting and demanding) has for example been coined with the 'Job-AQTIV legislation' enacted in the beginning of 2002, AQTIV standing for activation, qualification, training, investment and placement. The slogan captures *flexicurity* issues insofar as the unemployed are to be actively supported at an early stage by a range of labour market integration measures. On the other hand, unemployed are obliged to actively search for employment and to take up almost every job. The Job-AQTIV legislation thus introduced a clear paradigm change on both the security and the flexibility dimension: Employability security is now favoured over job security and functional flexibility within a firm has decreased for the benefit of external numerical flexibility.

Later in that year (2002), the Hartz-commission chose a similar slogan: 'Eigenaktivitäten auslösen – Sicherheiten einlösen' (to help launch own initiatives but at the same time grant securities). This slogan, however, had a somewhat different connotation than 'Fördern und Fordern'. Instead of granting benefits and services only if the beneficiaries in return behave in the expected way, the Hartz-slogan intended to offer a wider range of choices and a broader set of services. The beneficiaries' own integration efforts should have been supported actively through services, for instance, child care facilities for working parents, comprehensive counselling services, including personnel services for small and medium sized enterprises, or incentives for employability measures both for employees and

employers. In the following sections, we are going to ask how far this strong proactive and preventative approach has been implemented in the selected reforms.

#### **4. What are the experiences with some specific ‘flexicurity’ measures in Germany?**

The Hartz-reforms comprise a wide range of measures. Most important are the conversion of the federal employment office into a modern service provider, the improvement of job placement activities and the merging of unemployment assistance and social assistance into a new basic benefit at the level of social assistance (‘Arbeitslosengeld II’)<sup>4</sup>. Additionally, a range of new and modified policy instruments has been introduced. The most promising among them in terms of *flexicurity* are first (1), a new *self-employment grant* for formerly unemployed, the so-called *Ich-AG*, second (2), the introduction of *personnel service agencies* (PSA), third (3), the reform of the *Mini-* and the introduction of the *Midi-Jobs*, and fourth (4), the *wage insurance* for elderly workers. In the following paragraphs, we will present these measures and assess their potential for an efficient as well as equitable flexibility-security nexus.

(1) The new *self-employment grant* (coined ‘*Ich-AG*’ by Hartz) supplements the already existing *bridge money* which capitalises unemployment benefit entitlements in order to support the unemployed in setting up their own business. Whereas the individual amount of bridge money results from the unemployment benefits plus social insurance contributions and is paid for only six months, the *Ich-AG* allowance is paid as a yearly decreasing lump-sum for three years provided that the yearly income does not exceed € 25,000. The *Ich-AG* allowance therefore is especially suitable for those self-employed who do not expect high profits from their self-employment endeavour at the beginning and for those who only have low unemployment insurance entitlements.

The take-up of the *Ich-AG* allowance has been much higher than expected, and it did not substitute the bridge money as originally feared. In terms of stock figures, in September 2005, 73,592 people were on bridge money, 236,412 on *Ich-AG* allowance, altogether about 0.8 percent of the active labour force (Bundesagentur 2006). However, subsidised business-founders are rather close to the labour market (Martin 2000); thus windfall gains cannot be cancelled out. Furthermore, there is evidence that at the end of 2004 some founders only intended to improve their financial status with the *Ich-AG* allowance due to the introduction of Arbeitslosengeld II (Bundesregierung 2006: 190).

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4 ‘Arbeitslosengeld II’ comes effective when claims to unemployment insurance (‘Arbeitslosengeld I’) have expired.

How should this measure be judged with respect to the ideal flexibility-security nexus? Regarding flexibility, the possibility to hire a self-employed instead of a dependently employed has, among others, the advantage for the employer that dismissal protection does not apply to self-employed. In this regard, both types of external flexibility have been strengthened.<sup>5</sup> Furthermore bureaucratic thresholds for founders have been lowered and recruitment of additional employment for founders has been facilitated through the option of fixed-term contracts for up to four years. Regarding branches, *Ich*-AGs are mainly taken up in services, construction, trade, craft and IT (Bundesagentur 2006).

Regarding the security-dimension, minimum income security is provided by a monthly allowance of € 600 in the first year, € 360 in the second, and € 240 in the third year. Concerning social security, it is important to note that in contrast to regular self-employment social insurance is obligatory as long as the *Ich*-AG-founders receive the corresponding allowance. In this context the possibility to return to Arbeitslosengeld I or II and the facilitation to enter health and care insurance under favourable conditions weaken traditional disincentives to take the risk of self-employment.<sup>6</sup> Although the *Ich*-AG allowance at first glance seems to provide the founder with minimum income security for three years, from the second year on the allowance just suffices to cover the cost of social insurance contributions. In fact, more than 20 percent in a sample of those who had already abandoned their *Ich*-AG stated as a reason that they had underestimated the cost of social insurance (Wießner 2005b: 397). In its recent plan to merge *Ich*-AG and bridge money (Bundesagentur: 2005), the Bundesagentur should consider those experiences.

Since this measure focuses on unemployed, the question whether the *Ich*-AG-founders will be able to sustain their businesses or at least don't return to unemployment is substantial for judging the effectiveness of this measure. So far, evaluation studies were faced with the problem that even the first *Ich*-AGs were still in the phase of assistance. This also applies to Wießner (2005a) according to whom 80 percent of the cumulated foundations were still active at the end of 2004. Interviews revealed that for more than half of the people surveyed, bridge-money and *Ich*-AG subsidised foundations have good or very good perspectives in the future (Wießner 2005b).

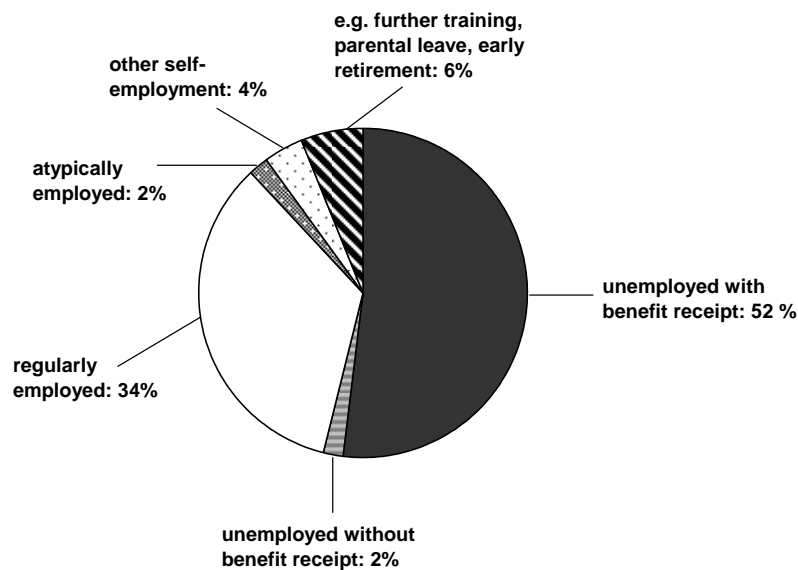
Until December 2004, 48,000 break-ups (nearly 18 percent) had been counted. Wießner (2005a) examined a sample of those break-ups. As can be seen in figure 1 around 54 percent of those affected returned to unemployment (only 2 percent without benefit receipt). 34 percent, on the other hand, abandoned their

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5 However, the legislator aimed to prevent the exchange of employment subject to social insurance contributions through *Ich*-AGs and also adapted the criteria to define false self-employment.

6 At a reduced rate of 14 percent *Ich*-AG founders have to pay about € 140 health insurance and a contribution of about € 20 to care insurance.

Figure 1: Continuance of the *Ich-AG* quitters



n = 643

Source: Wießner 2005a

business and took up employment subject to social insurance contribution. If the sample results could be generalized, this would mean that 90 percent of the *Ich-AG*-founders did not return to unemployment until the end of 2004.

What are the reasons for *Ich-AG* failures? No business plan was required until 2005. This clearly was a shortcoming. It would have helped to uncover the capacity to realise the business idea and the financial viability of the project. In a sample based on the measure entrants in the third quarter of 2003, detailed consulting was only supplied to 10 percent (Wießner 2005b: X).<sup>7</sup> Granting money without assisting the clients with their business idea by helping them to draft a business plan not only risks fast return to unemployment but can also drive clients into indebtedness. One third of the sample analysed by Wießner had accumulated debt.

It is interesting to note that the *Ich-AG* is increasingly carried out as part-time work. In this form, the *Ich-AG* is mostly taken up by women earning an additional household-income (Wießner 2005b: VII). In this regard they could use the working-time autonomy connected with *Ich-AG* subsidised self-employment to combine paid work with social tasks or obligations, thereby increasing option security.

To conclude, it must be acknowledged that the introduction of the *Ich-AG* clearly strengthens the German flexibility-security nexus. At the end of 2004, more than

<sup>7</sup> One question asked to the sampled founders referred to consulting, thus about one third would have even abstained from parts of their allowance in exchange to a wider range of founding consulting offers (Wießner 2005b: 393).

80 percent of the newly founded businesses supported by the *Ich-AG* allowance were still active. Nevertheless, improvements of the scheme should be envisaged: more care has to be taken to support the sustainability of these new forms of self-employment through comprehensive counselling, training, coaching and – of special importance – networking during all stages of the business initiative. Though further evidence is needed, the introduction of the *Ich-AG* also seems to strengthen parents' possibilities to combine paid with unpaid family work and thus cater to option security.

(2) The *personnel service agencies (PSA)* institutionalise temporary employment as a regular labour market measure. The Hartz-legislation requires each labour office to place a contract with at least one *temporary work agency (TWA)* – preferably an external service provider. In its function as *PSA*, the temporary work agency is required to place the unemployed who are assigned to them by the labour office. The idea is to privilege unemployed with barriers to employment who are usually not hired by conventional temporary work agencies (Jahn and Windsheimer 2004a). Until 2005, unemployed who were hired by a *PSA* got a temporary contract lasting from nine to twelve months; the employment-relationship was subsidized by the labour office which paid a monthly declining, case-based fee. In 2005, the contracting practice was changed. The duration of the contracts was fixed at six months and the subsidy was modified by reducing the average payment from € 1,100 to € 500 and by paying constant instead of declining amounts. A negotiable premium if the unemployed is placed is still granted. In contrast to conventional temporary work agencies, *PSAs* carry out placement rather than rental functions. To prevent cut-throat competition, collective agreements concerning wage formation in the temporary work agency sector have been adopted. The *PSA*-measure was highly contested, mainly due to over optimistic expectations provoked by the Hartz-report and the bankruptcy of a large provider (MAATWERK).

What is the general assessment of this measure? Regarding the flexibility-dimension, the introduction of *PSAs* had important side effects: it led to the abolishment of regulations of the temporary work market (for instance time limits of temporary work contracts) and thus helped to break the path for a more extended temporary work market. In this regard, *PSAs* can be judged as having enhanced external numerical flexibility and, to the extent that temporary work agencies can offer specialised and professionally skilled workers to firms, also external functional flexibility. The latest developments show indeed a growing dynamic in this market. Additionally, the introduction of *PSAs* also contributed to collective agreements that allow lower starting wages for *PSA*-workers, this also puts wages of regular temp agencies under a certain pressure.

With regard to the security dimension, the introduction of collective agreements for temporary work can be judged as having significantly contributed to enhance security for employees in this branch. Temporary work agencies are now committed to precise standards which led to an increasing acceptance of temporary

work. *PSA*-employees receive an employment contract and a wage with subsequent entitlements to social security benefits.

To cope with the initial idea that *PSAs*, compared to regular *TWAs*, should be more open to unemployed with barriers to employment, employment offices are required to specify personal characteristics and occupational properties of target groups within a tender procedure. Set by a tender, the monthly paid fee was supposed to differ depending on regional labour market conditions or individual barriers to employment. We would thus expect that workers in *TWAs* and *PSAs* vary in their characteristics.

*Table 2: Share of selected socio-economic groups in the TWAs and in the PSAs compared to the overall share in unemployment*

	<b>TWA-average in 2002</b>	<b>PSA-average from April to October 2003</b>	<b>Share of all unemployed in 2003</b>
<i>Socio-economic group</i>			
Women	27%	34%	44%
Foreigners	14%	10%	13%
Aged under 25	22%	33%	12%
Aged 50 or older	12%	11%	24%
Without vocational education	46%	30%	34%
(Formerly) long-term unemployed	8%	14%	34%
Health-related constraints	Unknown	13%	28%

Source: Bundesagentur (2003), Jahn and Windsheimer (2004b), own calculations.

As can be seen in table 2, compared to temporary work agencies, more women (as intended) are employed by *PSAs*. Foreigners, on the other hand, are under-represented. The high share of young workers in the *PSAs* results from a special stipulation which focusses on young workers (Jahn and Windsheimer 2004b). It demonstrates how certain target groups can be assisted in entering the labour market by specific contracting practices. Access for elderly workers who constitute about a quarter of the unemployed is as restricted in *PSAs* as in *TWAs*. Contra-intuitive is the fact that the share of workers without any vocational training is higher in *TWAs* than in *PSAs*. With 14 percent, the share of workers who formerly experienced long-term unemployment is higher in *PSAs* than in regular *TWAs*. All in all, the shares of disadvantaged groups in the *PSAs* are too small to allow the conclusion that the original intentions have been met. Because unemployed with low employment barriers are preferred, deadweight and substitution effects cannot be ruled out. Although it is recognised that the effect of targeted premium incentives is limited by the existence of structural unemployment, the public em-

ployment agency should concentrate on target groups and further enhance its efficiency by precise descriptions and improved contracting practices (a detailed analysis of the contracting-out is provided by Gülker and Kaps 2006).

Transitions into regular employment are supposed to be enhanced by a two-sided approach. On the one hand, *PSAs* are given financial incentives to place people into 'secure' jobs; a success bonus is paid when the unemployed is placed. On the other hand, the *PSA* is obliged to deliver training to workers in times when they are not on an assignment in order to improve their employability. Although some *PSAs* sporadically cooperated with educational institutions to deliver further training to their employees, training measures were mainly limited to 'coaching and assisted placement'. Structural reasons, for example the unknown and usually short duration of periods when the unemployed are not on an assignment hamper the organization of training measures.

Data on outflows from *PSA* lessen the great expectations that had been connected with this policy-measure. As can be seen in table 3, from the start of the *PSA*-measure in April 2003 until December 2005, all in all 128,975 unemployed (much less than expected) entered a *PSA*. Only 30 percent left the *PSA* to take up regular employment. However, integration-success differs between East and West Germany. A considerable problem, in this context, is the unfavourable economic environment especially in East Germany. Without positive job dynamics, the bridging function of temporary work misses its target. The time of the *PSA*-measure, therefore, might still come with the economic upswing.

Concerning the destination of the majority of participants who leave the *PSA* without getting a regular employment contract, some presumptions can be drawn based on a study conducted by Jahn and Windsheimer (2004b). The authors

*Table 3: Ongoing PSAs, cumulated inflows, stock, cumulated outflows and integration success in/until December 2005*

	Ongoing PSAs	Cumulated inflow	Stock	Cumulated outflow	Outflow into regular employment	Average integration rate*
<i>Region</i>						
Germany (total)	412	128,975	10,058	118,773	39,435	30%
East Germany	104	42,917	3,054	39,791	10,300	24%
West Germany	308	86,058	7,004	78,982	29,135	34%

\* The average integration rate is the share of outflows into regular employment on cumulated inflows.

Source: Bundesagentur (2006).

analysed *PSA*-exits from April to October 2003. During that time-span, 9,005 outflows had been counted, nearly half of which entered regular employment. A majority of the remaining workers (nearly 40 percent of the outflow) had been dismissed by the *PSA*, mainly due to behaviour-based reasons (ibid.). At least in part this could be due to comparatively high flexibility requirements that temporary workers are faced with.

To summarize, the success of *PSAs* was so far very limited and remained much behind the original expectations. Regarding flexibility, they led to the abolishment of temporary work market regulations and thereby strengthened external numerical flexibility. External functional flexibility has improved by the extent to which labour supply in temp agencies has broadened and diversified. Concerning unemployed with barriers to employment, the expectations have not been fulfilled. Although some risk groups – especially youth and long-term unemployed – are better represented in *PSAs* than in regular *TWAs*, foreigners, elderly and the low qualified are underrepresented. In order to better serve disadvantaged groups of unemployed, the public employment agency has to concentrate on these groups in the tender procedure. However, the latest modifications in the tender procedure point to a different dynamic in the future. Since the negotiable case-based subsidy was transformed into a constant amount, now only the placement-premium can account for individual barriers to employment. But as is known from other countries (Australia and the Netherlands in particular), the proper design of targeted premium incentives and a contested market of effective private providers can both be created.

(3) Marginal employment (*Mini-* and *Midi-Jobs*) was newly regulated through the Hartz-legislation. Different objectives were envisaged with these reforms: the containment of illegal work, especially in private households, the strengthening of employment subject to social insurance contribution, the creation of employment in the low wage sector and increasing incentives for unemployed to take up short-time employment as stepping stones to regular jobs (BMWA 2003: 4, Bundesregierung 2003: 2-4). As part of the reform, the 15 hours limit has been abolished and marginal employment can once again be exercised in addition to regular employment without becoming subject to social insurance contribution. Concerning *flexicurity* the most relevant part of this reform is the introduction of the new *Midi-Jobs*. They are to weaken financial disincentives to earn more than the maximum earnings of a *Mini-Job* by preventing the sudden onset of full social insurance contributions. Before the latest reforms, full social insurance contributions set in when passing the € 325 income limit. Now employees pay reduced contributions of 4 percent of their earnings when they earn at least € 401. Contributions then increase linearly until an income of € 800 when they reach the regular size of 21 percent. Full social insurance rights are achieved. Employers pay full contributions that are at 20.85 percent somewhat lower than the contributions for *Mini-Jobs* that usually amount to 25 percent (Rudolph 2003, Oschmiansky 2004). Theoretically, employers thus might be inclined to transform *Mini-Jobs* into *Midi-Jobs*.

From 2003 to 2004, *Mini-Jobs* increased by 11 percent to 6.64 million. *Midi-Jobs* increased by a 100,000 (Bundesregierung 2006: 211) to about 720,000. One reason for the limited emergence of *Midi-Jobs* could be lacking knowledge about this measure. For example, at the end of December 2003 only 670,000 workers were registered as *Midi-Jobbers* although 1.1 million were employed at a gross pay between € 401 and € 800 (Bundesagentur 2004: 3, 11). Another reason can be seen in the German tax law. Due to a couple's possibility to jointly tax its income, incentives to enhance working hours within that wage range are low if the spouse draws a regular salary.<sup>8</sup> Therefore the smoothing of the marginal employment trap only holds for persons whose income is between € 401 and € 800 and who are taxed as unmarried (Steiner and Wrohlich 2004).

The overall evaluation of marginal employment by employer representatives turns out positive. Especially *Mini-Jobs* are recognized as a cost-efficient and very flexible measure to deal with work peaks and extended opening hours. In this context, competitive branches such as trade, cleaning, gastronomy and tourism but also private households benefit most from this measure. Particularly small businesses appreciate the aspect of flexible and rapid use of marginal employment at relatively small costs (Fertig and Friedrich 2005: 129-130). Whereas those aspects already existed before 2003, by abolishing the weakly working hours limitation for *Mini-Jobs* the Hartz-reforms further strengthened internal numerical flexibility.

Concerning the security dimension, the maximum earnings for *Mini-Jobs* were raised from € 325 to € 400. Up to the maximum earnings only the employer pays social insurance contributions as part of a global contribution of 25 percent of earnings (12 percent retirement insurance, 11 percent health insurance and 2 percent taxes). Employees acquire claims to retirement insurance proportional to their small wages<sup>9</sup>. It is possible to pay an optional pension insurance contribution (7.5 percent of earnings) that supplements employers' contribution in order to gain full pension rights: entitlement to rehabilitation services, adherence of retirement benefits in case of invalidity and accomplishing waiting periods. This option has only been taken up by 10 percent in a sample of marginal employed workers (Fertig et al. 2004: 56-65).

Although possible earnings have been raised, marginal employment clearly does not provide sufficient independent income and social security. According to Bundesagentur (2004), about a quarter of the *Mini-Jobs* is occupied by young (under 20) and elderly (over 64) people who are usually covered by other sources of security. Another quarter is exercised as an additional second job (ibid.: 12).

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8 For married couples with one earner above the social assistance threshold, the option for the remaining partner to supply working hours within the sliding scale of payments to social contributions remains unattractive compared to a *Mini-Job*.

9 In 1999, before the latest reform, one year of working in a *Mini-Job* gave right to 4.17 DM (€ 2.12) retirement entitlement and 1.4 month were taken into account as waiting period (Neuhold 1999: 63).

By abolishing the regulation that *Mini-Jobs* – exercised in addition to regular employment – are subject to employees' social insurance contributions, the reform strengthened incentives to use *Mini-Jobs* in that sense. This part of the reform is neither financially sustainable nor useful from a flexicurity-viewpoint because it gives advantages to those groups who already have income security.

To judge the bridging function of this measure, one has to differentiate between transitions from illegal employment into formal employment and from unemployment into regular employment. In order to give incentives to transform illegal household work into formal employment, the private household pays a reduced contribution to social insurance of 12 percent and can set off ten percent of the *Mini-Job's* costs against its tax liability (€ 510 at the maximum). The doubling of declared marginal employment in private households within one year to 60,000 (Bundesagentur 2006) is an indicator for the success of this strategy.

To support the policy-aim that *Mini-Jobs* function as a stepping stone for the unemployed, the legislator made 'Arbeitslosengeld II' conditional on accepting any job including marginal employment. In a sample of 2,445 *Mini-Jobbers* analysed by Fertig et al. (2004), 15 percent had been unemployed before they took up marginal employment.<sup>10</sup> The small share was seen as a result of income thresholds for earnings additional to unemployment benefits. For beneficiaries of 'Arbeitslosengeld II', the legislator therefore raised thresholds in 2005.

When it comes to the bridging function of *Mini-Jobs* doubts are appropriate. Table 4 displays information on the reasons for taking up marginal employment and on the shares that made transitions to regular employment. It reveals that 15 percent of the sampled marginal workers took up a *Mini-Job* because they did not find another job. At the same time, only 9 percent of those who had left their *Mini-Job* on the date of interview performed regular employment instead.

*Midi-Jobs* rather fulfil bridging expectations than *Mini-Jobs* but as has been pointed out they are considerably less important in number than *Mini-Jobs*. 32 percent of those who had left their *Midi-Job* at the date of interview had made a transition to regular employment. More than one fourth of respondents exercised a *Midi-Job* because it was the only employment found. There is evidence that transition success of marginal employment significantly differs between East and West Germany. In this regard, the overall bad economic situation in East Germany constitutes an additional barrier to realise transitions into regular employment. Furthermore, the question whether marginal employment substitutes employment subject to social insurance contributions – thereby reducing income security – is a vital issue in Germany. Although transitions from marginal employment to regular employment have increased, the general balance between

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10 Among the unemployed who took up a *Mini-Job* the majority was long-term unemployed before (Fertig et al. 2004: 67).

Table 4: Selected figures on the bridging function of marginal employment

Type of marginal employment	Region	Share of workers who...	
		could not find other employment	exercised regular employment afterwards*
Mini-Job (n = 2,445)	Germany (total)	15%	9%
Midi-Job (n = 576)	Germany (total)	28%	32%
	East Germany	45%	27%
	West Germany	20%	35%

\* Share on all workers who had left their Mini- or Midi-jobs at the date of interview.

Source: Bundesagentur (2004: 14); Fertig et al. (2004: 67, 81); Fertig and Friedrich (2005: 163-166).

marginal employment and employment subject to social insurance contributions tends towards zero (Bundesagentur 2004: 14). It is questionable whether each regular job that had been converted into a *Mini-Job* would still exist otherwise.

It can be taken for granted that marginal employment improves option security for many parents. Asked why they exercised marginal employment, a quarter of the *Mini-Jobbers* and a third of the *Midi-Jobbers* answered that they consciously decided to do so in order to improve their work-life balance (Fertig et al. 2004: 81, Fertig and Friedrich 2005: 166). Given the great dependence on other security sources (such as derived rights to social insurance provided by the spouse); the effect of marginal employment on 'gender-mainstreaming' as an important issue in the European Employment Strategy, however, has to be considered critically.

Table 5 shows that about three-quarter of all *Mini-Jobbers* and 84 percent of all *Midi-Jobbers* are women. Furthermore, the majority of *Midi-* and especially *Mini-Jobbers* is married and about two third of all spouses of marginal workers are employed and in most cases probably provide derived social security rights to pension, health and care insurance. These simple figures already show how combination security enabled by marginal employment still depends on the so-called male breadwinner model. The reform of *Mini-Jobs* enhanced both the advantages as well as the disadvantages of this employment form. For women who have to perform unpaid family work marginal employment often is the only possible form of employment, and for them potential earnings have somewhat increased. The concentration of marginal employment in the service-sector on the other hand could turn into a barrier for women in this sector who would like to move on to regular full-time employment.

Table 5: Share of selected socio-demographic characteristics of the Mini-and Midi-Jobbers

	Woman	Married	Spouse employed	Receiving transfers	Average age
Mini-Job (n = 2,445)	73%	72%	66%	27%	47 years
Midi-Job (n = 576)	84%	64%	67%	16%	42 years

Source: Fertig et al. (2004: 51), Fertig and Friedrich (2005: 156).

To draw a conclusion on marginal employment, *Mini-Jobs* and *Midi-Jobs* should be discussed separately. Although *Mini-Jobs* provide flexibility and are highly appreciated as side-jobs by many employees, the core idea of *flexicurity* is hardly promoted by this policy measure. Instead of enabling an (independent) minimum income security; the exercising of *Mini-Jobs* depends on the availability of other sources of security and income. Although the latest reform helped to convert illegal private household employment into legal employment, transitions into regular employment of only 9 percent are too few to serve as a stepping stone for unemployed into regular employment. *Midi-Jobs*, on the other hand, lead to higher shares of upward transitions but too less people are engaged in this employment relationship as to significantly enhance the *flexicurity*-nexus. While marginal employment today enables many mothers to combine paid and unpaid family work, it is at the cost of 'gender-mainstreaming' and more sustainable individual security entitlements.

(4) The main idea of the *wage insurance* for elderly workers which was newly implemented as part of the Hartz-reforms is to temporarily compensate wage losses of elderly workers. Job changes might become necessary due to structural changes or the loss of individual productivity. Especially elderly workers face large income losses in case of unemployment and subsequent re-employment. Their risk of income loss is also nourished by the fact that internal labour markets which implicitly provided wage insurance through seniority wages are increasingly disappearing. Furthermore, the escape into early retirement as an income insurance device is not any longer a viable option. Wage insurances have already been introduced in various forms in the United States, in France, and most comprehensively and successfully in Switzerland.

Concerning the flexibility dimension, *wage insurance* is supplemented by setting incentives for employers to hire elderly workers. The employees' benefit may be cumulated with wage cost subsidies for the employer; these subsidies already existed before the latest reform. Additionally, the Hartz-reforms included a regulation specifying that workers older than 52 (before, the age-limit had been 58) could be employed on the basis of a fixed-term contract without time limit. The

German legislator is now planning to introduce other flexibility mechanisms, because the European court of justice in the end of 2005 declared that the regulation violates community law.

With regard to the security dimension, the German scheme is a supplement to the unemployment insurance system. It temporarily replaces 50 percent of the wage loss between the previous and the new job if an unemployed person who is older than 50 takes up a new lower paid job which is subject to social insurance contribution. The fact that contributions to pension insurance are increased so that 90 percent of the formerly paid contributions are reached is interesting from a flexicurity viewpoint.

Although *wage insurance* for elderly workers constitutes an attractive combination of wage flexibility and income security, in 2004 only 6,433 elderly workers participated in this measure (Eichhorst and Sproß 2005). To some extent the German scheme is not well balanced with respect to flexibility and security. The wage compensation is only paid during the remaining time of unemployment benefit entitlement which has to be at least 180 days. Those unemployed who do not comply with this minimum requirement do not have access to the scheme in the first place.

To draw a conclusion, the *wage insurance*-measure strengthens external numerical flexibility while at the same time granting some income security to elderly workers. Participation in the measure is restricted to workers who at the time of a new job offer still have at least 180 days entitlement to unemployment insurance benefits. And as most unemployed elderly workers – especially in East Germany – are long-term unemployed, the *wage insurance* incentive had a very limited impact. If the results do not improve, the scheme is going to be discontinued in the current year.

## **5. What lessons can be learned from the German experiences for the European Employment Strategy?**

First, there is no definition of *flexicurity* which is shared by social partners. Trade unions perceive security as a precondition for flexibility and emphasise functional flexibility within stable employment. The employers, on the other hand, tend to consider flexibility – especially wage flexibility – as the solution for employment security and stress disincentive effects deriving from employment protection and unemployment benefit receipt. These varying perceptions of *flexicurity* reflect the structural tension of different interests that have to be taken into account when measures aimed at the reconciliation of flexibility and security are designed and implemented.

But the debate on a proper flexibility-security nexus is just beginning. There is some chance that it could be the vehicle to revitalise the social dialogue and promote the negotiation of new topics between the social partners, both at national and European level. Especially the improvement of employment security by establishing branch specific collective training funds or facilitating complementary relations between flexibility and security in the course of people's lives seem to be issues for negotiations where all sides could win in the long run. The further stimulation and coordination of this debate at the European level could be a promising task for the Directorate General 'Employment and Social Affairs'. Especially the creation of adequate indicators, the careful screening and the effective diffusion of good practices are worthwhile objectives.

Concerning the recent German experiences, it must first be acknowledged that the German labour market reforms responded to the debate on *flexicurity* with some innovative measures. In terms of flexibility, the presented measures clearly strengthen numerical flexibility which, compared to the EU-15 average, had indeed been underdeveloped. The possibility to return to compulsory social insurance facilitates the decision to found an enterprise. Increased thresholds for additional income for long-term unemployed, the smoothing of social insurance contributions within the *Midi-Job*-scheme and the conversion of claims to unemployment insurance into a wage grant within the *wage insurance*-scheme for elderly workers clearly alleviate disincentives in the German security system typically criticised by employer representatives.

But in terms of security, the presented measures only cover the (new) social risks to some degree and do not go far enough. The strong pro-active and preventative implications of the slogan 'Eigenaktivitäten auslösen – Sicherheiten einlösen' (to help launch own initiatives but at the same time grant securities) were only partly taken up. Whereas the original approach included services, for instance childcare facilities for working parents or comprehensive counselling services, the *PSA* is the only measure which includes a link to the employability concept. Also new social rights such as the right to substantive training leaves, the right to sabbaticals, to income insurance at temporary working time reduction or to consulting are still missing in the German *flexicurity*-nexus.

The analysis of the four measures revealed that the balance of the flexibility-security nexus in Germany could be improved by strengthening the security dimension within the individual measures. Although the experiences with the *Ich-AG* are encouraging, especially when it comes to the question of sustainability of new businesses a more encompassing strategy that provides consulting, training and networking is of utmost importance. In general, self-employment initiatives are only useful for a small group of unemployed who are rather close to the market.

*PSAs* still fail to concentrate on their original target group – unemployed with barriers to employment. The contracting-practice has to be improved to cope with

this, otherwise there is little justification to subsidise the work of *PSAs* because they could as well be substituted by regular *TWAs*.

With regard to *Mini-Jobs*, employers have meanwhile been demanding the re-amendment of this measure. They want to handle the monthly wage-limit of € 400 in a more flexible way (Fertig and Friedrich 2005: 131). Often criticised are the facts that marginal employment due to income-thresholds is unattractive for recipients of unemployment benefits and attracts people who primarily receive security from other sources – especially housewives. *Midi-Jobs* which grant individual insurance were to function as stepping stones into regular employment for persons who were formerly trapped in marginal employment. In fact, the measure has not been very successful, probably due to the possibility to jointly assess a couple's income so that in effect the marginal employment trap has only been smoothed for singles. German evaluation studies on the effects of subsidising social insurance contributions of people with low earnings and their employers have so far not been favourable (Sinn et al. 2002: 13-16). The qualification fund that was part of such a pilot project, namely the 'Saar-Gemeinschafts-Initiative', is worth mentioning. A qualification strategy that could promote upward transitions is completely lacking in the *Mini-* and *Midi-Job* concepts.

Although *wage insurance* in Germany has not been successful due to both its restrictive design and lack of information among potential users, in principle, it could become a paradigm example for a functioning flexibility-security nexus in the European Employment Strategy. The Swiss scheme, in this regard, has proven more successful than the German one. According to rigorous evaluations, it is more successful for the following reasons: First, all workers entitled to unemployment benefits are also entitled to *wage insurance* independent of their age, second, the replacement rates of the Swiss 'Zwischenverdienst' are quite generous, especially for elderly workers with dependent family members, and third, the requirement to accept jobs with lower income is strictly administered (Lechner et al. 2004).

To finish as we began with Schumpeter's paradox: If we want a high speed labour market, we have to develop – in analogy to broader traffic routes, more reliable bridges, stronger brakes but also speed limits and speed control for fast travelling motorcars – improved labour market services, transitional labour markets bridging critical events in the course of people's lives, stronger income and employability securities and, last but not least, strictly controlled minimum standards.

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