

The evolution of labour market-related government expenditure in Germany

The extremely favourable and persistently robust development of the German labour market since the middle of the last decade has significantly eased the strain on public finances, with even the severe economic downturn of 2009 ultimately leaving no lasting mark. As a result, labour market-related government expenditure as a percentage of gross domestic product has contracted from 4% to 2½% since 2005. The Federal Employment Agency's spending on unemployment benefit I and active labour market policy measures has fallen significantly, consequently making it possible to cut the contribution rate from 6.5% to 3.0%. Labour market-related expenditure by central government (the basic allowance for job seekers, in particular) initially rose markedly following the entry into force of the Hartz IV reform in 2005 but has been in steady decline since 2009. On the whole, the financial strain on local government budgets has also eased considerably.

The Federal Employment Agency may currently be recording surpluses, but a further reduction in the contribution rate would, at most, only appear financially manageable if the present extremely favourable labour market situation and the exceedingly low number of unemployment benefit I recipients were to prove sustainable. Irrespective of this, it would also be possible to cut the contribution rate if central government were to assume financial responsibility for non-insurance-related benefits, which are financed through contributions at the current juncture. It is occasionally proposed at the European level to fundamentally reform unemployment insurance by introducing a European unemployment insurance scheme to partially replace national schemes. However, in order for these proposals to hold water, the economic and socio-political framework of the European Union must be harmonised to a more in-depth and fundamental extent, which is not currently on the agenda.

At present, there are no signs of further noticeable relief at the central, state and local government level with respect to labour market-related spending. The fiscal impact of the statutory minimum wage, which was introduced in 2015, hinges on how it affects employment. All other things being equal, the wage increases triggered by the minimum wage will lower the need for transfer payments by general government and also boost its revenue. On the other hand, however, if jobs were lost, which would be a particular concern in the event of sharp increases in the minimum wage in future, it would also place a strain on public finances.

The impact of labour market developments on public finances¹

Labour market exerts significant influence on public finances

Developments on the labour market exert a considerable influence on government revenue and expenditure. For example, tax and social contribution receipts fluctuate with employment, wages and salaries. Expenditure is affected by changes in unemployment, in particular, with the main expenditure items including labour market-related benefits such as unemployment benefit I (insurance-related benefit), unemployment benefit II (welfare-related benefit) and spending in connection with active labour market policy measures.

Labour market-related government expenditure significantly down after rising in the wake of labour market reforms and economic crisis

Looking at the overall picture, labour market-related government expenditure amounted to €88½ billion in 2004 (for information on the classification of expenditure, see the box on page 15).² It was chiefly the merger of unemployment assistance and social assistance to create the basic allowance for job seekers that initially drove this expenditure to €91½ billion in 2005, which was largely attributable to a higher uptake by persons able to work who were generally already entitled to social assistance. However, this was followed by a marked underlying trend decline, which was only interrupted by a brief spike in 2009 as a consequence of the financial and economic crisis. At last report, labour market-related expenditure totalled around €73 billion, meaning that it has contracted sharply as a percentage of gross domestic product (GDP) from 4% to 2½% over the past ten years.

IAB calculations on fiscal costs of unemployment paint similar picture

The Institute for Employment Research (IAB) takes a different approach to calculating the fiscal costs of unemployment.³ First, it factors in the tax and social contribution revenue estimated to be lost as a result of unemployment. Second, compared with the aforementioned calculations, expenditure is defined more narrowly, and spending on non-registered (long-term) unemployed persons is not taken into account.⁴ Using this method, a drop in fiscal

costs was recorded immediately after the Hartz IV reform as far back as 2005. Expenditure-related and revenue-related costs calculated in this manner virtually halved as a percentage of GDP from almost 4% in 2005 to 2% in 2013. Here too, the temporary resurgence observed in 2009 and 2010 only briefly overshadowed the general downward trend.

This article will focus on the evolution of labour market-related government expenditure and the range of variables in play since 2005, the year in which the Hartz IV reform entered into force. In addition to spending by the Federal Employment Agency, which is generally financed through contributions, the spotlight will also shine, in particular, on the tax-financed basic allowance for job seekers and other associated benefits, as well as the labour market policy measures implemented at the central, state and local government level. It will go on to also explore the revenue side of the unemployment insurance scheme organised by the Federal Employment Agency, before presenting the financial cross-connections between the Federal Employment Agency and central, state and local government budgets with respect to labour market-related benefits.

Focus on labour market-related expenditure

¹ For the evolution of labour market-related government expenditure in the years prior to 2006, see Deutsche Bundesbank, The evolution of labour market-related expenditure, Monthly Report, September 2006, pp 59-83.

² Financial relations between central, state and local government, such as, in particular, refunds of administrative costs and the central government grant to the Federal Employment Agency as well as, conversely, the latter's payments to central government, but also central government's contribution to local government expenditure on accommodation, are factored out of the overall review.

³ See Institute for Employment Research (IAB), Gesamtfiskalische Kosten der Arbeitslosigkeit im Jahr 2013 in Deutschland, Aktuelle Daten und Indikatoren, December 2014. For more information on the methodology used, see IAB, Kosten der Arbeitslosigkeit nochmals gesunken, IAB-Kurzbericht 2/2014, p 11.

⁴ The IAB only examines how public finances are affected by factors directly associated with registered unemployment. Consequently, in contrast to the definition used here, expenditure such as spending on participants in training schemes and on recipients of unemployment benefit II who are employed ("income boosters") or not registered as unemployed and cohabiting social allowance recipients is disregarded. According to IAB calculations, around 57% of costs (€32 billion) was attributable to expenditure and 43% (€24 billion) to revenue in 2013.

The classification of labour market-related expenditure

Labour market-related expenditure is primarily understood here as the total expenditure by the Federal Employment Agency as well as expenditure by the central, state and local governments (especially the former and the latter) on the basic allowance for job seekers and other associated active labour market policy benefits or measures.¹ In this respect, the scope of benefits associated with the basic allowance not only comprises monetary transfers to recipients of unemployment benefit II who are able to work, but also the social allowance for dependants living in the same household who are unable to work (particularly children). Unemployment benefit II recipients also include persons who are not registered as unemployed, but who, for reasons of childcare, nursing care, illness or training, are usually temporarily unavailable to the labour market, or those who take up employment but receive means-tested top-up benefits.

The basic allowance comprises the standard financial need as well as contributions to health and long-term care insurance schemes,² the assumption of rent costs of an appropriate level including heating costs³ and other additional needs. Until 2010, it also included a staggered additional payment after the switch from unemployment benefit I. In connection with the basic allowance, expenses related to the active labour market policy of (re)integrating the long-term unemployed and administrative costs associated with support are also incurred.

Finally, labour market-related expenditure also comprises other needs-based expenditure by central, state and local governments which is closely related to unemploy-

ment benefit II. This includes the additional children's allowance, also introduced in 2005, which aims to prevent low-income families from claiming unemployment benefit II solely to meet the needs of their children. It also includes the education and integration allowances introduced in 2011, which finance primarily non-financial benefits in the area of school and leisure for children and young people who normally receive the basic allowance.⁴

When interpreting the figures, it should be noted that the classification made here does not solely consider government expenditure directly influenced by developments on the labour market, since basic allowances for persons able to work but temporarily unavailable to the labour market are also included, for example. Benefits for family members who are unable to work (social allowance recipients) are also taken into account, given that their needs are related to the income situation of unemployment benefit II recipients living in the same household.

¹ In 2004, ie before the introduction of the basic allowance (Hartz IV reform), this comprised, in addition to unemployment assistance, the estimated benefits as well as the reintegration and administrative costs borne by central, state and local governments for recipients of a housing allowance and social assistance who were able to work. Following the reform, these expenses were integrated into the basic allowance. In 2005, outstanding expiring unemployment assistance payments were incurred.

² Central government also initially made contributions to the statutory pension insurance scheme for unemployment benefit II recipients. These contributions were effectively halved in 2007, and completely abolished in 2011.

³ Pursuant to section 22 of the Second Book of the Social Security Code (SGB II).

⁴ These benefits are also available to children in low-income families who are in receipt of a housing allowance or additional children's allowance.

The financial development of the Federal Employment Agency

Federal Employment Agency's financial situation significantly improved since 2005

Responsibility for the statutory unemployment insurance scheme in Germany lies with the Federal Employment Agency (see the box below for the debate surrounding a European unemployment insurance scheme). In particular, temporary wage substitutes in the event of unemployment and active labour market policy measures are, as a general rule, financed equally by employees and employers in the form of contribution payments. The Federal Employment Agency's finances have been subject to major fluctuations in the past. After over a decade dominated by deficits, which were very high in some instances, and a broadly balanced budget in 2005, sizeable surpluses were initially recorded in 2006 and 2007. However, the crisis then sent the deficits higher still in 2009 and 2010, and the reserves that had been built up previously were fully depleted. The

Federal Employment Agency has since recorded slight surpluses, which have been edging upwards in recent times. However, to look solely at the bottom line would be to ignore a fundamental improvement in the Federal Employment Agency's finances over the past ten years on the back of both positive labour market developments and a generally muted spending policy. Against this favourable backdrop, the contribution rate has swiftly and incrementally contracted by more than half from 6.5% to 3.0% (see the annex on legislative changes on pages 28 to 33). Overall, this shrank the Federal Employment Agency's revenue by almost 5% and its expenditure by almost 5½% on an an-

Comments on a European unemployment insurance scheme

Discussions on institutional reforms in the EU occasionally elicit a proposal to shift some of the tasks of national unemployment insurance schemes to a European unemployment insurance scheme.¹ The objective is to share the financial burden – which varies from country to country owing to differing developments in unemployment – across the EU or the euro area. A levelling of structural differences would be accompanied by longer-term transfers between the countries. However, it appears that this would only be worthy of consideration if social and economic policy were also fundamentally centralised at the European level, as national decisions would otherwise have a strong financial impact on other member states. But as there is currently no majority to go down that path, the proposals focus more on the potential to improve economic stabilisation by means of a cross-border balancing system. This holds the promise of better cushioning the impact of asymmetric shocks on unemployment in individual countries.

However, if a country has sound public finances, it would currently not be problematic for it to

cover cyclical financing requirements at the national level by depleting reserves or borrowing and then correspondingly replenishing the reserves or repaying the loans in better times. The European budgetary rules are also based on cyclically adjusted budget balances and therefore do not stand in the way of cyclically induced fluctuations in the budgets of national unemployment insurance schemes (automatic stabilisers). Furthermore, it should be borne in mind that although, in principle, the proposals aimed at improving economic stabilisation do not envisage any permanent structural transfers between countries, doubts have been raised from a practical viewpoint – not least regarding whether, for example, enough can be done to counteract the incentives for individual countries to interpret uniform insurance conditions more freely. All in all, as things currently stand, the proposals for a European unemployment insurance scheme appear to hold no water.

¹ See, for example, European Commission, Employment policy beyond the crisis, Social Europe guide, Volume 8, September 2014, pp 48-51.

nual average between 2005 and 2014 (see the table on page 18).⁵

Expenditure

Bulk of spending on wage substitutes and vocational assistance

The Federal Employment Agency's expenditure is dominated by unemployment benefit I, which accounted for approximately half of its budget in 2014. Roughly one-fifth was spent on active labour market policy measures (preparatory vocational training and advanced vocational training, in particular), while around one-quarter was set aside for administrative costs (about one-sixth in net terms if central government's refunds for transferred administrative functions are deducted).

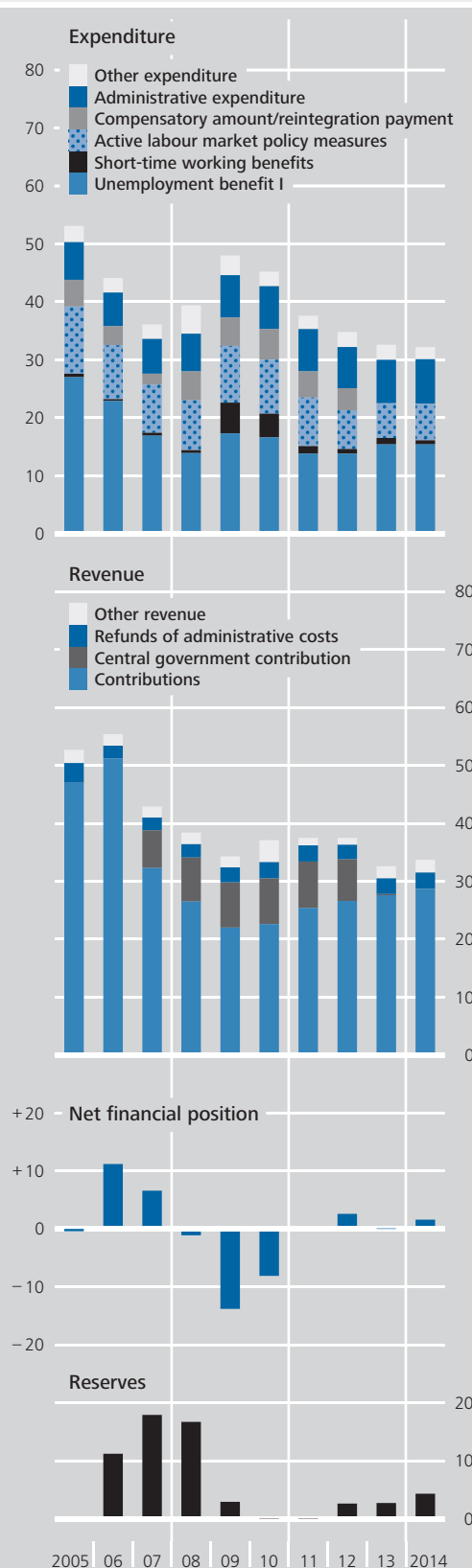
Since 2005, spending sharply down on wage substitutes ...

The Federal Employment Agency's spending on both unemployment benefit I and active labour market policy measures has fallen by an average of around 6% *per annum* since 2005. The drop in unemployment benefit I had more or less levelled off by 2008 (see adjacent chart). Expenditure picked up again in the crisis year of 2009 before returning to its previous low level. Spending on unemployment benefit I has thus halved to ½ of GDP at last count, primarily on account of the dwindling number of recipients of unemployment benefit I, which shrank from 1.7 million in 2005 to below 1 million in 2008. Since then, it has only ever edged above the million mark in 2009 and 2010, when pay-

⁵ This does not take into account the pension fund for civil servants at the Federal Employment Agency, which was set up in 2008. Contributions calculated in actuarial terms are transferred to this fund for current civil servants out of the Federal Employment Agency's budget. It also received one-off allocations totalling €2.5 billion in the year it was established. At the same time, the fund has assumed current expenditure for pensions and retired civil servants' health-care subsidies. Although contributions currently outstrip payments, this is set to reverse. The Federal Employment Agency is no longer awarding civil servant status to its employees, and the pension reserve should be fully depleted in the latter half of the century. The calculation hinges on the anticipated return on fund capital, which is managed by the Bundesbank. Owing to the persistent low-interest-rate environment, the "allocation rate" (actuarial contribution rate as a percentage of pensionable remuneration) was raised from 60% to 80% with effect from 1 January 2015. The capital stock totalled just over €4½ billion at the end of 2014.

Finances of the Federal Employment Agency

€ billion



Source: Federal Employment Agency.
 Deutsche Bundesbank

Financial development of the Federal Employment Agency*

€ billion

Item	2005	2010	2011	2012	2013	2014	2014 versus 2005 ¹
Revenue							
Contributions	47.0	22.6	25.4	26.6	27.6	28.7	- 5.3
Revenue from insolvency benefit contributions	1.3	2.9	0.0	0.3	1.2	1.3	0.0
Central government contribution ²	-	7.9	8.0	7.2	0.2	-	.
Central government refunds of administrative costs	3.4	2.8	2.8	2.5	2.7	2.8	- 2.0
Other revenue	1.0	0.8	1.3	0.9	0.9	0.9	- 1.4
Total	52.7	37.1	37.6	37.4	32.6	33.7	- 4.8
Expenditure							
Unemployment benefit I	27.0	16.6	13.8	13.8	15.4	15.4	- 6.1
Short-time working benefits	0.6	4.1	1.3	0.8	1.1	0.7	1.2
Insolvency benefit	1.2	0.7	0.7	1.0	0.9	0.7	- 6.0
Active labour market policy measures	11.6	9.3	8.4	6.7	6.0	6.3	- 6.6
Benefits pursuant to the Phased Retirement Act (<i>Altersteilzeitgesetz</i>)	1.1	1.3	1.3	1.3	1.4	1.1	- 0.1
Compensatory amount/reintegration payment	4.6	5.3	4.5	3.8	-	-	.
Administrative expenditure	6.5	7.4	7.3	7.1	7.5	7.7	1.9
Other expenditure	0.4	0.4	0.3	0.3	0.3	0.3	- 5.1
Total	53.1	45.2	37.5	34.8	32.6	32.1	- 5.4
Surplus (+) or deficit (-)	- 0.4	- 8.1	0.0	2.6	0.1	1.6	.
Reserves	0.0	0.0	0.0	2.6	2.7	4.3	.
<i>Memo items</i>							
Contribution rate (as a percentage)	6.5	2.8	3.0	3.0	3.0	3.0	.
Recipients of unemployment benefit I (in thsd)	1,728	1,024	829	849	915	888	- 7.1
Monthly spending per recipient of unemployment benefit I	1,303	1,351	1,384	1,357	1,403	1,443	1.1

Source: Federal Employment Agency. * Core budget of the Federal Employment Agency, excluding pension fund for civil servants.
 1 Annual average change as a percentage. 2 Excluding deficit offset by central government up to and including 2005 and again in 2010.
 2013: last refund of excess reintegration payments in the preceding year.

Deutsche Bundesbank

ments of short-time working benefits, in particular, increased very significantly (see the chart on page 19). Cuts in the maximum period of entitlement (initially from 32 to 18 months from 2006 and finally back up to 24 months from 2008) also drove down the number of recipients.⁶ Spending per benefit recipient has, on average, only risen by just over 1% *per annum* amid quite substantial fluctuations.⁷ What this ultimately shows is that cyclical unemployment has, over time, tended to increasingly focus on lower income groups. Spending on short-time working benefits, which are normally insignificant in quantitative terms and can be regarded as a special form of unemployment benefit I or, to some extent, as its replacement in times of crisis, spiked in 2009 and 2010 and was amplified further still by government intervention measures – chief among them extending maximum periods of entitlement and refunding social contributions, the onus of which is normally on employers.

In the area of active labour market policy, expenditure fell somewhat more steadily over the overall observation period. While spending likewise increased in this area in the crisis year of 2009, it resumed its downward path in the ensuing period before bottoming out, it would appear, in 2013. All in all, spending on active labour market policy measures has moved largely in tandem with unemployment benefit I and, thus, with unemployment as a whole.⁸

... and on active labour market policy measures

⁶ As a general rule, unemployment benefit I is paid out for a maximum of 12 months. On reaching 50, 55 and 58 years of age, this rises to 15, 18 and 24 months respectively (section 147 of the Third Book of the Social Security Code (SGB III)).

⁷ Unemployment benefit I is generally set at 60% of the recipient's previous net earned income. If the recipient is the parent or guardian of at least one child, this rises to 67% (section 149 of the Third Book of the Social Security Code (SGB III)).

⁸ The reintegration payment, which the Federal Employment Agency paid to central government to refund half of the reintegration benefits and administrative costs for recipients of unemployment benefit II, was completely phased out in 2013. At their peak (in 2010), payments to central government reached almost €5½ billion.

Administrative costs out of line with downward trend in benefits spending

By contrast, administrative costs have risen by an average of just under 2% *per annum* (currently totalling just over €7½ billion), with their share of expenditure recently hitting 24%. It should be noted that the Federal Employment Agency also performs administrative functions for central government, especially in connection with support for unemployment benefit II recipients. Factoring out refunds paid by central government for these services, administrative costs account for 16½% of the correspondingly reduced (net) overall expenditure.⁹ The sharp decline in unemployment has thus sent administrative expenditure per unemployed person significantly higher. On the one hand, this implies more intensive support. On the other hand, however, this is likely to be an area for potential savings that the Federal Employment Agency has identified and is aiming to tap.¹⁰ Another factor contributing to the rise in the Federal Employment Agency's administrative expenditure was the decision to build up a capital stock to cover future pension obligations. In consolidated terms (including the pension reserve), spending would have risen by 1½% on an annual average.

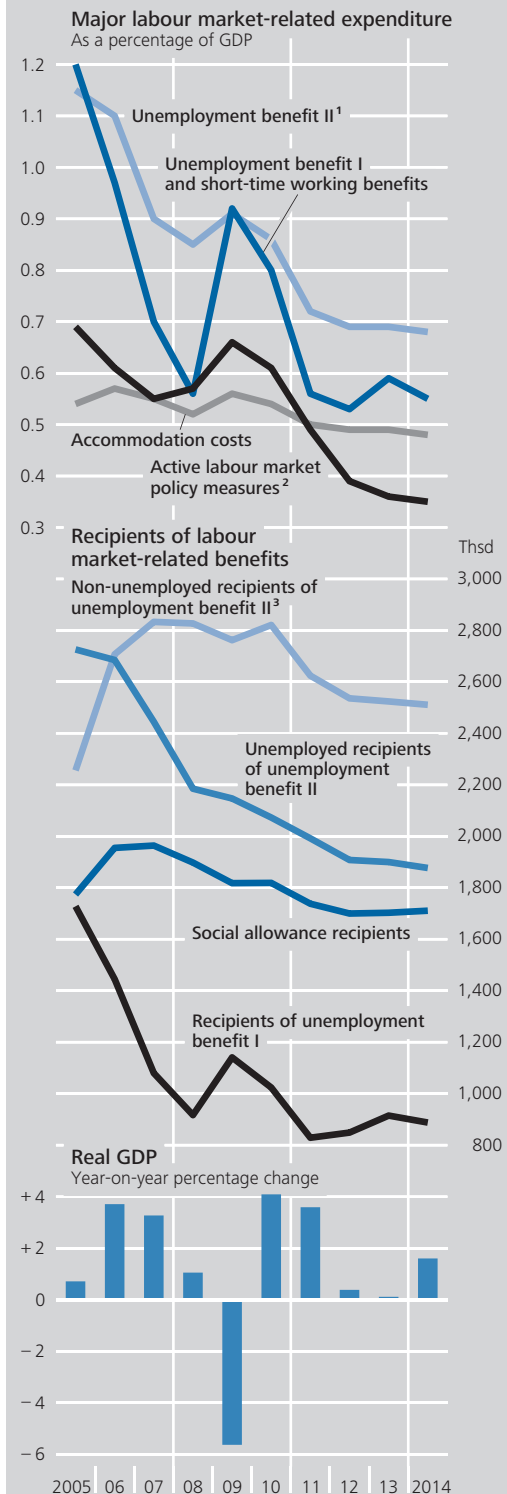
Phased retirement subsidies discontinued

Above and beyond its core functions, the Federal Employment Agency also plays a role in subsidising phased retirement. Under the state-subsidised phased retirement scheme introduced in 1996, the Federal Employment Agency reimburses for a maximum of six years the remuneration top-ups and increased pension contributions paid by employers if the vacancies created as a result are filled by either un-

⁹ Adjusted for these refunds, administrative costs actually climbed by an annual average of 5% between 2005 and 2014 – but this is attributable, in large part, to the especially high refund amounts transferred in 2005.

¹⁰ For example, the Federal Employment Agency is planning to cut around 17,000 jobs by 2019 (based on a headcount of around 107,000 employees at the end of 2014). See Handelsblatt, interview with Federal Employment Agency Executive Board member Heinrich Alt, 7 April 2015, p 5.

Labour market-related government expenditure, recipients of benefits and gross domestic product



Sources: Federal Ministry of Finance, Federal Employment Agency, Federal Statistical Office and Bundesbank calculations.
¹ Including expiring unemployment assistance in 2005. ² Expenditure by central government and the Federal Employment Agency. ³ Recipients in work ("income boosters") and recipients out of work.
 Deutsche Bundesbank

employed persons or vocational trainees.¹¹ These subsidies were discontinued at the end of 2009, with expenditure totalling an average of just over €1 billion *per annum*. Phased retirement contracts concluded in or after 2010 are no longer subsidised by the Federal Employment Agency, meaning that scarcely any spending will be incurred after the end of 2015.

Revenue

Revenue side dominated by contributions

The Federal Employment Agency's revenue largely comprises contributions from employees subject to social security contributions (share in 2014: 85%). On top of these, there are revenue shares earmarked for insolvency benefit and the winter construction subsidy (5% altogether) and, in particular, central government's aforementioned refunds of administrative costs incurred primarily for supporting unemployment benefit II recipients (8½%).¹²

Revenue patterns mainly shaped by changes in contribution rate

Revenue patterns were shaped, first and foremost, by the gradual reduction in the contribution rate, which was made possible by the positive labour market situation characterised by rising employment subject to social security contributions and shrinking unemployment figures. While remuneration subject to compulsory insurance rose by an annual average of just over 3% between 2005 and 2014, contribution receipts fell by almost 5½% on an annual average. Besides contribution receipts, significant central government grants financed through turnover tax, in particular, have occasionally played a role since 2007. Insolvency benefit contributions have fluctuated highly erratically. Further to the launch of the second economic stimulus package in the crisis year of 2009, the special contribution rate¹³ was raised significantly from 0.1% to 0.41% in 2010 to compensate for a considerable shortfall of around €1 billion. Furthermore, expenditure was expected to remain high in 2010 but turned out to be substantially lower than anticipated. The contribution rate was subsequently set at zero for 2011 in order to run

down the surpluses that had accumulated. By contrast, central government's refunds of administrative costs for recipients of unemployment benefit II climbed very steadily and totalled a volume of almost €3 billion in 2014.

Financial relations between the Federal Employment Agency and the central government budget

In the years up to and including 2006, central government was required to offset any deficits incurred by the Federal Employment Agency with a grant. This last occurred in 2005 (€½ billion), after which the Federal Employment Agency ran up a considerable surplus of €11 billion in 2006 – the first surplus since German reunification.¹⁴ A rule-based central government grant was subsequently introduced in 2007. Following the rise in the standard rate of turnover tax by 3 percentage points, it was planned for the revenue generated from 1 percentage point to be transferred to the Federal

Central government grant revised several times and ultimately abolished

¹¹ Subsidies from the Federal Employment Agency encompass a top-up amounting to 20% of employees' gross part-time remuneration and a top-up to 90% of full-time pension contributions. In addition, top-up amounts are tax-exempt (albeit subject to incremental tax progression).

¹² Some benefit recipients fall under the authority of municipalities with separate responsibility for the unemployed (Optionskommunen). Under the experimental clause in section 6a of the Second Book of the Social Security Code (SGB II), sole and all-encompassing responsibility for the basic allowance for job seekers was transferred to these municipalities (initially 69 but later reduced to just 67) on 1 January 2005. Since 1 January 2012, a further 41 municipalities have been permitted to establish this form of job centre (see the information on the Act on the Further Development of the Organisation of the Basic Allowance for Job Seekers (Gesetz zur Weiterentwicklung der Organisation der Grundsicherung für Arbeitsuchende) in the annex, pp 28-33). These receive separate refunds from central government.

¹³ The contribution rate was set according to each year's financial requirements in the years up to and including 2012 before a fixed contribution rate of 0.15% of insured employees' remuneration was introduced in 2013. Surpluses and deficits arising from the insolvency benefit and the associated contribution are being offset over time via a separate reserve.

¹⁴ Bringing forward the deadline for the transfer of social contributions resulted in social insurance funds receiving almost 13 instead of 12 monthly contributions in 2006. This meant that the Federal Employment Agency recorded one-off windfall receipts estimated at just over €3 billion.

Employment Agency on a permanent basis. At its peak in 2009, this grant constituted no less than almost a quarter of the Federal Employment Agency's total revenue (around €8 billion). The central government grant was initially reduced in 2012 before being abolished altogether in 2013.

Deficit offset replaced by lending where necessary

In parallel with the introduction of this rule-based central government grant, central government ceased to offset deficits from 2007 onwards. Deficits run up by the Federal Employment Agency that cannot be covered by reserves now have to be financed using central government loans that, while non-interest-bearing, are repayable. However, no use has hitherto been made of this bridging mechanism. Reserves totalling almost €18 billion had initially been built up by the end of 2007, which were rapidly depleted once again in 2009 and 2010, leaving a financial shortfall of just over €5 billion in 2010. However, in contravention of the new offsetting rule, this was covered by a non-repayable, one-off central government grant.¹⁵ Reserves were built up again recently (end of 2014: almost €4½ billion).

Reintegration payment likewise eliminated

Conversely, the Federal Employment Agency also made payments to central government. For instance, the implementation of the Hartz IV reform was initially accompanied by the introduction of a compensatory amount based on the number of benefit recipients switching from unemployment benefit I to unemployment benefit II. This totalled €4½ billion in the year of its introduction (2005) before falling to €2 billion by 2007. The compensatory amount was replaced in 2008 by the reintegration payment, which the Federal Employment Agency used to pay half of the costs relating to the basic allowance (reintegration and administration) incurred by central government. The reintegration payment totalled around €5 billion *per annum* up to 2010, after which it shrank significantly to less than €4 billion in 2012. It was abolished together with the central government grant in 2013. In retrospect, the lasting impression one gains of the Federal Em-

ployment Agency – and of other social security funds, too, for that matter – is that financial relations with central government have repeatedly been the subject of *ad hoc*, unsystematic interference. At the current juncture, central government no longer makes any significant financial contribution towards unemployment insurance.

Labour market-related expenditure by central, state and local government

Basic allowances for job seekers

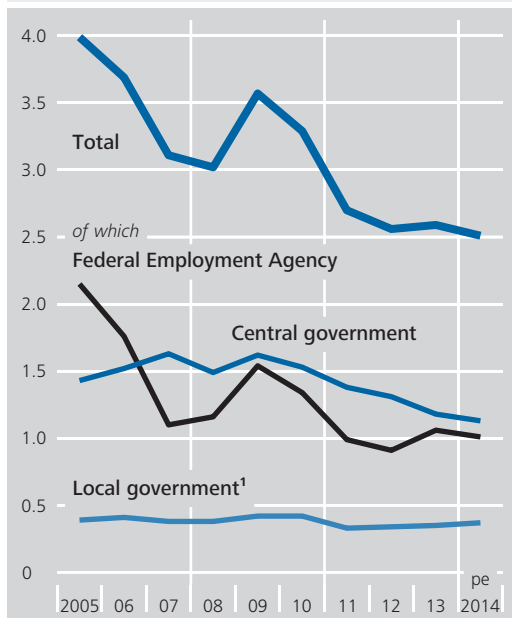
While the Federal Employment Agency essentially represents a contributions-based insurance against the financial repercussions of unemployment by providing insured persons with temporary wage substitutes, means-tested benefits ensuring subsistence are paid out of the central, state and local government budgets. In 2005, the Hartz IV reform combined the benefits of income-based unemployment assistance and social assistance for persons able to work to create the basic allowance for job seekers. As was previously the case for social assistance, the beneficiaries here are not only unemployed persons or persons able to work who are temporarily unavailable to the labour market, but also persons in work whose income is below the basic allowance. Persons who are generally able to work but are in need of financial assistance receive unemployment

Tax-financed basic allowance for persons able to work and their dependants

¹⁵ With respect to the debt brake, the lending facility envisaged since 2007 has not increased the relevant central government deficit as these loans are factored out as financial transactions. As loan repayment only falls due when the Federal Employment Agency has sufficient own funds, this regulation tends to accord some leeway for debt financing and, therefore, provide a way of circumventing the constitutional rule on new borrowing. Due to a one-off grant nevertheless being provided in 2010, the starting deficit to be gradually reduced by central government in subsequent years was higher. The structure chosen therefore granted additional scope for credit financing in later years. See also Deutsche Bundesbank, Federal budget for 2010 and scope for borrowing up to 2016, Monthly Report, February 2010, pp 72-73.

Labour market-related expenditure by levels of government

As a percentage of GDP



Sources: Federal Ministry of Finance, Federal Employment Agency, Federal Statistical Office and Bundesbank calculations. Adjusted for transfers between federal states. ¹ Including the local governments of the city states of Berlin, Bremen and Hamburg. Not including transfers from state governments resulting from the savings in connection with the Hartz IV reform. Deutsche Bundesbank

and services (70%) and net wages and salaries (30%). Over time, the options to top up earnings were notably expanded as well; at the same time, however, the sanctions, too, were tightened to strengthen the incentives to take up employment. In addition, the conditions for drawing the additional children's allowance were eased in 2008, sending the number of recipients sharply higher as well.¹⁸ Lastly, 2011 saw the creation of an education and integration package for children and adolescents as part of the reform of standard financial needs under unemployment benefit II.

Central, state and local governments also fund active labour market policy measures, albeit to a somewhat lesser extent than the Federal Employment Agency. Central government, for example, pays for reintegration benefits for recipients of unemployment benefit II and for other adjustment assistance or job creation schemes. Until 2012, central government also shouldered some of the Federal Employment Agency's expenditure by way of the rule-based grant. Originally it was the state governments of eastern Germany, in particular, which made greater use of their own budgets, co-financed in part by the European Social Fund, to support recipients of social assistance who were able to work and to ease the burden on local governments. When the Hartz IV reform was implemented, the state governments practically discontinued their active labour market policy measures, confining their activities to regionally-specific supplementary measures.

Active labour market policy measures and Federal Employment Agency grant

benefit II; cohabiting dependants who are unable to work receive a social allowance.¹⁶ A further needs-based, labour market-related benefit not covered by the basic allowance is added in the form of an additional children's allowance (see also the box on page 15).

The basic allowance for job seekers has been the subject of numerous statutory adjustments. The (maximum) standard monthly rate for unemployment benefit II (for single households) has climbed since its introduction in 2005 from €345 in western Germany (€331 in eastern Germany until 2006) to a uniform €399 in 2015.¹⁷ This rise by an average of 1½% *per annum* was, in particular, attributable to the legislative changes made in 2011 following a ruling by the Federal Constitutional Court. The standard financial needs, which were subsequently raised slightly and nuanced rather more clearly, are now re-evaluated in a more systematic manner every five years or so and adjusted annually in line with the prices of basic goods

Benefits and options to top up earnings expanded over time

¹⁶ Pursuant to sections 7 and 8 of the Second Book of the Social Security Code (SGB II) persons who are above the age of 15 and are, for the foreseeable future, not unable to work at least three hours daily due to sickness or disability are deemed able to work.

¹⁷ The current monthly standard financial need pursuant to section 20 of the Second Book of the Social Security Code (SGB II) amounts to €399 for single households or single parents as well as persons of age with underage partners without sufficient own income. For household members (without sufficient own income), an extra €360 is added for each partner of age, €320 for 18 to 25-year-old children, €302 for 14 to 18-year-old children, €267 for 7 to 14-year-old children and €234 for children under the age of seven.

¹⁸ The monthly additional children's allowance currently amounts to up to €140 per child (under the age of 25).

Labour market-related expenditure by central and local government							
€ billion							
Item	2005	2010	2011	2012	2013	2014	2014 versus 2005 ¹
Central government							
Unemployment assistance	1.5	–	–	–	–	–	.
Basic allowance for job seekers, <i>of which</i>	35.2	35.9	33.0	31.8	32.2	32.0	– 1.0
Unemployment benefit II/social allowance	25.0	22.2	19.4	19.0	19.5	19.7	– 2.6
Contribution to accommodation costs	3.5	3.2	4.9	4.8	4.7	4.2	1.8
Reintegration benefits	3.6	6.0	4.4	3.8	3.5	3.4	– 0.5
Refunds of administrative costs	3.1	4.4	4.3	4.2	4.5	4.7	4.9
Children's allowance	0.1	0.4	0.4	0.4	0.4	0.4	14.7
Other active labour market promotion measures (adjustment assistance, job creation schemes)	0.7	0.3	0.4	0.4	0.5	0.5	– 3.6
Grants to Federal Employment Agency ²	–	7.9	8.0	7.2	0.2	–	.
Total	37.5	44.6	41.8	39.7	33.3	32.9	– 1.5
Adjusted for compensatory amount/reintegration payment by Federal Employment Agency	33.0	39.3	37.3	35.9	33.3	32.9	– 0.0
Local government³							
Basic allowance for job seekers, <i>of which</i>	12.5	14.0	13.8	13.6	14.0	14.3	1.5
Accommodation costs	12.3	13.8	13.6	13.5	13.8	14.1	1.5
Reintegration, other benefits	0.2	0.2	0.2	0.2	0.2	0.2	2.2
Education and integration benefits	–	–	–	0.4	0.5	0.5	.
Total	12.5	14.0	13.8	14.1	14.5	14.8	1.9
Adjusted for central government contribution to accommodation costs	9.0	10.8	9.0	9.2	9.8	10.6	1.9

Sources: Federal Ministry of Finance, Federal Employment Agency, Federal Statistical Office and Bundesbank calculations. 1 Annually, as a percentage. 2 Excluding deficit offset by central government up to and including 2005 and again in 2010. 3 2014 partly estimated. Not including transfers from state governments resulting from the savings in connection with the Hartz IV reform.

Deutsche Bundesbank

Financial responsibilities in the context of the basic allowance

With regard to financial responsibility, central government not only refunds the administrative costs of the Federal Employment Agency and the municipalities with separate responsibility for the unemployed and covers its own active labour market policy measures, as described above; it also bears the full cost of financing unemployment benefit II (including the social allowance) and the additional children's allowance. As a rule, local government covers accommodation and heating costs. However, central government also contributes markedly to these costs by assuming a variable annual share, which differs in part from one federal state to the next; in principle, it also funds all the education and integration benefits (which are also paid out by local government). The resulting percentage share of participation was lifted again this year to provide general relief for local government budgets and now stands at an average of around 36% across Germany (compared with 29% in the starting year of 2005; see also the annex on legislative

changes on pages 28 to 33). On top of this, local governments receive transfers (which are not mentioned here) from the state governments that are generally oriented to the amount which the state governments saved as a result of the Hartz IV reform being introduced and the housing allowance being scrapped for persons able to work.

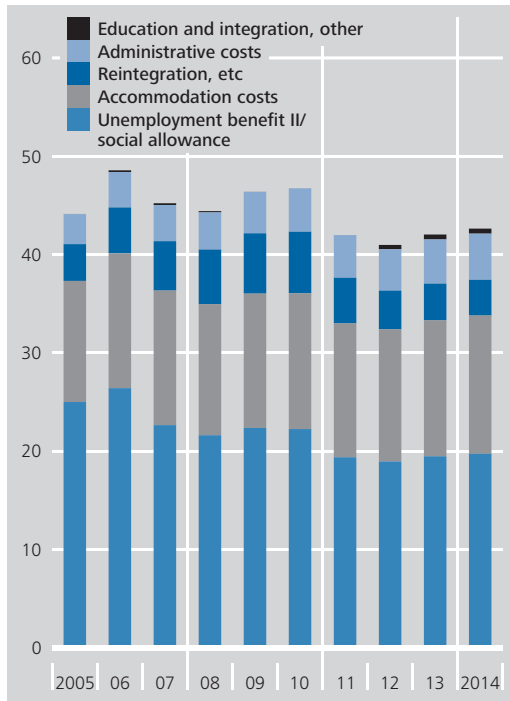
Expenditure patterns

Labour market-related expenditure by central government captured here (not including spending to offset the Federal Employment Agency's deficit) amounted to €23 billion in 2004 and grew when the Hartz IV reform was introduced in 2005, initially jumping to €33 billion net (1½% of GDP; adjusted for payments by the Federal Employment Agency, but including contribution to local government accommodation costs). (Net) expenditure climbed to €41 billion by 2007 but has shrunk perceptibly

Central government expenditure sharply higher initially following Hartz IV reform, but considerable decline since 2007

Expenditure on basic allowance for job seekers

€ billion



Sources: Federal Ministry of Finance, Federal Employment Agency, Federal Statistical Office and Bundesbank calculations. Deutsche Bundesbank

since 2011 to €33 billion (just over 1% of GDP) at the current end (see also the table on page 23). Thus, current expenditure as a percentage of GDP is barely higher than in 2004, ie before the HartzIV reform entered into force. However, compared with the first few years after the reform, there has been a distinct decline.

Unemployment benefit II hardly affected by economic cycle

This development is, *inter alia*, attributable to the largest expenditure item, ie unemployment benefit II (including social allowance), which, having peaked in 2006, declined by an annual average of 3½% to stand at around just over €19½ billion in recent years. Unlike unemployment benefit I, unemployment benefit II is hardly affected by cyclical influences. Generally speaking, poverty under unemployment benefit II is of a structural nature, and fundamental aspects, such as qualifications or family circumstances, play more of a role in determining the need for assistance. Such factors may also be relevant for employed persons, entitling them to draw supplementary benefits.

Expenditure on unemployment benefit II was generally increased through the aforementioned statutory adjustments to the basic allowance benefits. However, this was offset by statutory changes such as the discontinuation of pension contributions for recipients of the basic allowance, but above all by the distinct trend decline in the number of unemployment benefit II recipients (persons able to work but in need of financial assistance). Since rising immediately in the wake of the HartzIV reform and peaking at 5½ million recipients in 2006,¹⁹ the number of recipients dwindled steadily – even during the financial and economic crisis – and from 2012 stabilised at under 4½ million recipients. Together with social allowance recipients, where the decline was somewhat less pronounced, the overall number of recipients drawing these basic allowance benefits has fallen from 7½ million in 2006 to 6 million of late. In this context, the average monthly amount of benefits received by each household in need has decreased from €560 since 2005 to just under €500 of late, which may, *inter alia*, be attributable to pension contributions being scrapped and the reduced share of households with unemployed persons. Unemployment benefit II reflects the decline in unemployment in that unemployed persons as a proportion of the number of persons able to work drawing benefits is down sharply from 55% in 2005 to around 43% at the current end. The number of benefit recipients who were not unemployed but required benefits to top up their income from employment (which is usually low-income and part-time) remained relatively static at just under 1½ million. Their share of the overall number of persons able to

Higher benefit rates more than offset by lower number of recipients

¹⁹ According to Federal Employment Agency estimates at the time, there were around 4.4 million persons able to work (including dependants able to work) drawing social and/or unemployment assistance at the end of 2004. Added to this was an unknown number of dependants unable to work. As early as January 2005, the number of recipients of unemployment benefit II who were able to work amounted to 4.5 million and recipients unable to work (social allowance) amounted to 1.6 million (see, for example, Federal Employment Agency, Der Übergang von der Arbeitslosen- und Sozialhilfe zur Grundsicherung für Arbeitsuchende, Sonderbericht, August 2005).

work and drawing benefits has increased overall of late and stood at around one-third in 2014. By contrast, the number as well as the percentage share of persons receiving benefits who were not registered as unemployed and who were able to work but temporarily unavailable to the labour market fell meanwhile.²⁰

Other benefits under unemployment benefit II

Central government contributions to local government accommodation costs fluctuated in line with statutory adjustments and amounted to just over €4 billion of late, whereas refunds of administrative costs to the Federal Employment Agency and municipalities with separate responsibility for the unemployed grew by around 5% *per annum* to reach just over €4½ billion. Yet active labour market policy developments played an important role, too. For example, reintegration payments for unemployment benefit II recipients climbed to €6 billion in 2010, only to fall back to their 2005 level of €3½ billion of late.

Local government accommodation costs relatively constant

Local governments²¹ benefited financially from the Hartz IV reform and their overall labour market-related expenditure dropped overall from an estimated €10 billion in 2004 to €9 billion net in 2005 (since then, almost exclusively accommodation costs, adjusted for central government contributions). Spending has since climbed by an annual average of 2% to around €10½ billion in 2014, although the benefit recipient ratios sometimes differ substantially between states and between individual local governments. However, local government expenditure as a percentage of GDP virtually never exceeded ½%. Average monthly refunds to households in need increased perceptibly from €275 to roughly €360. This development is likely to have reflected higher rental and energy prices, particularly in urban areas, where a disproportionate number of benefit recipients reside. The net cost for local government budgets is likely to be somewhat lower still if the savings from the Hartz IV reform forwarded by state governments are taken into account. At the state government level, direct labour market-related expenditure has been

negligible since 2005 due to the elimination of housing allowances and reintegration benefits for persons in need of financial assistance who are able to work.

All in all and from today's perspective, the Hartz IV reform saw a considerable expansion in government spending on social benefits, mainly because the number of recipients increased sharply – but probably also because persons previously entitled to social assistance began drawing these benefits more intensively. Central government initially bore the brunt of the reform, while the burden on local governments was eased. However, in recent years, central government has experienced gradual yet noticeable relief, whereas local government expenditure has trended moderately upwards, somewhat below nominal GDP growth.

Central government initially burdened and later relieved and Hartz IV reform; local governments mostly relieved

■ Conclusions and outlook

The very favourable development in the labour market has perceptibly eased the strain on public finances over the past ten years. Since peaking in 2005, the number of unemployed persons has declined significantly from almost five million to under three million. This development has been reflected in labour market-related public expenditure and made it possible, first, for the Federal Employment Agency's contribution rate to be slashed by more than half; second, it contributed to consolidation at the central, state and local government level. The improvements left more of a mark on the more cyclical items of the Federal Employment Agency's expenditure. However, spending on the basic allowance for job seekers, too, contracted substantially. When unemployment and social assistance were combined in 2005, this drove the number of recipients sharply

Successful labour market developments substantially ease public finances

²⁰ In addition, a small number of persons (around 100,000) were drawing basic allowance benefits supplementing unemployment benefit I.

²¹ Including expenditure by the city states of Berlin, Bremen and Hamburg for accommodation costs.

higher initially, but this figure has been on a steep and steady downward trajectory since 2006. Overall, the number of unemployment benefit II recipients diminished by 1½% *per annum* until 2014. The number of long-term unemployed persons²² appears to have levelled off at around one million since 2011.

Reforms make important contribution to lowering unemployment

There are many reasons for the significant decline in unemployment in Germany. The reforms seen in the past decade were probably a major catalyst – combined with flexibility measures at the firm level, relatively moderate collective labour agreements and improved corporate competitiveness, they are likely to have put the German labour market on the path to success. Particularly noteworthy in this respect are the Hartz IV reforms, which, through more efficient job mediation and stricter means-testing, have ultimately helped drive down unemployment.²³

Substantial financial relief for Federal Employment Agency

In particular the Federal Employment Agency, which is the main institution paying short-term unemployment benefits, reaped the rewards of the very favourable developments in the labour market. Besides reducing its previously high funding deficits, the Federal Employment Agency also succeeded in slashing the contribution rate, which had a positive knock-on effect on employment and growth conditions in Germany. As things stand today, the current contribution rate seems to be just sufficient to finance around one million recipients of unemployment benefit I, assuming the Federal Employment Agency's remaining spending per unemployed person is roughly proportional to its expenditure on unemployment benefit I. Last year, the number of recipients stood at 890,000, and the outlook appears to suggest that their figure will at least stabilise at this low level. That means the Federal Employment Agency would also be able to go without a loan from the central government budget in the medium term, thus enabling it to further boost its general reserves.

As far as the setting of the contribution rate is concerned, it must be borne in mind that the prevailing labour market situation is certainly on the upbeat side and that it would be quite appropriate for the Federal Employment Agency to further boost its reserves. A further cut in the contribution rate should only be considered possible if the present situation in the labour market does, in fact, turn out to be the new structural normal and the low number of unemployment benefit I recipients proves to be sustainable, such that the Federal Employment Agency does not drift into deficit territory over the course of the economic cycle. This would additionally presuppose that strict budgetary discipline is maintained, especially regarding active labour market policy measures, which actually seems rather plausible given that it is probably viewed with some scepticism overall concerning its impact on the prospect of unemployed persons finding new employment, causes "free-rider" effects and can even be counterproductive (eg in the case of job creation schemes), especially considering the financial burdens involved.²⁴ In principle, conducting further reviews of Federal Employment Agency benefits (eg the level of the replacement rate, the period of entitlement to un-

Slight reduction in contribution rate by Federal Employment Agency contingent on favourable labour market situation lasting

²² Persons who have been registered as unemployed for more than one year. Including long-term recipients of unemployment benefit I; excluding recipients of unemployment benefit II who are in work as well as those who are not available to the labour market.

²³ See, for example, M Stops, Revisiting German labour market reform effects, IAB Discussion Paper 2/2015; N Gadsch, N Stähler and B Weigert, German Labor Market and Fiscal Reforms 1999 to 2008: Can They be Blamed for Intra-Euro Area Imbalances?, Working Paper 05/2014, German Council of Economic Experts; T Krebs and M Scheffel (2013), Macroeconomic Evaluation of Labor Market Reform in Germany, IMF Economic Review Vol 61, pp 664-701; M Krause and H Uhlig (2012), Transitions in the German Labor Market: Structure and Crisis, Journal of Monetary Economics, Vol 59, pp 64-79.

²⁴ See G Heyer, S Koch, G Stephan and J Wolff: Evaluation der aktiven Arbeitsmarktpolitik, ein Sachstandsbericht für die Instrumentenreform 2011, IAB Discussion Paper 17/2011, p 29; Deutscher Bundestag, Bericht 2009 der Bundesregierung zur Wirksamkeit moderner Dienstleistungen am Arbeitsmarkt, Bundestagsdrucksache 16/3982 of 21 December 2006; as well as T Büttner, T Schewe and G Stephan, Maßnahmen auf dem Prüfstand, IAB-Kurzbericht 8/2015. What these papers all have in common is that they neglect funding aspects. Hence, it is the effectiveness, but not the efficiency of the promotion measures that is being assessed here.

employment benefit I) offers further potential for lowering the contribution rate; however, this does not appear to be on the agenda at present.

Tax financing of non-insurance-related benefits could further lower contribution rate

Irrespective of this, adequately funding non-insurance-related benefits by the Federal Employment Agency also opens up potential for lowering the contribution rate. As a rule, non-insurance-related benefits allocated by central government should be financed using general tax revenue so that they are not shouldered by contribution payers alone. However, in the past, the allocation of central government grants to the Federal Employment Agency was relatively arbitrary and occasionally gave the impression – as with other social security schemes – that fiscal policymakers shift funding at a whim to suit the cash balance at any given time. As a case in point, the central government contribution was done away with and not replaced in 2013.

Definition of non-insurance-related benefits not undisputed

Although it is probably virtually impossible to make an undisputed and universally applicable distinction between insurance-compliant and non-insurance-related benefits, it would be useful if the legislator were to draw up a detailed list and justify insurance benefits. The identified expenditure could then be financed in the form of a rule-based central government grant so as to move towards relieving contribution payers of the burden of financing tasks which belong to society as a whole and, as a more general initiative, to boost the transparency of the social security system. The Federal Employment Agency itself estimates that non-insurance-related benefits account for around 10% of its expenditure of late, citing above all rehabilitation benefits and preparatory vocational measures for adolescents.²⁵ Together, these benefits involve spending of just over €3 billion, matching the revenue from around 0.3 contribution percentage point. Moreover, benefit rates that differ depending on whether or not the recipient is a parent are somewhat incompatible with the essence of unemployment insurance. Longer-term claims of un-

employment benefit I by older recipients, too, could be regarded more as a separate government transfer than a regular element of an insurance scheme against the risk of unemployment.

The Hartz IV reform and the subsequently agreed amendments to the funding arrangements across the different levels of government placed a significant additional burden on central government and provided a degree of relief for local governments. However, from 2011, central government's labour market-related burdens as a percentage of GDP declined again markedly, while the situation was virtually unchanged at the local government level. In the medium term – given the current labour market outlook and owing to the general indexation of benefits – both central government and local governments can expect no more than moderate growth rates, so burdens will probably change only slightly. At the present time, there is no sign of any further perceptible relief in terms of expenditure on unemployment benefit II, and accommodation costs are likely to follow the essentially upward overall trend in rental prices and energy costs. Additional statutory adjustments to the scope of benefits or other aspects are not envisaged at this stage.

No fundamental change in burden to be expected at central and local government level

Looking ahead, further extending the provision of childcare could potentially further increase labour market participation by numerous recipients of unemployment benefit II, especially single parents, and, thus, ease the strain on labour market-related expenditure. The medium-term impact of the introduction of the minimum wage on public finances cannot yet be gauged precisely. If the minimum wage does not have a persistently and substantially negative impact on employment levels, the burden on central government is more likely to be eased as the need to top up low incomes

Fiscal impact of extending childcare and minimum wage

²⁵ See Federal Employment Agency, Finanzentwicklung in der Arbeitslosenversicherung, Bericht über das erste Quartal 2013, April 2013.

with unemployment benefit II would decline due to the higher wage level and additional tax and contribution income can be expected to be generated. However, if jobs were lost, which

would be a particular concern in the event of sharp increases in the minimum wage in the future, this would also place a strain on public finances.

■ Annex

Major legislative changes concerning labour market policy since 2005 with an impact on finances

Fifth Act Amending the Third Book of the Social Security Code and Other Legislation (*Fünftes Gesetz zur Änderung des SGB III und anderer Gesetze*) (2005)

Extension, until 31 December 2007, of temporary active employment promotion measures and of the option for persons over the age of 58 to claim unemployment benefit I without being available to the labour market.

Phasing out of one-person business start-up grants to unemployed persons (*Existenzgründungszuschuss*) by 30 June 2006.

Act Revising the Exemption Limit Regulations for Persons in Need with the Capacity to Work (*Gesetz zur Neufassung der Freibetragsregelungen für erwerbsfähige Hilfebedürftige*) (2005)

Improvement of options to top up earnings and more generous allowance of income in the calculation of unemployment benefit II.

Act Amending the Fourth and Sixth Books of the Social Security Code (*Gesetz zur Änderung des SGB IV und SGB VI*) (2005)

Bringing forward of the deadlines for the payment of social security contributions from the middle of the following month to the end of the month in which the work is carried out. In the year in which this comes into force (2006), the social security funds record a one-off higher inflow of liquidity.

First Act Amending the Second Book of the Social Security Code (*Erstes Gesetz zur Änderung des SGB II*) (2005)

In 2006, too, central government contributes 29.1% to accommodation and heating costs within the framework of the basic allowance for job seekers.

Act Amending the Second Book of the Social Security Code and Other Legislation (*Gesetz zur Änderung des SGB II und anderer Gesetze*) (2006)

Convergence of the standard rate of unemployment benefit II for eastern Germany with the level in western Germany (€345 per month).

Extension of income-support households to include unmarried children under the age of 25 living in the household.

As of 2007, virtual halving of pension insurance contributions paid by central government on behalf of recipients of unemployment benefit II.

Act Promoting Year-round Employment (*Gesetz zur Förderung der ganzjährigen Beschäftigung*) (2006)

As of the 2006-07 period of bad weather, the newly implemented seasonal short-time working benefits replace the promotion of winter construction previously in place. Seasonal short-time working benefits are granted as of the first working hour lost and financed from contributions to the Federal Employment Agency. Previously, the first 30 hours were covered by the individual working time account and, beyond that, the winter compensation payments were financed by means of the winter construction levy paid by employers in the construction sector. Only after this was the Federal Employment Agency responsible for providing funds.

The refunding of employers' contributions to the social security funds and the compensation for additional costs incurred when working in winter (*Mehraufwands-Wintergeld*) or the allowance for hours taken as flexitime (*Zuschuss-Wintergeld*) are financed by means of a levy to which employees in the construction sector are also to make a contribution for the first time.

Act Accompanying the 2006 Budget (*Haushaltsbegleitgesetz 2006*) (2006)

Lowering of the contribution rate to the Federal Employment Agency from 6.5% to 4.2% as of 1 January 2007. The rate was initially envisaged to be cut to 4.5%. However, as a result of the Act to Lower the Contribution for the Promotion of Employment and to Determine Contribution Rates in the Statutory Pension Insurance Scheme and Contributions and Contribution Grants for Agricultural Pensions for 2007 (*Gesetz über die Senkung des Beitrags zur Arbeitsförderung, die Festsetzung der Beitragssätze in der gesetzlichen Rentenversicherung und der Beiträge und Beitragszuschüsse in der Alterssicherung der Landwirte für das Jahr 2007*), the lower contribution rate is adopted in the Act Accompanying the Budget.

As of 2007, central government pays a rule-based grant to the Federal Employment Agency, which is to amount to the revenue generated from one percentage point of the rise in the standard rate of VAT on 1 January 2007 (from 16% to 19%) and, as of 2010, is to be extrapolated at the rate of change in the VAT assessment basis.

As of 2007, any central government liquidity assistance remaining at the end of the year is no longer converted to non-repayable grants but takes the form of interest-free central government loans to the Federal Employment Agency that are to be repaid in years when the economy is in better shape.

Lowering of health insurance contributions paid by central government on behalf of recipients of unemployment benefit II.

Act on the Further Development of the Basic Allowance for Job Seekers (*Gesetz zur Fortentwicklung der Grundsicherung für Arbeitsuchende*) (2006)

Expansion of small employment opportunities for job seekers, closer examination of benefit abuse, more targeted sanctions.

Bridging payments and one-person business start-up grants to unemployed persons are combined into new start-up grants for unemployed persons wishing to become self-employed.

Act Amending the Second Book of the Social Security Code and the Act on Financial Equalisation (*Gesetz zur Änderung des SGB II und des FAG*) (2006)

To provide local government with appropriate relief, central government's contribution to accommodation and heating costs for 2007 is adjusted and differentiated according to federal state (Baden-Württemberg 35.2%, Rhineland-Palatinate 41.2%, other states 31.2%²⁶). As of 2008, the central government grant is to be changed by law using an adjustment formula based on the development of the number of income-support households. A fundamental review of central government's contribution is scheduled for 2010.

Second Act Amending the Second Book of the Social Security Code (*Zweites Gesetz zur Änderung des SGB II*) (2007)

Implementation of new labour market policy measures for the long-term unemployed who are particularly difficult to place (in particular, employment grants for employers).

²⁶ At that time, Baden-Württemberg and Rhineland-Palatinate had a disproportionately low number of recipients of SGB II benefits meaning that, overall, local government would have received less relief if a standard contribution rate had been introduced for the whole of Germany.

Sixth Act Amending the Third Book of the Social Security Code and Other Legislation (*Sechstes Gesetz zur Änderung des SGB III und anderer Gesetze*) (2007)

Lowering of the contribution rate to the Federal Employment Agency from 4.2% to 3.3% as of 1 January 2008.

As of 1 January 2008, the Federal Employment Agency makes a reintegration payment to central government to cover half of its expenditure on labour market reintegration benefits and half of its administration costs for the basic allowance for job seekers. The compensatory amount levied previously (for recipients of unemployment benefit I switching to unemployment benefit II) is abolished.

Transfers from the Federal Employment Agency are to be paid into a pension fund administered by the Bundesbank, enabling a capital stock to be accrued from which pensions to the Agency's remaining civil servants are to be paid.

Third Act Amending the Second Book of the Social Security Code (*Drittes Gesetz zur Änderung des SGB II*) (2007)

Adjustment of central government's contribution to accommodation and heating costs for 2008 (Baden-Württemberg 32.6%, Rhineland-Palatinate 38.6%, other states 28.6%).

Seventh Act Amending the Third Book of the Social Security Code and Other Legislation (*Siebttes Gesetz zur Änderung des SGB III und anderer Gesetze*) (2008)

For new cases from 1 January 2008 onward, the general maximum period of entitlement to unemployment benefit I no longer rises from 12 to 18 months from the age of 55, but to 15, 18 or 24 months, respectively, from the age of 50, 55 or 58.

Recipients of unemployment benefit II who have reached the age of 58 and have not received an offer of employment subject to social security contributions for one year are no longer included in the unemployment figures.

Pension Adjustment Act (*Gesetz zur Rentenanpassung*) (2008)

Raising of the standard rates for the basic allowance for job seekers and social assistance to €351 per month in line with the change in the current pension level.

Fourth Act Amending the Second Book of the Social Security Code (*Viertes Gesetz zur Änderung des SGB II*) (2008)

Lifting of the original 2010 time limit on central government's contribution to accommodation and heating costs.

Act Amending the Federal Child Benefit Act (*Gesetz zur Änderung des Bundeskindergeldgesetzes*) (2008)

Changes to the additional children's allowance, in particular lowering of the minimum income limit and extension of the period of entitlement.

Eighth Act Amending the Third Book of the Social Security Code and Other Legislation (*Achtes Gesetz zur Änderung des SGB III und anderer Gesetze*) (2008)

Lowering of the contribution rate to the Federal Employment Agency from 3.3% to 3.0% as of 1 January 2009.

Act Revising Labour Market Policy Measures (*Gesetz zur Neuausrichtung der arbeitsmarktpolitischen Instrumente*) (2008)

Further development of active labour market policy measures (including reintegration measures within the framework of the basic allowance for job seekers).

Fifth Act Amending the Second Book of the Social Security Code (*Fünftes Gesetz zur Änderung des SGB II*) (2008)

Adjustment of central government's contribution to accommodation and heating costs for 2009 (Baden-Württemberg 29.4%, Rhineland-Palatinate 35.4%, other states 25.4%).

Family Benefit Act (*Familienleistungsgesetz*) (2008)

Implementation of a school package providing additional benefits for children of recipients of unemployment benefit II each school year as of 2009.

Act on Securing Employment and Stability in Germany (*Gesetz zur Sicherung von Beschäftigung und Stabilität in Deutschland*) – Second Economic Stimulus Package (2009)

Lowering of the contribution rate to the Federal Employment Agency from 3.0% to 2.8% as of 1 January 2009, and raising it back up to 3.0% as of 1 January 2011.

Specific regulations stipulating that repayment of central government's interest-free loans to offset the Federal Employment Agency's deficit will be deferred until the Agency again records surpluses at the given contribution rate.

In 2009 and 2010, the Federal Employment Agency is to refund half of the employer's share of social security contributions for recipients of short-time working benefits; if the firm provides training measures, the employer's share is to be refunded in full.

Expansion of active labour market policy measures.

Raising of benefits for children of recipients of unemployment benefit II aged between 6 and 13 (from 60% to 70% of the standard rate) for the period from 1 July 2009 to 31 December 2011.

Third Act Amending the Fourth Book of the Social Security Code and Other Legislation (*Drittes Gesetz zur Änderung des SGB IV und anderer Gesetze*) (2009)

As of the seventh calendar month, the employer's share of social security contributions for recipients of short-time working benefits is to be refunded in full irrespective of any other requirements.

Social Security Stabilisation Act (*Sozialversicherungs-Stabilisierungsgesetz*) (2010)

In a departure from the general repayment obligations, the Federal Employment Agency's loan re-

quirements are converted to a non-repayable central government grant on a one-off basis in 2010.

Under unemployment benefit II, the property exemption limits ("protected means") for old-age provision are raised.

Act on the Further Development of the Organisation of the Basic Allowance for Job Seekers (*Gesetz zur Weiterentwicklung der Organisation der Grundsicherung für Arbeitsuchende*) (2010)

Following the Federal Constitutional Court's ruling of December 2007, job centres in the form of joint institutions, comprising both local employment agencies and municipal authorities, are set up to carry out tasks related to the basic allowance for job seekers. At the same time, further job centres in the form of *Optionskommunen* – where the municipal authority has sole responsibility – are approved, with the total number rising from 67 to 108 as at 1 January 2012 (a maximum of 25% of all job centres).

Employment Opportunities Act (*Beschäftigungschancengesetz*) (2010)

Extension of temporary special regulations for short-time working benefits until 31 March 2012.

Extension of temporary regulations for expanding active labour market policy measures.

Act Accompanying the 2011 Budget (*Haushaltsbegleitgesetz 2011*) (2010)

Discontinuation of the pension insurance obligation for recipients of unemployment benefit II and thus also of central government's contributions to pension insurance.

Discontinuation of the temporary surcharge when switching from unemployment benefit I to unemployment benefit II.

Inclusion of parental benefit in future calculations of entitlement to unemployment benefit II, social assistance and the additional children's allowance.

Sixth Act Amending the Second Book of the Social Security Code (*Sechstes Gesetz zur Änderung des SGBII*) (2010)

Adjustment of central government's contribution to accommodation and heating costs for 2010 (Baden-Württemberg 27%, Rhineland-Palatinate 33%, other states 23%).

Seventh Act Amending the Second Book of the Social Security Code (*Siebttes Gesetz zur Änderung des SGBII*) (2011)

Adjustment of central government's contribution to accommodation and heating costs for 2011 (Baden-Württemberg 28.5%, Rhineland-Palatinate 34.5%, other states 24.5%).

Act on Calculating Standard Requirements and Amending the Second and Twelfth Books of the Social Security Code (*Gesetz zur Ermittlung von Regelbedarfen und zur Änderung des SGBII und SGBXII*) (2011)

Following the Federal Constitutional Court's ruling of February 2010, the standard requirements for the basic allowance for job seekers (as well as the assistance for living expenses (social assistance) and the basic allowance for the elderly and for persons with reduced earning capacity pursuant to SGBXII) are recalculated as at 1 January 2011. The six new levels of standard requirements range between €213 (for children under the age of six) and €364 (for single adults) per month. They are calculated on the basis of the sample survey of income and expenditure (which is carried out every five years) and extrapolated each year using a mixed index comprising the price developments of goods and services relevant for the standard requirements (70%) and the development of net wages and salaries per employee (30%).

In addition, new benefits for education and participation for schoolchildren are introduced on 1 January 2011 as part of the basic allowance for job seekers and social assistance. To finance these benefits provided by local government, central government's contribution to accommodation costs is raised and adjusted each year in line with the development of expenditure on education and participation.

Act Increasing the Financial Capacity of Local Government (*Gesetz zur Stärkung der Finanzkraft der Kommunen*) (2011)

Discretionary cut to the rule-based central government grant to the Federal Employment Agency in 2012 (according to central government's financial plan, the grant will be virtually halved by 2014).

Act Improving Reintegration Opportunities on the Labour Market (*Gesetz zur Verbesserung der Eingliederungschancen am Arbeitsmarkt*) (2011)

The labour market policy measures in SGBIII and SGBII are revised and more closely integrated. The legal right to the start-up grant is abolished, among other things.

Act Accompanying the 2013 Budget (*Haushaltsbegleitgesetz 2013*) (2012)

The reintegration payment, by means of which the Federal Employment Agency covers half of central government's expenditure on reintegration benefits and administration costs for the basic allowance for job seekers, is discontinued as of 2013.

Central government's grant to the Federal Employment Agency, which is calculated on the basis of VAT revenue, is also discontinued as of 2013.

Act Strengthening Free Collective Bargaining (*Gesetz zur Stärkung der Tarifautonomie*) (2014)

A general minimum wage of €8.50 gross per hour comes into force on 1 January 2015. The Federal Government is to adjust the amount every two years – starting on 1 January 2017 – by way of a statutory order based on recommendations by a standing committee (comprising employee and employer representatives).

Act Providing Further Relief for State and Local Government as of 2015 etc (*Gesetz zur weiteren Entlastung von Ländern und Kommunen ab 2015 etc.*) (2014)

To implement the coalition agreements, central government eases the financial burden on local govern-

ment by €1 billion per year between 2015 and 2017. Half of this relief is provided in the form of a 3.7 percentage point increase in central government's contribution to accommodation and heating costs (Baden-Württemberg 35.3%, Rhineland-Palatinate 41.3%, other states 31.3%).