

## Changes in the governance of employment services in Germany since 2003

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Institut für Arbeitsmarkt-  
und Berufsforschung

Die Forschungseinrichtung der  
Bundesagentur für Arbeit

IAB

# IAB-Discussion Paper

10/2008

Beiträge zum wissenschaftlichen Dialog aus dem Institut für Arbeitsmarkt- und Berufsforschung

## Changes in the governance of employment services in Germany since 2003

Regina Konle-Seidl

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Regina Konle-Seidl (IAB)

Mit der Reihe „IAB-Discussion Paper“ will das Forschungsinstitut der Bundesagentur für Arbeit den Dialog mit der externen Wissenschaft intensivieren. Durch die rasche Verbreitung von Forschungsergebnissen über das Internet soll noch vor Drucklegung Kritik angeregt und Qualität gesichert werden.

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## Abstract

Institutional changes in the governance of employment services were the starting point of comprehensive labour market and social policy reforms – the so-called Hartz-reforms (2003-2005) – in Germany. Particularly with the Hartz IV reform in 2005 Germany's status- and occupation-oriented social protection regime has been relinquished for a larger share of dependent population. At the interface of labour market and social policy high shares of means-tested income support recipients are going to be activated now. In line with similar developments in other countries the challenge for Germany's public employment and social services is the jointly managing of activation measures and income support policies in order to increase employment and to avoid exclusion. To deal with this challenge several European countries have set up "single gateways" and "one-stop shops" by merging the administration of different income support schemes (unemployment, work disability, social assistance) with employment and welfare services. The changes in the realm of employment services in Germany, however, follow a different path. Instead of implementing a single gateway for all unemployed and inactive working age people a two-tier or even three-tier system was created: Public Employment Service (PES) offices for short-term unemployed and joint agencies combining former local PES and municipal social assistance (ARGEn) for recipients of the basic income support. This new structure of administrative bodies, a result of protracted federal negotiations, created governance problems and hampers an effective activation strategy for potential long-term unemployed. The paper aims at a preliminary assessment of the effects of changing governance in employment services and sets out probable paths of future adaptation to arrive at more coherent activation strategies for all employable persons on income support.

**JEL classification:** D 78; J78

**Keywords:** governance of labour market policy, activation, public employment service, contracting out

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## 1 Introduction

Activation of labour market and social policy are one of the corner stones of making welfare states more sustainable by promoting labour market participation of benefit recipients out of work. However, activating welfare states is not only a question of "what" in terms of de-commodification, retrenchment or workfare but also linked to changing forms of governance in welfare policies.

"How" to implement activation policies is a core concern in understanding the full effects of labour market and welfare reforms. In discussion of activation policies, it seems by now to be widely accepted that the success of activation policies depends at least partly on effective working relations between public actors implementing the policy in job centres or welfare offices, the local and regional community and the individuals that are going to be activated. Governance, then, refers to a set of organisational or managerial forms and processes by re-shaping relationships between various actors and institutions and by introducing new ways of steering and running public institutions<sup>1</sup>.

Instruments of a New Welfare Governance named in all the concepts that outline a shift of the present welfare state paradigm are quite similar. They include processes of territorial or functional decentralisation and the introduction of a split between those who provide services and those who purchase or use them. Moreover, competition or networking mechanisms in the provision of public services and the involvement of 'other actors' in the provision of services are as well on the agenda as the empowerment of service users' vis-à-vis service providers.

In Germany as well as in many other countries an increasing focus on individualised, personalised and tailor-made service provision and the introduction of new tools for the management of public institutions like performance targets and monitoring can be observed. Introducing forms of New Governance and New Public Management (NPM) is expected to contribute to the realisation of activation objectives. It is said to reduce public expenditure, to increase the quality of public services and the responsiveness of the agencies delivering them, to improve the effectiveness and efficiency of policy programmes, and to promote the choice of the users of public or publicly financed services.

Earlier studies (e. g. Clarke et al., 2000) have demonstrated that the way in which public policy is administered significantly contributes to the nature and effects of the welfare state, particularly to citizen-state relations. In promoting the successfulness of social policies the provision and delivery has to be considered in connection with the organization and management of this process. Substantial policy changes and governance changes therefore could be considered as complementary and mutual reinforcing. However, in the proliferation of comparative welfare studies, the implementation and governance side has received less attention.

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<sup>1</sup> A good overview of international trends in administrating welfare governance provide the volume edited by Paul Henman and Menno Fenger (2006) and the book on "Contractualism in Employment Services" edited by Els Sol and Mies Westerveld (2005).

This paper tries to link the changes in the German welfare system and service provision since 2003 with new forms of governance of activation policies introduced with the First to Fourth Law for Modern Services on the Labour, the so-called Hartz-reforms. The paper focuses on the changing relationship between the different agents and institutions responsible for the implementation of welfare policy (Federal and *Länder* governments, municipalities, social partners, public and private providers, PES staff and clients). It does not provide, however, an in-depth analysis of street-level practice within employment agencies. The analysis is based on legal provisions, internal PES documents and (preliminary) results of a comprehensive evaluation mandate linked to the recent reforms.

The remainder of this paper is structured in three parts: Chapter two describes the major changes in the German social protection system and the shift to activation since 2003. Chapter three gives an insight into the fundamental changes in the delivery of employment services. The last chapter provides a preliminary assessment of changing governance in employment services based on microeconomic evaluation results as well as on a descriptive analysis of reform objectives and outcomes.

## 2 Changes in the German welfare system

In Germany comprehensive welfare reforms were not on the agenda until 2003, when the government announced the 'Agenda 2010', a programme of fundamental economic and social policy reforms designed to re-invigorate the stagnating German economy and to ensure the long-term stability of the social system. Especially the enactment of Hartz I-IV stated a milestone in the evolution of the German labour market regime as well as on the welfare state in general. For a long time Germany was characterised as a country unable to proceed with the pressing reforms needed to react to declining economic performance. In general, the German crisis of stagnation was ascribed to 'ingrained over-commitment to old institutions and historical entitlements' (Kitschelt/Streeck, 2003). The Hartz reforms are seen as the most ambitious German reform project in social policy since World War II to overcome "a frozen welfare state".

In 2002 a partial labour market reform was designed by the Hartz Commission and put into practice as of 1 January 2003. The commission named after its chairman Peter Hartz was set up by the government following a 'placement scandal' within the German PES, the *Bundesanstalt für Arbeit* (BA)<sup>2</sup>. The proposals of the Commission were enacted by the First to Fourth Law for Modern Services on the Labour Market and came into force between 2003 and 2005 (table 1).

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<sup>2</sup> In February 2002 the Federal Audit Court discovered that the placement statistics of the BA were wrongly reported. As a result of the report the government presented a reform plan not only to modernise the BA but to introduce some important changes in the institutional framework for employment and labour market policy.

**Table 1**  
**The four laws on "Modern Services on the Labour Market" (Hartz I-IV)**

Hartz I 2003	Redesign and introduction of new ALMP measures, closer targeting
Hartz II 2003	Reform of mini-jobs and new start-up program (Me-Inc.); deregulation of temp-agency work /TWA)
Hartz III 2004	Reorganisation of PES (BA) according NPM principles
Hartz IV 2005	Merging of two tax-financed, means-tested welfare benefit schemes to the new "basic income support for able-bodied jobseekers"
	Creation of a second tier service provision for welfare clients (i.e. long-term unemployed)

The government's willingness to implement the Hartz proposals in a comprehensive way implied further clarification of crucial issues such as the level of the unified benefit for long-term unemployed that was to replace unemployment assistance and social assistance for people capable of working (*erwerbsfähig*) by a means-tested "basic income" system. With the "Agenda 2010" presented in March 2003 it became clear that the government would opt for a flat-rate benefit with about the same level as social assistance thus effectively severing the link with prior earnings. This was to be implemented with the fourth Hartz Act (Hartz IV) in January 2005. In addition, the government announced shortening unemployment insurance benefit duration for older workers from 32 to 18 months and other elements of labour market deregulation<sup>3</sup>.

This sequence of rather "harsh" reforms that were perceived as a break with traditional social policy approach to labour market problems provoked broad public unrest that resulted in a significant decline in political support for the red-green coalition, in particular for the Social Democrats, the emergence of a new left-wing party and the electoral defeat of the red-green coalition in autumn 2005. Although the increase in open unemployment figures<sup>4</sup> did not mean a substantial increase in broad unemployment, it was perceived as a major policy failure and the proof of the fact that the Hartz reforms did not work. Moreover, as the new unemployment benefit II (UB II; see table 2) is primarily designed to prevent poverty and not to secure previous living standards, Hartz IV became the symbol for a policy that was seen as a break with the principle of "the social insurance state" of providing status-oriented benefits while imposing only limited demands on unemployed.

<sup>3</sup> By Jan 2008 the maximum UB I duration for older unemployed has been re-extended from 18 to 24 months. The announcement of having longer UB I benefit periods for older workers has proven to be highly popular given the widely shared perception of a "savings account logic" embedded in this scheme.

<sup>4</sup> The number of registered unemployed exceeded in February 2005 5 million for the first time in Germany. However, this was mainly a statistical effect as many social assistances recipients and the non-working partners of former benefit claimants were now obliged to register as unemployed. Therefore, a large number of former "inactive" benefit recipients were counted in January 2005 in the unemployment statistics.



However, contrary to widespread beliefs ("poverty by law") and although a flat rate benefit, UB II is not in general lower than means-tested benefits prior to the Hartz IV reform. This holds for virtually all former social assistance beneficiaries, but also for a relevant share of former unemployment assistance recipients. Household income of lone parents, families with many children and low-wage earners – the winners of the reform – increased on average between 18 per cent and 30 per cent (Becker/Hauser 2006, Rudolph/Blos 2005). The broad rejection of the Hartz IV-reform is therefore rather a consequence of a fundamental deficit in legitimating the "hidden" or silent shift from a social insurance state to a welfare state dominated by basic income support and stronger activation (Konle-Seidl et al. 2007).

## 2.1 Structural changes in the benefit system

Before 2005 unemployed people – after exhausting the unemployment insurance benefit – could apply for unemployment assistance which was still related to previous earnings but on a lower level. Although unemployment assistance was tax-funded, it was seen as a prolongation of unemployment insurance benefit. To secure social status and the acquired standard of living, the unemployment benefit and the previous unemployment assistance referred to the former income. The duration of the contribution based unemployment benefit varied strongly according to age.

In the old system, a person becoming unemployed was entitled to unemployment insurance benefits for a certain period if he/she had an employment record of at least one year during the past three years. This benefit initially amounted to more than two thirds of the previous income with an in-built ceiling in accordance to the "equivalence principle", and thus "rewarded" prior earnings and effort. The higher an individual's achievements during his or her employment career, the higher the benefits. Older workers with a longer employment record could rely on extended unemployment insurance benefits.

Persons relying on unemployment insurance benefits could also benefit from heavy investment in "enabling" active labour market policy schemes. These programs were not primarily used in the sense of "right and duty"- schemes but as instruments to stabilize human capital and restore benefit claims. Hence, removing occupational protection (as early as in 1997), but more specifically, shortening benefit duration in unemployment insurance for older workers and abolishing earnings-related unemployment assistance means a departure from status protection and the strong reliance on the insurance principle and the equivalence of contributions and benefits. Both – unemployment assistance and contribution-based unemployment insurance benefit – implied a status of "worker citizenship" or "social security citizenship" rather than "social citizenship" by being restricted to persons able to work (Ludwig-Mayerhofer, 2005).

By January 1, 2005 unemployment assistance and social assistance became integrated into one single means-tested scheme, the "basic income scheme for needy jobseeker". Basic income can be received in all cases of need where resources from work and other income are not sufficient to pass the threshold income set by law. Although it has a strong focus on the labour

market the new benefit scheme is foremost a genuine social policy programme to avoid poverty. Hence, basic income support does not only focus on registered unemployed without entitlements to unemployment insurance benefits, but also on people in school and training or in dependent employment if they pass the means-test. The same holds for self-employed. In contrast to former social assistance, UB II recipients are covered by both statutory health insurance and old-age pension insurance which also means that self-employed can receive health insurance coverage at a low premium under UB II. In January 2005, 97 percent of former social assistance have been assessed as "capable of working" and consequently transferred from municipal responsibility to the new basic income support scheme financed out of taxes at the Federal level.

Table 2 shows the main differences between the old and the new benefit system. The new benefit is paid out for people capable of working as unemployment benefit II (UB II). The scheme is funded by taxes. The amount is need-based. UB II is also paid if the person in need of assistance has not paid contributions to social insurance. It is paid if and as long as need exists. Besides UB II, the new basic income scheme provides social allowance (*Sozialgeld*) to persons who live together with needy persons capable of working in a joint household (so-called *Bedarfsgemeinschaften*). Recipients of social allowance are normally kids below the working age of 15. Social assistance continues to exist for people in need but permanently unable to work and for needy persons above 65 years.

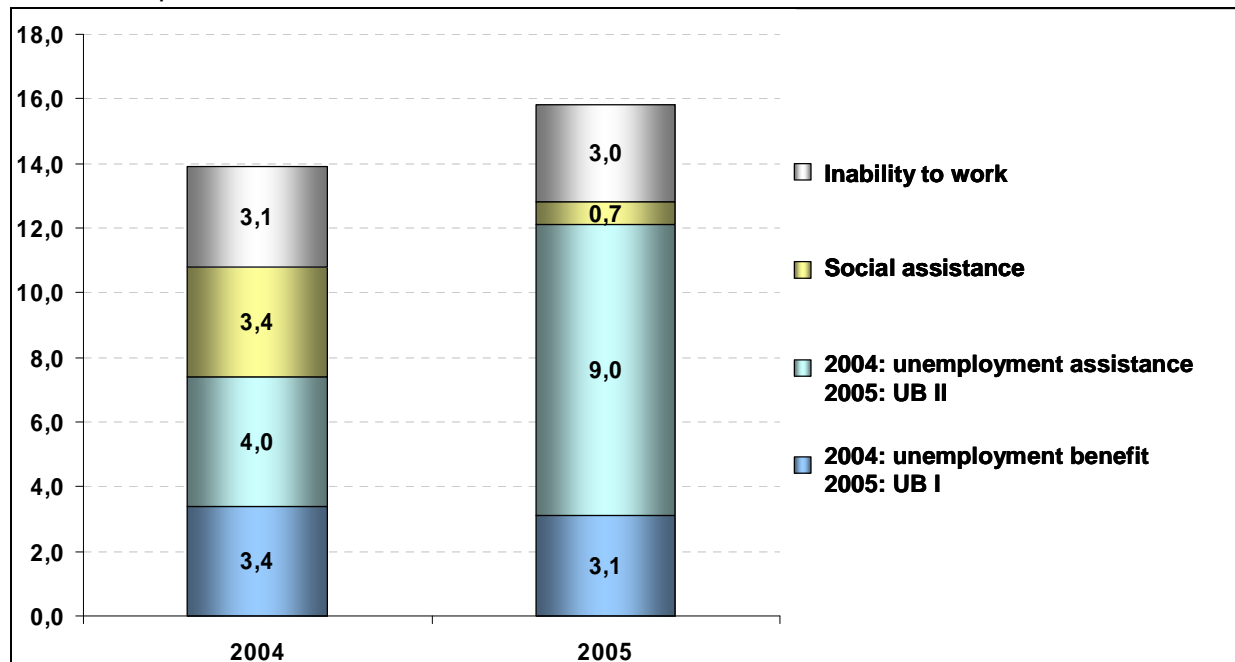
**Table 2**  
The Old and the New Benefit System

Old System (until 2004)	New System (2005 -)
<i>Arbeitslosengeld</i> (UB =unemployment benefit): unemployment insurance benefit; funded through contributions, earnings-related, limited duration	<i>Arbeitslosengeld I</i> (UB I): funded through contributions, earnings-related, limited duration
<i>Arbeitslosenhilfe</i> (UA= unemployment assistance): earnings-related unemployment assistance; tax-funded, earnings-related, means-tested, infinite duration	<i>Grundsicherung</i> (Basic income scheme for needy jobseekers) Consisting of a) <i>Arbeitslosengeld II</i> (UB II): tax-funded, means-tested, flat rate, after expiry of UB I (and temporary supplement) for people capable of working; infinite duration b) <i>Sozialgeld</i> (social allowance) for kids below the working age of 15 living in a household of an UB II recipient
<i>Sozialhilfe</i> (SH=social assistance): tax-funded, means-tested, flat rate, infinite duration	<i>Sozialhilfe neu</i> (Social assistance): means-tested, tax-funded for those working age people permanently not capable of working and for needy persons above 65 years

Figure 1 gives an impression of the quantitative changes in the benefit system. In 2005 9 percent of the working age population claimed means-tested and flat-rate benefits (basic income support for jobseekers) compared to 3,4 percent receiving social assistance and 4,0 percent

receiving means-tested but earnings related unemployment assistance in 2004. By including partners and dependants of the needy unemployed and by opening up the system for needy self-employed there are nearly one million people more on benefits. By tightening up the definition and assessment of "working ability" high shares of means-tested income support recipients are going to be activated now. The integration in an "active" unemployment regime where needy persons are more visible has been a declared objective of Hartz IV. In quantitative and structural terms Hartz IV could be characterized as a "big bang" welfare reform.

Figure 1  
Transfer recipients (15-64)

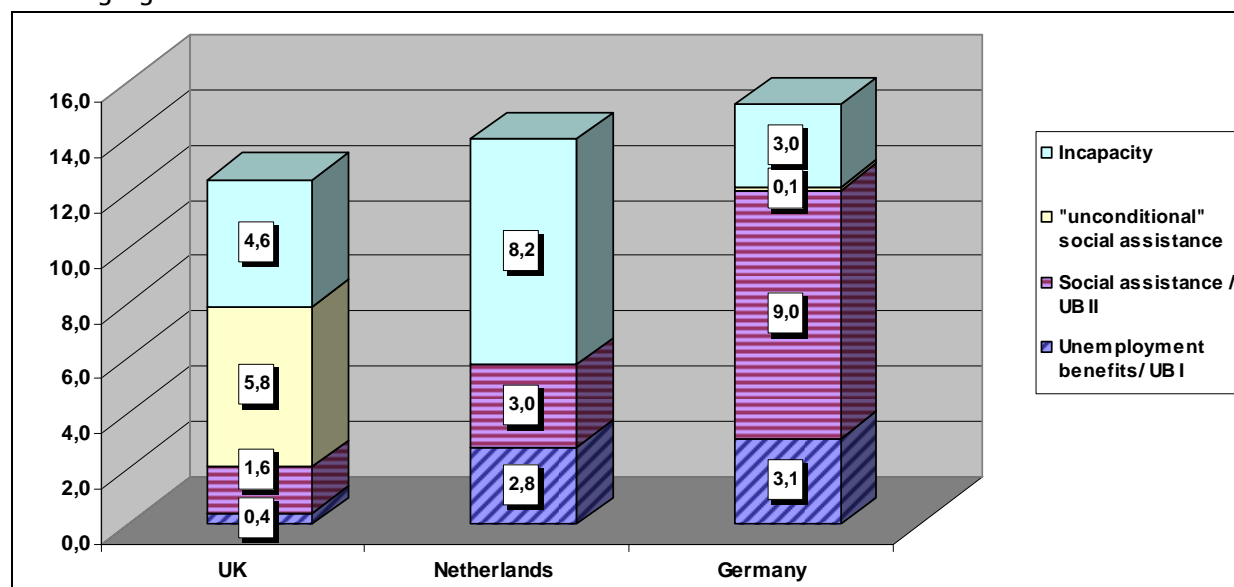


Source: Federal Statistical Office Germany, Federal Employment Agency Germany (2005), Federation of German Pension Insurance Institutes

Basic income for jobseekers, but also means-tested earnings top-up for low-wage earners, is now by far the more important benefit scheme. This new arrangements questions the status of lifetime achievement and occupational orientation that was characteristic for the German model of industrial production in the past. Hence, similar to other countries an indirect increase of public financing of unemployment benefits has taken place.

The "activation degree" of the whole social protection system in Germany is now higher than in countries like UK or the Netherlands (see Figure 2). Regarding the share of non-employed people underlying activation requirements Germany has developed from a latecomer to an early bird.

Figure 2  
Working Age Claimants 2005



Source: Statistic Netherlands, StatLine Database; DWP: Income Support Tables + Incapacity Benefits and Severe Disablement Allowance Tables; National Statistics Online, Time Series; Bundesagentur für Arbeit; Federation of German Pension Insurance Institutes

## 2.2 Activation on the intersection between labour market und social policies

The basic principle of activating social and labour market policy in a more narrow sense is "*Fördern und Fordern*", i.e. enabling or supporting the jobseekers on the one hand and demanding individual effort on the other. The recent reforms are in fact a recalibration of the German welfare state emphasizing both the role of demanding provisions (*Fordern*) and the enabling or empowering elements of social and labour market policy (*Fördern*). While these principles have been in place for some time under former social assistance and in the well established active labour market policy framework, what is new is a tighter conceptual and practical linking of promoting and demanding elements (*Fördern durch Fordern*). Among other measures eligibility criteria have been tightened. These general orientations were explicitly fixed in the new SGB II (Second Book of the German Social Security Act, SGB II).

The concept of individual "co-production" for needy persons "capable of work" replaces the former paternalistic model. The activation policy is more strongly orientated towards measures for job seekers who actively seek work to improve their situation in a self-responsible way. As participation in the labour market is assumed to be the high road to societal integration, taking up work is superior to receiving passive benefits only. Formal terms defining the basic orientation of German activating labour market policy, however, open up ample space for divergent interpretations that are crucial for actual implementation.

Like in other European countries also in Germany two previously separate domains of welfare and work as well as their policy domains of social protection and employment services have become merged, intertwined and are no longer thinkable as distinct. Complementary to work-

fare instruments like public relief jobs (so-called "One Euro Jobs"), SGB II comprises enabling schemes such as specific labour market policy programs for UB II recipients and other social services like child care provision or help in case of social problems like drug abuse, debt or housing that have been conceived in order to facilitate labour market integration. The discourse of workfare with its attendant phrase of "mutual obligation" or "*Fördern und Fordern*" reinforced in the German case the conditionality in social protection that cuts across and destabilises its logic through its new coupling with the policy logic of employment services.

### **3 Institutional changes in the delivery of employment services**

The Hartz reforms did not only change the system of social protection but also the general framework in which the delivery of employment and social services operates. The reorganisation of public employment services (Hartz III) has been the starting point of comprehensive reforms. The governance of active as well as passive labour market policy underwent a complete overhaul in order to facilitate a more "activating" police stance for the insured unemployed as well as for the long-term unemployed relying on welfare benefits.

#### **3.1 Reform of labour administration as starting point**

The re-structuring of the Public Employment Service, the *Bundesanstalt für Arbeit* (BA), initiated comprehensive labour market and welfare reforms. In 2002 the government took the "window of opportunity" to commission an expert group to work out a fundamental reform of the BA, blamed for operating inefficiently and customer-unfriendly. The traditional PES was seen as a large, sleepy and inefficient public bureaucracy restricted by law and regulation and by a lack of performance measures and competitive incentives. The Hartz report made especially tripartism in operative decisions responsible for ineffective and bureaucratic work of the BA. The report of the Commission – presented in August 2002- legitimized the BA-reform as well as further reforms of labour market policy and regulation (Hartz I-II). However, the Hartz I-III reforms were designed not only to increase the efficiency of the organisation but also to improve the effectiveness of labour market programmes as well as focusing more on individual tailored assistance.

At the beginning of 2004, legal changes concerning the organisational structure of the BA became effective with Hartz III. The aim of Hartz III was to improve the performance by streamlining public employment services. The *Bundesanstalt für Arbeit* (BA) – a self governing parafiscal unemployment insurance agency – was modernised along the lines of the New Public Management. In 2004 the organization was re-named in *Bundesagentur für Arbeit*. In accordance with a goal-oriented labour market policy, the former management-by-directives approach has been replaced by a management-by-objectives approach. Now quantitative goals are set for each local office taking into account the special circumstances in their local labour market. The formerly hierarchically organised employment offices were converted into customer- oriented job centres (*Kundenzentren*).

For recipients of unemployment insurance benefits the BA has been a "one-stop-shop" since its creation in 1927. The BA is still responsible for unemployment benefit payments as well as for counselling and placement services and the implementation of active labour market policy according to the Third Book of the Social Code (SGB III). The federal government, through the legal oversight of the Federal Ministry of Labour and Social Affairs, only has the duty of ensuring that the BA complies with the statutes and all other legal requirements of the SGB III. The government has no official influence on either the BA's operational business or the great majority of resource allocation as the BA is funded exclusively by compulsory social insurance contributions of employers and employees<sup>5</sup>.

In the old BA employers and employees representatives have had far-reaching co-determination rights for more than 70 years. A close-knit symbiosis between the state, employers and labour determined for decades the form and content of corporatist labour market policy. With Hartz III the "corporatist governance" of the BA was altered. The influence of the social partners with respect to the regulation of labour market services was withdrawn. Since 2003 tripartite codetermination of the BA is limited to the administrative council, which only has a controlling function, while the executive committee is set up limited in time. The tripartite administrative board was transformed into a supervisory board with extended information rights but fewer formal executive functions (Konle-Seidl 2003).

Unlike its new name the BA structure, however, still differs from a PES 'agency model'. For insurance-based services the BA sets its targets and performance goals independently from the government. Although contributions and benefits are defined by legislation, it has far reaching autonomy concerning the regulation of implementation. However, this holds only for the administration of the insurance scheme (SGB III).

Since 2005 the BA - together with the municipalities - is also responsible for the implementation of the new basic income support scheme (SGB II). The Ministry of Labour and Social Affairs has the legal oversight over the implementation of the SGB II. Decisions regarding operational objectives and resource allocation for the tax-funded UB II scheme services are steered by contracts between the ministry and the BA. Hence, administering the UB II scheme follows a clear 'principal-agent' relationship. By now the BA could be characterised as "Janus" faced: It is an autonomous insurance agency where social partners have supervisory and extended information rights (SGB III) and simultaneously it is a task force of the government (SGB II) where social partners have no co-determining and supervisory rights.

### 3.2 Contracting out of employment services

In the past the BA has been responsible for the implementation of active labour market policy under SGB III. However, the proper provision of labour market programmes was always con-

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<sup>5</sup> In 2007 the deficit coverage paragraph (§ 365 SGB III) was abolished. In the past a deficit of the BA at the end of the year was legally covered by the government budget.

ducted by third parties, mostly by non public, but third sector organisations and – to a minor extend – by for-profit organisations.

The long tradition of „the principle of subsidiarity“ in social policy implied not only the creation of self-governing bodies but also the involvement of third sector organizations in the delivery of labour market and welfare services. Since the early 1970s the provision of training services functioned within the framework of a “system of preferred suppliers”. As a consequence a highly developed market structure with about 28.000 private – mainly non-profit- training institutes were established at the local level in 2002. The owners of the largest training institutes in the country have been in the past unions or employers’ associations. They have gained a strong market position in the system of preferred suppliers. However, the amalgamation of management’s and labour’s interest in labour market policy, especially in expenditures for training schemes, has been publicly criticised as ‘cartel agreements’ and as one of the reason for an inefficient allocation of funds.

Despite the critics in pre-reform times and although one of the basic ideas was to introduce more competition in order to improve services the government did not set out a clear option for a comprehensive privatisation of placement and reintegration services like in the Netherlands. A rather cautious opening up of private delivery arrangements took place. Priority was given not to splitting up but to transforming the BA into a client-oriented ‘service organisation’ as well as to improving its performance in line with New Public Management (NPM) concepts.

However, the implementation of some of the commission’s proposals introduced decisive institutional changes in the German system of providing employment services. ‘Hartz I’, which came into force 1 January 2003, for the first time established and legislated outcome-funded instruments by allowing for contestable markets in the provision of re-integration services. The most prominent recommendation has been the creation of Personnel Service Agencies (PSA), publicly funded temporary work agencies to which the local PES refers jobseekers. Another small-scale programs like the ‘contracting out of re-integration services’ through public tendering was introduced. This instrument is targeted at unemployed persons for whom regular measures have failed. It is administered by local PES offices and strictly outcome-oriented. It works on a bonus payment system and is time-limited

An earlier step towards privatisation was made with the placement voucher (*Vermittlungsgutschein*). The voucher not only implies more competition on the re-integration market for the unemployed but also makes use of client empowerment, concepts previously unknown in the public provision of core employment services in Germany. On 1 January 2003 another voucher system for training schemes was amended. Even though the training voucher (*Bildungsgutschein*) was not part of the Hartz Commission proposals, the government introduced it without broad discussion, without considerable consultations with the stakeholders and without any piloting.

The government's decision to strengthen market mechanisms in the publicly funded training sector for jobseekers has been motivated by a desire to bring more transparency to the training market. The awarding of contracts for training measures was made more competitive and related to quality controls. Processes of networking were supported by the tendering procedures. However, the instruments for contracting out have been introduced as a pragmatic approach on a trial-and-error basis rather than as a well-designed contract management approach. Even though the relevance and design of contracting out placement and re-integration services to private providers are still in a rather early stage of development, a shift from diffuse delegation to a system with an increasing number of contestability criteria can clearly be observed. However, what one finds in current labour market policy is not a coherent model of stronger 'market governance' but rather peculiar hybrid forms of regulation. The German labour intermediation regime is characterised by a mix of procedural and contract governance, providing a mix of public financed and public-private delivered services (Konle-Seidl, 2005).

In countries with a corporatist tradition in labour market policy like Germany there are generally more obstacles in establishing quasi-markets than in countries with a powerful state and weaker social partners. The need for more individualised services for hard-to-place unemployed persons, however, opens up broader options for contracting out employment and welfare service provision. In this sense the BA started in July 2007 a new pilot aiming to test "successful context criteria" for a better involvement of private agencies. The step to a further "privatisation" of the German PES takes the British "Employment Zones" as example (Adamy 2007). The option of creating broader market governance in the sense of far-reaching privatisation of employment services, such as in the Netherlands and Australia, however, is – at least at the moment – still limited due the PES' character of taking on societal tasks, which is deeply rooted in the German tradition, its mode of funding and its historically high institutional legitimacy.

### 3.3 The new institutional setting

Simultaneously with the changes concerning the internal structure of the BA an external reorganisation of employment services took place. Joint agencies combining former local PES and municipal social assistance (*Arbeitsgemeinschaften, ARGEn*) for recipients of the basic income support were set up by Hartz IV in 2005. Table 3 gives an overview of the responsibilities of employment and welfare services with respect to regulation, funding and service provision after the Hartz-reforms.

The introduction of Unemployment Benefit II in 2005 was combined with the creation of joint jobcentres which was supposed to end the different treatment of recipients of unemployment benefit and social assistance administered by the municipalities over all with respect to access to labour market programmes. But instead of implementing a single gateway and a single one-stop-shop for all jobseekers rather two or even three "one-stop shops" have been created. Not only the PES customer centres but also the jobcentres of the ARGEn as well as the welfare offices of the "opting municipalities" can be considered as "one-stop shops" in the sense that they integrate front line services such as registration of jobseekers, benefit payment, intake,



counselling and direct placement on vacancies as well as the assignment on labour market programmes. They are supposed to bundle all services related to the labour market including counselling and support services from the social welfare offices, the youth welfare office, the housing office and job search assistance.

**Table 3**  
Institutional responsibilities in delivering welfare services

<i>Regime</i>	Unemployment Insurance	Basic Income Support
<i>Regulation</i>	Third Book of the Social Security Code (SGB III) Curtailing of tripartite codetermination within BA	Second Book of the Social Security Code (SGB II)
<i>Target groups</i>	Short-term unemployed	Needy persons capable of working; partners and dependants
<i>Benefits</i>	Unemployment Insurance Benefit (UB I)	Basic Income ( <i>UB II and Sozialgeld</i> )
<i>Funding</i>	Compulsory social insurance contributions of employees and employers	General taxes - at Federal level (income support and activation measures and about one third of the housing and heating cost) - at municipal level (two thirds of housing and heating cost and additional social services)
<i>Responsible organisations</i>	Bundesagentur für Arbeit (BA)	BA + Municipalities
<i>Training programmes</i>	Third sector and for profit organisations; networks	Third sector and for profit organisations; networks
<i>Placement and reintegration services</i>	Local BA offices private and non-profit organisations	ARGEn + 69 municipalities; private and non-profit organisations

Despite the joint legal framework (SGB II), the financial responsibilities as well as the decision powers between the central and the Länder (municipal) level are divided. From unclear regulation of organisational competences concerning organizational procedures arise a lot of administration problems within the ARGEn. Having their own direction and governance structures and being able to issue legal acts, the ARGE consortia are legal entities of their own. The local authorities are responsible for reimbursement of accommodation, heating and one-time costs for e.g. initial furnishing and clothes, child care services, as well as debt, drug and socio-psychological counselling according § 16 (2) sent.1 SGB II. The BA agencies are responsible for the payment of UB II as well as for all activation measures. Funding for these services is provided out of the federal budget. Additionally, about 30 percent of the housing and heating costs are also financed out of the federal budget.

Difficulties in harmonising activation targets across regions became apparent when the municipalities complained that the BA would hamper efficient job placement by centralistic ordinances. In response, an agreement was made in October 2005 between the federal government, the BA and the municipalities that leave the determination of operational targets for the ARGE to their governing council. However, the agreement could not solve so far the fun-

damental governance problems often described as "clash of cultures" between a more centralistic BA staff used to decide upon detailed legal provisions and the municipal staff used to decide on a greater discretionary leeway. Also the staff of the ARGE remains employed by different public sector entities – the Federal Labour Office (BA) and the respective municipality – with differing contractual employment conditions such as working time and salaries.

Instead of a coherent framework for all jobseekers, recipients of UB I and UB II are dealt with in different offices. UB I is administered by 178 local PES agencies and UB II by 356 ARGE. The institutional setting is even more complicated by considering the 21 districts where the long-term unemployed are dealt with separately by municipalities and local PES offices. Additionally 69 municipalities (*Optionskommunen*) could opt out for taking over the re-integration of the new UB II benefit recipients without PES participation for a period declared as "experimental" and extending until 2010<sup>6</sup>. Thus municipal responsibility with respect to the implementation of labour market policy increased but the fragmentation of the delivery of welfare and employment services aggravated. By setting up consortia with rather unclear governance structures and very diverse policies, highly complex and sometimes impracticable structures have been created.

The outcome of this organisational arrangement is a prime example of the German "interlocking federalism"<sup>7</sup> that spreads financing, decision-making and political responsibility across all federal levels. The distribution of competences was disputed for a long time and is the result of protracted negotiations between the Federal and the *Länder* governments. Although the reform enjoyed the consensus of the two dominant political parties, the Christian Democrats and the Social Democrats, federalism proved to be a decisive hurdle on implementing the reform. Concurrent legislation required a consensus of the two Chambers provoking an unintended fragmentation of what once was the PES.

A prominent aim of Hartz IV was bridging institutional gaps by integrating employment support and income protection for all jobseekers in one single regime ("one face to the customer"). The single gateway, however, was diluted by conflicts about finances and decision powers at different layers of government. For the sake of coherence, it was suggested initially that the PES should take over this role and be supported by municipalities. The establishment of such a structure, which would have taken away responsibility from the municipalities, was stopped, however, by the conservative opposition party. They argued that the municipalities

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<sup>6</sup> With the "option clause" extended now until 2010, 69 municipalities have been given temporarily exclusive competence for administering the new system. A comparative quasi-experimental evaluation of the two different implementation systems required by federal law is under way. The evaluation results – required by end of 2008 – will partly determine the further assignment of employment services to the municipalities or a strengthening of decision rights of the BA within the ARGE.

<sup>7</sup> Municipalities are under the legislation and supervision of the 16 *Länder*. As the basic income scheme ensues from "concurrent legislative" the Second Chamber, the Bundesrat – made up of representatives of the *Länder* governed by a majority of Christian Democrats, had to approve the bill, too.

would be closer to the regional and local labour markets and the need of jobseekers and they would have a stronger incentive to reduce the number of benefit recipients because the benefit costs are at less partly borne by their own budgets (Bruttel/Kemmerling, 2005).

However, the obligatory establishment of joint offices (ARGEn) involves a form of mixed administration that is not admissible and highly problematical from a constitutional point of view as it poses a threat to the principles governing the autonomous performance of functions and the clear assignment of responsibility. By Dec 20, 2008 the Federal Constitutional Court declared the mixed administration of the ARGEn as in-constitutional. Till 2010 the organisational service provision of the basic income scheme has to be reorganised again. So far it's an open question if there is a political majority for a general implementation of the municipal option model, for divided structures creating again two stop shops for welfare clients or for a more centralised model being the PES the main actor. Another solution could be yielded by changing the Constitution in order to maintain the ARGE structure.

### 3.4 The German reforms in European comparison

Hartz I-IV implied a complete overhaul of the governance of active labour market policy (ALMP). Whereas Hartz I-III aimed primarily an increase in the effectiveness and efficiency of ALMP, the objective of the institutional and organisational changes of Hartz IV was to facilitate activation on the intersection between labour market and social policies. By the parallel implementation of a structural benefit reform and fundamental organisational and institutional changes the German "big bang" reforms differ from gradual changes in other European countries (table 4).

Table 4  
Benefit reforms and governance changes in European comparison

Country	Governance changes			Benefit reforms	
	Single gateway only access point to different benefits and employment services	One-stop shop combining benefit and employment service functions within the same organisation	NPM, Quasi-markets Internal restructuring, contracting out and the marketisation of employment services	Gradual Eligibility requirements, maximum duration, benefit levels	Structural Benefit types abolished or merged; new benefit type
D	no	BA 1927 ARGE 2005	BA modernisation 2003-2005 Quasi-markets in placement; voucher system		Basic income for able-bodied jobseekers 2005
GB	Jobcentre Plus 2002 - 2006 By merging benefit administration and employment services		NPM; employment zones		JSA 1996
DK	Jobcentre 2007 By merging PES offices and municipal service provision		More Contracting out of employment services	Since 1994 ongoing reforms	no
NL	2001 SUWI reform	For social assistance clients (WWB)	Privatisation of re-integration services (SUWI 2001)		1996 remove of unemployment assistance

## 4 Preliminary assessment of reform outcomes

With the Hartz reforms also the need for a rigorous scientific evaluation of program effectiveness was recognized by policy makers and a corresponding evaluation mandate was implemented. The results of comprehensive research into the effectiveness of active labour market schemes and placement services (Hartz I-III) became available recently (see table 5 p. 24). However, the evaluation of the shift towards activation of the long-term unemployed (Hartz IV) is still in progress. Final empirical results concerning causal effects of activation and the impact of different institutional models on the outcomes are not available until end of 2008. A comprehensive assessment of the whole German labour market and welfare reforms implemented between 2003 and 2005 is therefore not possible yet.

However there are preliminary results. The evaluation of the "option clause" (§ 6c SGB II) is designed to compare the impact of different institutional models - the ARGE consortia, the licensed municipalities and divided structures- in four lots<sup>8</sup>. Descriptive analysis shows by now no fundamental differences between the competing institutional models concerning outcomes variables like re-integration, employability or social stabilization

[http://www.bmas.de/coremedia/generator/22834/f369\\_forschungsbericht.html](http://www.bmas.de/coremedia/generator/22834/f369_forschungsbericht.html)).

Beyond referring to empirical results in the following chapter we try to link major changes in the German welfare governance since 2003 with objectives generally pursued by them. New forms of Welfare Governance and New Public Management are supposed to contribute

- to reduce public expenditure,
- to increase the responsiveness of the agencies delivering them,
- to improve the effectiveness and efficiency of policy programmes,
- to increase the quality of public services, and
- to promote the choice of the users of public or publicly financed services (empowerment).

### 4.1 Insurance logic versus welfare logic

Where other countries tend to mix contributions and tax revenue in the funding of their unemployment benefit schemes, Germany kept the two sources apart and allocated them to different stages of people's unemployment careers. The insurance-based UB I system and the tax-funded UB II system follow different governance logics leading to a negative spill-over for the

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<sup>8</sup> The question "who performs better and why" (ARGE consortia or municipal option model) is analysed according three success criteria (a) re-integration in the labour market (b) improvement of employability and (c) social stabilising function.

The four evaluation lots comprise

- (1) Descriptive analysis and regional matching (154 out of 439 local units matched for in-depth analysis);
- (2) The implementation and governance in 154 local units (semi- standardised case studies);
- (3) Outcomes and efficiency (2-wave survey of 25,000 customers in 154 local units, linked with administrative data for econometric analysis) and
- (4) Macro-economic simulation and benchmarking

<http://hartz.isg-institut.de/isg.de>

overall system. Hence, the strict division of two "accounting systems" reinforced the above analysed governance failures.

For insurance-based services the BA sets its targets and performance goals independently from the government. The main objectives of the new BA are the effective and efficient use of the measures provided by the Third Book of the Social Code (SGB III). The setting of operational goals follows an insurance logic. This logic involves transparency about how and with which results unemployment insurance funds are spent. Cost-effectiveness in the specific context of each regional labour office is the key criteria when choosing programme contents and participants. Improved targeting of active measures and the allocation of measures and resources opened up a wider scope for fitting clients to measures more individually. Provision of services has been decentralised with the aim of bringing BA activities closer to the specific, individual needs of the clients of the BA. The caseload of advisers is to be reduced and every jobseeker is assigned to a fix caseworker.

Profiling and segmentation of jobseekers constitutes an essential element in the BA reform process. It has been applied since 2005. Profiling in the German PES serves as a tool for customer segmentation and the determination of individual assistance as well as an instrument for resource allocation. The unemployed jobseekers are segmented into four categories: "market clients", "clients for counselling and activation", "clients for counselling and qualification" and "intensive assistance clients". The assignment to one of the four categories determines the future treatment. Based on the individual profiling result tailor-made action programs (*Handlungsprogramme*) for each client group are developed. At the end of the intake interview caseworker and jobseeker agree on an action plan specifying individual "integration objectives" and resources.

The strict outcome oriented performance management shows after five years of fundamental and ongoing reforms positive and negative results. Evaluation results indicate positive effects concerning a faster re-integration of unemployed into regular employment (table 5 p. 24). The transition rate from unemployment to employment promoted by active measures as well as "just" by placement without extra financial resources could be improved. However, the most visible success seems to be the spectacular cost reduction and a surplus of the insurance funds. For more than one decade the financial balance of the contribution based receipts and expenditures of the BA was deficient. The Agency itself assessed that efficiency gains contributed to one third to the surplus (BA 2006).

Cost-effectiveness in the UB I system has improved the results for the "community of insured" (*Versicherungsgemeinschaft*). By January 2007 the rate for employers and employees could be reduced from 6.5 to 4.2 per cent and further to 3.3 per cent by January 2008. But the efficiency gains in the insurance system were accompanied by negative side-effects for the welfare system and the overall aim to prevent long-term unemployment. The critical assessment deriving from the success oriented overall strategy of the BA concerns the treatment of different client groups.

The new concept regarding the allocation of resources between client groups concentrated the Agency's resources and activities on the "clients for counselling" who, though not easy to find jobs for, still have a fair chance, in the short term, of being integrated into the labour market. This change has run the risk of disadvantaging the "intensive assistance clients" who have very poor chances of finding a job as such people will benefit less frequently from active labour market measures. Expensive and long lasting programmes for the intensive assistance clients did in the Agency's management cost-benefit logic not pay off, especially when the "penalty tax"<sup>9</sup> implemented as an incentive to reinforce integration efforts by the BA was in place. While participating in long-lasting programmes a transition for intensive assistance clients into employment before exhausting the UB I claim is rather unlikely the Agency had to pay additionally to the programme costs the "penalty tax". As a consequence, the incentives for the BA to "park" the hard-to-place clients<sup>10</sup> have been strong. But more than to blame the Agency for neglecting the fulfilment of social tasks it is the institutional setting of the German unemployment regime - contribution based UB I and tax financed UB II administered by different institutions and by different financial logics which generates a trade-off between the fulfilment of social and efficiency tasks.

The implementation of Hartz IV led in fact to higher rather than lower public expenditure and to an increase rather than a decline in the number of benefit recipients as compared to the situation before 2005. This development is partly explained by higher take-up rates of means-tested benefits after 2005 revealing unknown rates of "hidden poverty" in the old system (Becker 2006).

Hence, lower expenditures for the insurance systems resulted in higher ones for the tax-funded system. The additional expenditures for Hartz IV amounted to 7 billion € in 2005 and 2006. Expenditure increases in UB II and related active labour market policies reflects the shift from unemployment insurance to basic income which also means a shift from contribution-based to tax-funded passive and active labour market policy schemes. The division of responsibilities between national and local governments is one reason for increased expenditures and the necessary compensation by the federal government because of benefit over-run for the UB II scheme.

Whereas the federal burden of funding of UB II, related employment services and housing costs for the federal government went up, municipal responsibility with respect to the implementation of labour market policy decreased. As the municipalities maintain the financial responsibility for income support for persons who are not able to work (social assistance), they had especially in 2005, when the welfare system was reorganized, an incentive to shift costs

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<sup>9</sup> The "penalty tax", about 10.000 € per client, has to be paid by the Agency if being unable to integrate its clients into work during the regular UB I entitlement period. However, a recent legal expertise declared the penalty tax as unconstitutional so that it's abolished now.

<sup>10</sup> In 2007 the BA initiated in 6 regions pilots to test whether „intensive assistance clients“ will be better reintegrated by private service providers if no concrete integration perspectives could be offered by PES after 4 or 5 months of unemployment duration.

by classifying persons as being able to work who would otherwise obtain municipal social assistance. Indeed, in 2005 97 percent of the former social assistance recipients were assessed to be "capable of working" and therefore transferred to the federal funded UB II system (Statistisches Bundesamt 2007).

The in-congruency between spending and decision powers at the different layers of government inhibits a more efficient management of employment policies especially for the long-term unemployed. It seems that there is no simple solution of this very German "governance dilemma". Although the social partners disagree in how to spend the surplus of the BA, they agree in maintaining the strict separation of unemployment insurance contributions – considered as property rights of the insured – and tax-funded resources for welfare tasks. Due to increasing expenditures for the welfare system the legislator has to invent constantly new mechanisms for a distribution of resources between the two systems<sup>11</sup>.

## 4.2 Responsiveness of the actors

The basic structure of unemployment insurance and basic income support as well as activating labour market and social policies in Germany is mainly defined by legislation. Service provision is in great part a public task although third sector organisations have always been the main providers of training and public job creation services. Outsourcing and network building – now on the agenda in many countries – is not a new phenomenon in Germany. While a more far-reaching privatization of the PES was not considered seriously, performance of the BA in job placement was to be improved through more intense competition with private providers. Private profit and non-profit actors have become more prominent as contracting-out of active labour market policy services has grown over the last decade, most significantly in the area of re-integration and training services. Nonetheless, the use of market mechanism in delivering employment and welfare services in Germany has a rather complementary character.

However, further perspectives for contractualism in employment services depend heavily on the question of whether the added value of contractual government could be assessed fairly. Beyond a lack of standardised quality control of private providers due to multi-tasking problems, public accountability and the ability to assess quality also diminish when outsourcing becomes a dominant feature. Moreover, success or failure depends not only on contractual agreements but also on environmental conditions, especially the motivation of the unemployed and – even more critically – on the overall lack of jobs in the economy. The direct employment effects of more privatised employment services seem to be rather limited.

Empirical findings on a control group design about three new reintegration programmes relying on private service delivery display no significant effects, which maybe due to *de facto* inef-

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<sup>11</sup> As the construction of the "penalty tax" failed by being declared unconstitutional the Minister of Finance proposed now that a part of the surplus of the insurance fund should be spent for integrations measures for UB II recipients as before 2005 when active measures provided for unemployment assistance claimants were funded from contributions. However, this is only one example of new "Verschiebeshöfe" (literally: switching stations) between different financial systems.

fective or small-scale policies, or perhaps due to the fact that the post reform observation period is not yet long enough. While the assignment to private placement providers shows no positive effects, there is weak evidence in case of the "placement voucher" (see table 5 p. 24). Private providers could achieve better results on re-integration of unemployed than the local PES offices. It appears, however, that many clients who had received placement vouchers did not actually use them. Placement via subsidized temporary work (PSA) shows negative treatment effects. PSA even reduce the employment probability of participants (Kaps/Schütz 2007).

The influence of social partners was reduced significantly in the context of the Hartz reforms as they had been criticized for not being interested in an efficient allocation of funds and rather subsidizing training providers associated with either the trade unions or the employers' associations. This led to the erosion of traditional close networks between PES and providers of training and other services that were often affiliated with the social partners.

The BA reform introduced a shift from bureaucratic governance to one that is much more performance based. Following New Public Management (NPM) theories, the performance of the policies thus need to be tightly monitored and evaluated in order to adjust the policies for improving performance. In order to monitor and evaluate this performance, benchmarks of local employment offices were set up. Decisions regarding operational objectives and resource allocation for the tax-funded UB II scheme services are steered by contracts between the ministry and the BA but with weak enforcement mechanisms on the local level.

Hence, there is no dominant governance feature in the fragmented system of employment services in Germany. Actually there is rather a mix of governance modes: rule-oriented modes co-exist with NPM models supported by quasi-market mechanisms and network relations between public and private organisations. But there is also a paradoxical situation concerning the tendency to integrate employment support and income protection. On the one hand benefit payment, job search assistance and activation measures for UBI recipients are integrated in BA "one-stop-shop" since 80 years. Also the new jobcentres of the ARGE consortia provide income support for UB II claimants as well as employment and additional psycho-social support from one single stop. However, the missing unified structure and single gateway for different types of benefit claims and activation measures hamper a more coherent and efficient activation strategy lacking an effective overall strategy to prevent long-term unemployment as the most negative outcome<sup>12</sup>.

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<sup>12</sup> A rather late intervention is also in contrast to the recommendations of the OECD Jobs Study (1994) and the European Employment Strategy ([http://ec.europa.eu/employment\\_social/employment\\_strategy/index\\_en.htm](http://ec.europa.eu/employment_social/employment_strategy/index_en.htm)) where governments were urged to ensure early and effective activation for jobseekers. The European Employment Strategy Guidelines on active and preventative measures for the unemployed sets out that 'at an early stage of their unemployment, all jobseekers benefit from an early identification of their needs and from services such as advice and guidance, jobs search assistance and personalised action plans with special attention to people facing the greatest difficulties in the labour market.'



### 4.3 Effectiveness and efficiency of ALMP measures

Hartz I-III aimed to improve the performance of placement services and policy programmes mainly by streamlining public employment services and by introducing market mechanisms to the realm of placement services as well as improved targeting of active measures and the allocation of measures and resources. A comparison of the effectiveness of key elements of German ALMP before and after the Hartz reforms (table 5) indicates that the re-organisation of public employment services was mainly successful. The redesign of the customer service (*Kundenzentrum*) of PES offices appears promising. Re-designing training programmes seems to have improved their effectiveness, while job creation schemes continue to be detrimental for participants' employment prospects. Wage subsidies and start-up subsidies show significantly positive effects.

Table 5  
Main results of the Hartz I-III evaluation

	Employment effect	Cost-effectiveness
Re-organisation of local employment offices; new BA steering model	(+) Customer centres (+) transitions	++
Private service providers compared to PES	- PSA (-) outsourced reintegration programs (+) placement voucher	?
Redesigned ALMP measures with improved targeting	(+) vocational training (+) wage subsidies (+) start-up grants (-) job creation schemes	(+) general increase but still (-) cost/benefit balance

Source: Results of the final report (Bundesregierung 2006)

On balance, the Hartz reforms I-III have contributed to a better functioning of the German labour market as well as to improve specific active labour market policies. This positive assessment, however, has to be qualified somewhat in the light of the fact that the starting situation upon which the reforms intended to improve was quite dismal (Jacobi/Kluve, 2007).

The empirical results attribute a considerable success to governance changes, especially to the BA reorganization and a remarkable shift to a more goal- and efficiency-oriented approach within contribution-based active schemes administered by BA. So do empirical studies on matching efficiency (Fahr/Sunde, 2006). Stronger profiling and goal-orientation in the assignment of active schemes to short-term unemployed seems to explain the savings in contribution-based active and passive labour market policies.

Since the reform, selection into training measures and job creation schemes have deliberately used cream skimming in order to choose those clients who will benefit most. For vocational training programs only clients who are conjectured to have a 70 per cent probability of finding a job after the measure have been admitted. Post-Hartz evaluation have indicated that better

targeting and shortening of training course duration succeeded in significantly reducing lock-in effects and increasing exit rates into employment. Cost-effectiveness of measures increased after the reform, though the cost and benefit balance is still negative.

However, there are also complaints about the downscaling of activation programs by applying stricter effectiveness and efficiency criteria in ALMP. Compared to 2002, spending on active labour market policy through 2006 has decreased of about one-third. The financial volume for the most important instrument, vocational training programmes, decreased from €7.2 to €2.0 billion. Other important expenditure items as youth programmes as well as programmes for the disabled were also downscaled. Classical job-creation schemes – proved to have negative re-employment effects – have been effectively replaced by Social Code II employment opportunities (the so-called “One Euro Jobs”).

Despite a sharp decrease of spending statistics, average number of participants show a relative continuity over recent years. This is explained mainly by a shift of expensive but ineffective measures to cheaper and more effective ones. There was a notable expansion of shorter training schemes and aptitude tests, as well as of measures aimed at younger workers (Eichhorst/Zimmermann, 2007). The downscaling of further vocational training programs seems to be stopped now. Participation rates are rising again – in 2006 by 70 per cent – since restrictive targeting is partly lifted.

#### **4.4 Decentralised versus centralised service delivery**

With the evaluation of the “option clause” competitive federalism is going to be tested for the first time in Germany. Decentralised service delivery (“opting municipalities”) is tested against a more centralised one (ARGE). As decentralisation of employment policy is a central issue for ministries of Labour today and an important tool to improve local governance the empirical outcomes in terms of employment and employability are obviously of great interest not only for German policy makers.

However, decentralisation of governance or managerial power could not be interpreted simply as a stronger localisation of welfare reform. In the NPM literature it is well documented that such decentralisation processes are somewhat paradoxically often accompanied with a reinforcing centralisation. Central governmental powers accede day-to-day decision making and management processes to tighter definition and continual monitoring of performance objectives. Local agency operations can become more independent although tightly controlled in agency objectives and funding (Henman, 2006).

Decentralisation raises a number of challenges, both in terms of the degree of flexibility in policy management and of the capacity to guarantee public accountability. Politicians in many countries are looking for the right balance between the efficiency of central goal setting and the effectiveness of local provided services in order to tackle the trade-off between flexibility and accountability. The search for the right balance is also a crucial question of topical interest in Germany. Hartz IV contains elements of centralisation by shifting the larger share

of responsibilities to the PES as well as decentralising elements by enforcing cooperation between the municipal welfare offices and the PES offices, strengthening local arrangements, and providing opt outs for municipalities. However, the path- dependent „interlocking federalism“ hampered a stronger decentralisation of regulating and financing of social policy like in the Netherlands as well as a stronger centralisation like in the UK.

Compared to the US welfare reform with strong decentralisation or better federalisation of assistance – a model for some German conservative policy makers – the German reform strategy is more mixed. In Germany there are more constitutional constraints hampering a stronger localisation of services. Whereas in the USA the States have alternative resources at their disposal being free to go beyond or even ignore provisions of the act, in Germany is the uniform federal regulation deemed necessary both for the establishment of equivalent living conditions and for the maintenance of legal and economic unity according Art 72, 2 of the German Constitution.

Consequently, the governance part of the Hartz IV reform is a mix of the centralised Bismarckian unemployment regime and the legacy of poor relief, which had always been a municipal prerogative in Germany. This tradition allowed the creation of one-stop-shops but not the set-up of a single gateway for all benefit recipients out of work. However, also in the USA a single gateway option seems hampered by regional disparities, and by diverse administrative responsibilities and accountabilities within a federal structure. Anyway, in the case that responsibilities for UB II related policies would be assigned in the future to a greater degree to municipalities this should be accompanied by a financing mechanism (e.g. block grants) providing incentives for the municipalities to engage in efficient job placement and effective welfare services. In the experimental clause limited till 2010 the “opting municipalities” have a high discretionary leeway but are not fully responsible for their expenditures creating well-known free-riding problems.

#### **4.5 Institutional changes and activation policies**

With respect to activation of the long-term unemployment (Hartz IV) empirical data is only partially available yet. Comparative assessment on effectiveness of activation measures pre- and post Hartz IV is hardly possible due to a complete overhaul of the benefit system and the very new design of activation measures for UB II recipients. Before the reform previous social security contributions were the key criterion for access participation in active labour market policy programs. Now participation is strictly conditional on a person's ability to work. This is defined as being able to work at least three hours a day. Those capable of working are assigned to the ARGE offices and will be subject to activation policies on the basis of the principle of “rights and duties” (*“Fördern und Fordern”*).

UB II recipients are therefore no longer excluded from most of the instruments of ALMP. Additionally UB II claimants have access to measures which have been designed specially for welfare recipients and their particular barriers to employment like debt, abuse of alcohol or other drugs, socio-psychological counselling and child care services. Persons capable of working who

within the past two years have not received cash benefits under either SGB II or SGB III are immediately offered activation measures. If needy able-bodied persons find no job, public employment opportunities ("One Euro Jobs") are to be offered (§ 16 (3) SGB II). Apart from serving as work test the activating effect of One Euro Jobs is seen an improvement of employability in terms of regaining a steady work rhythm, punctuality etc.

As one-stop shops should also streamline assistance and activation one central promise of Hartz IV had been to cut down workloads in the new system of basic income support to 75 for the age group under 25 years (U25) and to 150 per household. In the old system, due to problems of missed targeting, job counsellors had caseloads of up to 700 jobseekers. It seems that a higher level of assistance and activation could best be achieved for the U25 group by now. Specialized case-managers activate especially more U25 people.

According to law, an integration agreement (*Eingliederungsvereinbarung*) is supposed to be concluded with each able-bodied claimant and to be renewed every six months. The first empirical data suggest a moderate approach towards activation in actual practice, i.e. regarding use of integration agreements, activation measures and sanctions. Till end of 2006 only 45 per cent of the clients concluded an integration agreement and one third was without an interview at the employment office in the last 6 months. Only 10 per cent of recipients with more problems than unemployed received integrated social services.

The activation profile differs across targeting groups. Unemployed people above 50 (50+) are going to be activated less than youngsters (U25). To 57 percent of them immediate work or training have been offered within three months. However, it seems that the size of the job-centre is important for an effective organization of the activation process and that the integration of benefit processing into case-management improves client satisfaction but hampers activation and labour market orientation (BMAS, 2007).

One explanation for the moderate level of activation may be explained time constraints. As there was no roll-out strategy and the change into the completely new governance and service structure was envisaged by the legislator to be effected within one juridical second, the new units had only few months to prepare themselves for the formidable task to take over nearly three million needy households (*Bedarfsgemeinschaften*). As priority was given to correct benefit payments without producing an organisational chaos, activation objectives had to be pushed into the background (Knuth 2006). Just recently, new entrants are going to be activated more intensive.

Another explanation of early intervention measures for potential long-term unemployed is the lack of a coherent normative framework. The described disincentives embodied in the existing funding and governance arrangements as well as the ambiguous institutional incentives hamper an overall strategy for potential long-term unemployed.

#### 4.6 Changes in the relationship between the citizens and the state

The status of individuals under German employment promotion law (SGB III) is still strongly codified (*verrechtlicht*). This was often deplored and assessed as stabilizing a status quo that is more or less resistant to reform. The greater degree of flexibility for employment offices under the new SGB II system implies generally a weaker legal position for the individual. However, the greater flexibility of activation at the local level does not mean that UB II beneficiaries do not have access to legal advice or the right to file a lawsuit.

Like in many other countries the relationship between citizens and the state are going to rely more and more on a contractual basis. The personal integration agreement (*Eingliederungsvereinbarung*) between the jobseeker and the case worker is the most striking example of changing relations. The two parts have to conclude an integration agreement stipulating the necessary services and obligations. For UB II claimants these agreements are mandatory. This duty is not a duty in the legal sense, but a so-called incidental obligation, meaning its fulfilment is not legally enforceable. But it is indirectly "compelled" via the imposition of a financial sanction.

Under the insurance scheme integration agreements, however, have a limited significance. Integration agreements for UB I recipients are not a precondition for participating in active measures. Rather they are regarded as an instrument for improving the placement procedure. They are linked only to active measures, but not to passive benefit receipt. The agreement therefore cannot be used to sanction unemployed persons. As a consequence, integration agreements are scarcely applied within the legal ambit of SGB III. In contrast to integration agreements for UB II claimants, the merits of negotiated strategies under the insurance scheme mainly lie in the psychological sphere (Konle-Seidl et al. 2007).

Individual integration agreements do not only enforce obligations but open up possibilities to strengthen the position of the individual vis-à-vis the welfare offices. Benefit recipients have the possibility to act as agents. They can demand benefits and services in case they are eligible and they have the right to appeal against sanctions applied for non-cooperation upon good cause shown.

Apart from the "empowering" element of the individual integration agreement the introduction of the placement and the training voucher in 2002/2003 makes also use of client empowerment, concepts previously unknown in the public provision of core employment services in Germany. But if 'enabling self management' is promoted seriously, an increase of the whole range of services is needed. Apart from counselling and job placement services, i.e. care services are needed in order to enable the individual – and over all women – to participate in the labour market. In such a system, activation crucially depends on frontline implementation of demanding and enabling schemes and the actual application of benefit conditionality.

Despite more contractual relationships between the individual and the state we still find many provisions with direct legal effects. Compared to PROWA in the USA which abolishes the indi-

vidual right to assistance, but operates almost exclusively via monetary incentives and sanctions vis-à-vis the States, the legal position of the individual under Hartz IV is still strong.

#### 4.7 Fluctuations and exits form unemployment

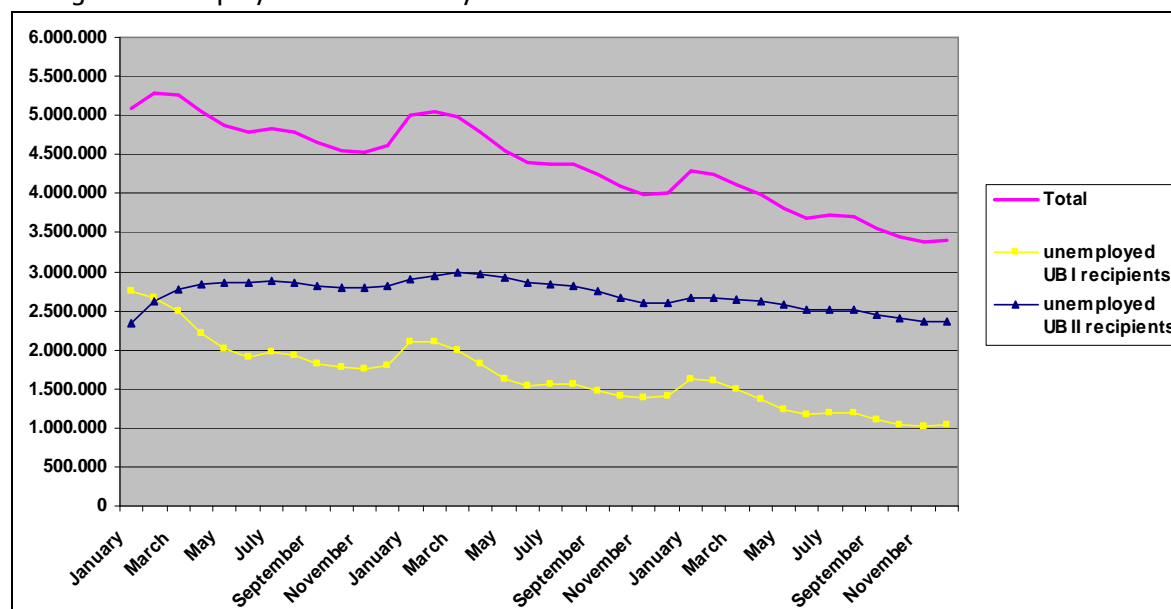
Due to the lack of impact studies on improved workload or the use of personal integration agreements on labour market outcomes we present some descriptive data<sup>13</sup> on exits from unemployment and reintegration rates in regular employment as a rough device of a modest reform success. Table 6 shows a great success in terms of fluctuation in the UB I and a modest success in the UB II system. In terms of unemployment (figure 3) there is a sustained positive trend. The sharp decline in unemployment rates is probably in great part attributed to the economic upswing since mid-2005. A positive (causal) influence of the reforms on improved performance on the labour market is likely but rather unclear yet.

Table 6  
Gross reintegration rates (2005–2007)

	UB I (unemployment insurance)			UB II ( basic income support)		
	Average annual stock - in 1 000-	Outflows employment - in 1 000-	Re-Integration rate	Average annual stock - in 1 000-	Outflows employment - in 1 000-	Re-integration rate
2005	2091	2206	51%	2770	557	21%
2006	1664	2019	52%	2823	744	26%
2007	1253	1974	52%	2523	833	27%

Source: Bach et al. 2008

Figure 3  
Changes in unemployment in Germany 2005–2007



<sup>13</sup> The profound changes of the German system of social protection for workless people and its governance go along with deep changes and inconsistencies in the administrative data structure. Many useful times series have not been available for a long time. Especially data from the 69 licensed municipalities are still lacking in central databases.

## 5 Conclusions

The late, but fundamental change in German's labour market and welfare system is most notable in comparison with other European countries such as Denmark, the Netherlands or Great Britain as the German approach to activation is relatively broad and ambitious. Especially with the Hartz IV- reform many "German givens" came to an end. The culture of transfers was replaced by activation and the culture of status continuity by biographical risks. Unlike most other countries opting for "activating" Germany combined this move with a fundamental change of the benefit system. Introducing a flat-rate benefit scheme for great part of the job-seekers was a "path-break" with the Bismarckian feature of the German welfare state.

Like in many other countries changes in the programmatic of activation policies were accompanied by new forms of organisational and operational implementation. But although these changes move by large into same direction as in other countries there are also very German features differing from the general trend.

Expenditure on unemployment insurance benefits tends to decline at the expense of higher expenditure on tax-based unemployment assistance and active labour market programs for recipients of UB II. This means an important step towards replacing contribution funding by tax funding but without a clear strategy for doing so and, consequently, without achieving an overall reduction of expenditure. One fundamental paradox of the German reform is that the fiscal costs are exceeding initial expectations, while on the other hand most of the concerned feel that something has been taken away from them.

Another paradox refers to the new institutional setting of employment and welfare services. Contrary to the aim of integrating employment support and income protection in one single regime the institutional gap that was intended to be bridged by the Hartz reforms is now wider than before. The single gateway idea has so far been very much diluted by conflicts about finances and autonomy among municipalities and the local PES branches. Instead of a coherent framework for all jobseekers, recipients of different benefit schemes (UB I and UB II) are referred to jobcentres following an eligibility logic instead of an individual assistance needs logic.

The in-congruency between spending and decision powers at the different layers of government and the missing single gateway for different types of benefit claims and activation measures hamper a more coherent and efficient activation strategy especially for the long-term unemployed. Diverging fiscal incentives of two strictly separated "accounting systems" work against early intervention to prevent long-term unemployment. The fundamental restructuring of organisations and governance created a lot of frictions and took up a lot of energy that the activation agenda was pushed into background for a certain time.

If the governance changes introduced with Hartz I-IV have created the right incentives to realize the main objectives of activation policies, is so far an open question. Empirical evaluation results attribute to the proper insurance based unemployment system a considerable suc-

cess, especially to the BA reorganization and a remarkable shift to a more goal- and efficiency-oriented approach within contribution-based active schemes administered by BA. The BA was modernized along the lines of the New Public Management by introducing a management-by-objectives approach and market mechanisms to the realm of placement services. The influence of social partners with respect to the regulation of labour market services was reduced significantly thus altering the long-standing corporatist tradition in German labour market policy.

While a general privatization of the BA was not considered seriously, performance of the BA in job placement was to be improved through more intense competition with private providers and contracting-out of placement services. Hence, the whole range of labour market policy is nowadays characterized by a greater mix of governance modes: rule-oriented modes co-exist with NPM models supported by quasi-market mechanisms and network relations between public and private providers.

As participation in activation programmes is strictly conditional on a person's ability to work UB II recipients are no longer excluded from most of the instruments of ALMP as they have been before the reform where previous social security contributions were the key criterion for access. Additionally UB II claimants have access to measures which have been designed specially for welfare recipients. Those capable of working are subject now to activation policies on the basis of the principle of "rights and duties" (*"Fördern und Fordern"*). The concept of individual "co-production" for needy persons "capable of work" replaced the former paternalistic model. The activation policy is stronger orientated towards measures for jobseekers who actively seek work to improve their situation in a self-responsible way.

Although there is still a lot of confusion and in-congruency in the welfare governance system there is also a modest success in terms of effectiveness of measures and services. The sustainability of this success, however, is an open question as well as the improvement of services for all unemployed jobseekers regardless the type of benefit system they are referred to. With regard to the foreseeable future, the German activation regime is most probably not a stable one. A final decision regarding the institutional organisation of welfare services for the long-term unemployed is required by the Constitutional Court till 2010. However, a more general revision of administrative competences and funding would help strengthen incentives for more efficient activation by PES, municipalities or even a new type of jobcentres.

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