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Income Support in the Absence of a Legal Minimum Wage: the Case of Germany

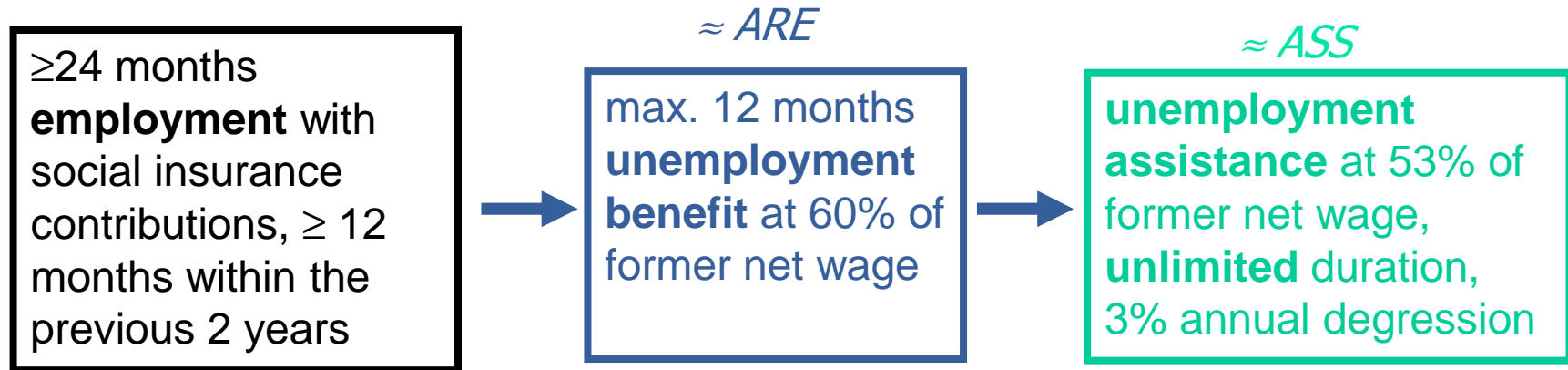
Seminar on Work, Employment and Social
Protection

From RMI to RSA: Minimum Income Support and
the Labour Market

Centre d'Economie de la Sorbonne
Paris, November 27, 2008

Benefit System until 2004

(no children, under 45 years old)

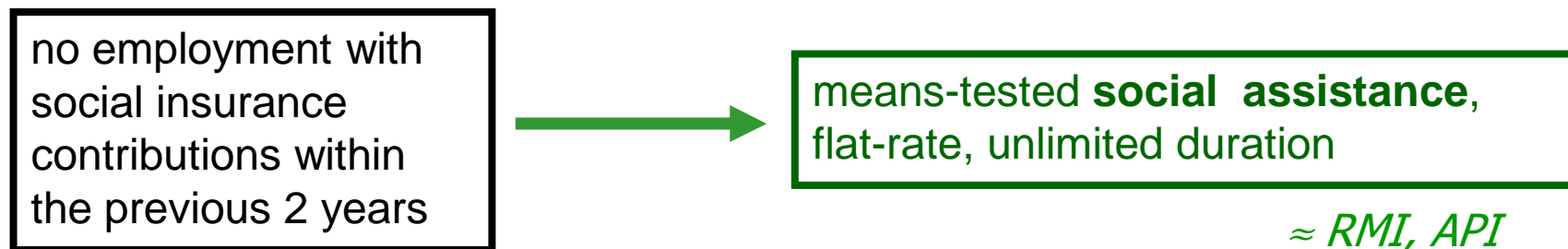


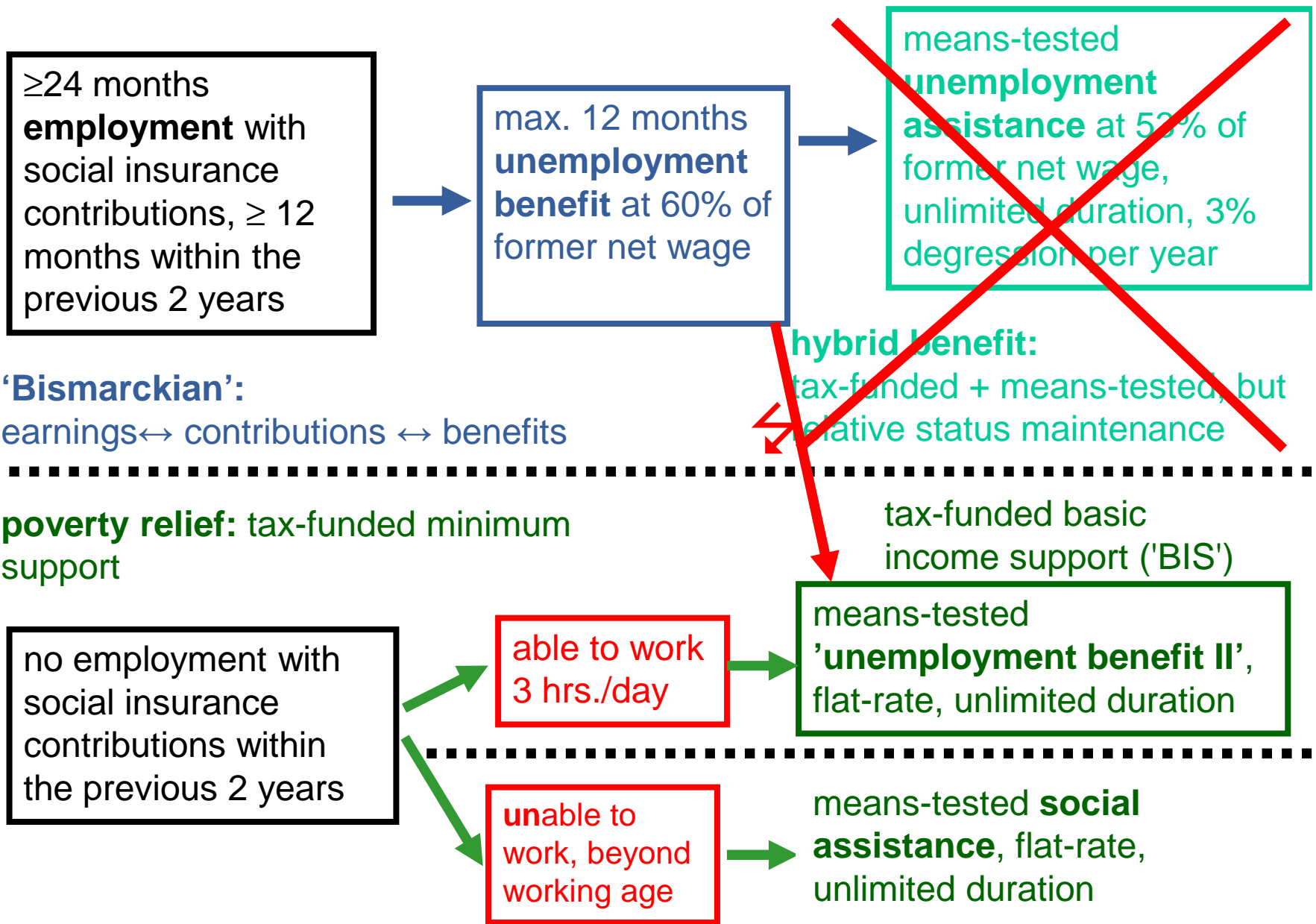
‘Bismarckian’:
earnings ↔ contributions ↔ benefits

hybrid benefit:
tax-funded + means-tested, but
relative status maintenance

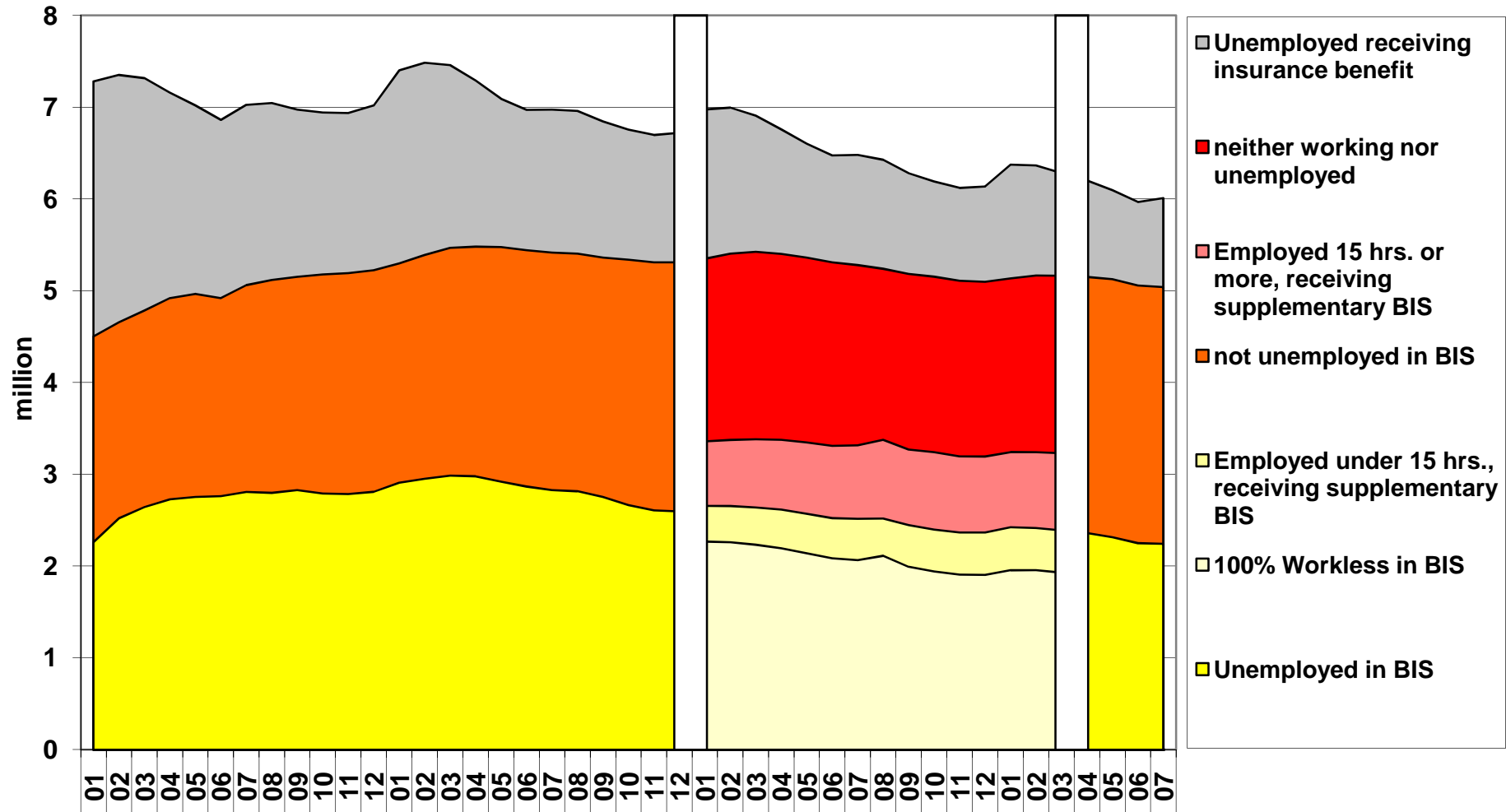
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poverty relief: tax-funded minimum support





PES 'Customer' Structure 2005 – 7/2008



Unemployment in the two regimes: Stocks, outflows into regular employment (thousands), and resulting exit rates (2005 - 2007)

	unemployment insurance			basic income support ^{*)}		
	average annual stock	outflows into regular employment	re-employment rate	average annual stock	outflows into regular employment	re-employment rate
2005	2091	2206	105%	2770	557	20%
2006	1664	2019	121%	2823	744	26%
2007	1253	1874	150%	2523	832	33%

^{*)} customers registered as unemployed only (in BIS, roughly 50% of working-age claimants); re-employment ending unemployment only (>15 hrs./week)

Basic Income Support, Current Rates

	basic rates	income support	housing & heating (emprical data)	total net income
single adult	351 €	351 €	248,57 €	600 €
adult partners	90%	631,80 €	315,36 €	947 €
15 to <25 (partner or child)	80%	280,80 €		
children < 15	60%	210,60 €		
adult couple, 1 child <15		912,60 €	370,33 €	1283 €
adult couple, 1 child <15, 1 child 15+		1193,40 €	439,81 €	1633 €
<i>single parent supplements depending on number and age of children</i>				
single parent, 1 child under 7		687,60 €	315,36 €	1003 €
single parent, 2 children under 16		889,20 €	370,33 €	1260 €
single parent, 3 children		1108,80 €	439,81 €	1548 €
single parent, 4 children		1361,40 €	542,55 €	1904 €

Criticism by social advocates:

- rates for children too low
- especially for children 6 to 15

Relevant 'Regime Aspects' of Basic Income Support

- 'Adult Worker Model' (in contradiction to male breadwinner model prevalent to the better off):
 - Adult recipients must fully **exploit every possibility** to end or reduce their need for support.
 - Formerly **inactive** spouses are thus **re-defined as 'adult workers'** as the household enters receipt of the benefit.
 - **Children under three** in general accepted as an **exemption from availability** for work (since public childcare not guaranteed for children under three).
- Almost unlimited acceptability of job offers:
 - acceptability not limited by previous training, professional practice or status
 - lower earnings, poorer working conditions, longer distance must be accepted
 - jobs paying below collective agreements or 'going rate' acceptable – no legal minimum wage in Germany
 - 'acceptable jobs' must not necessarily end need for the benefit or even end unemployment (if less than 15 hrs. per week)
- A 'benefit continued in work':
 - BIS not restricted to unemployed people but **continued in work** if need persists
 - BIS also **available while being in work** if need arises (e.g. birth of another child, job loss of partner, involuntary reduction of working hours)
 - no major and universal benefit conditional on taking up work (like working tax credits or PRE)
 - BIS = universal **benefit for the able-to-work and (more or less working) poor**

Earned Income Deduction Privilege

category of earned gross income	withdrawal rate of net income	net earnings kept on top of benefit at upper band ceiling
1 to 100 €	0	100 €
101 to 800 €	80%	140 €
801 to 1,200 €	90%	40 €
801 to 1,500 € (with at least one child <18)	90%	70 €
maximum total (no children)		280 €
maximum total (with children)		310 €

- not the principal objective of the reform – **no specific evaluation of incentives**
- obviously not easy to understand
- **fundamental incentive dilemma:**
 - 'optimal' incentive \Rightarrow incomprehensible formula \Rightarrow no incentive

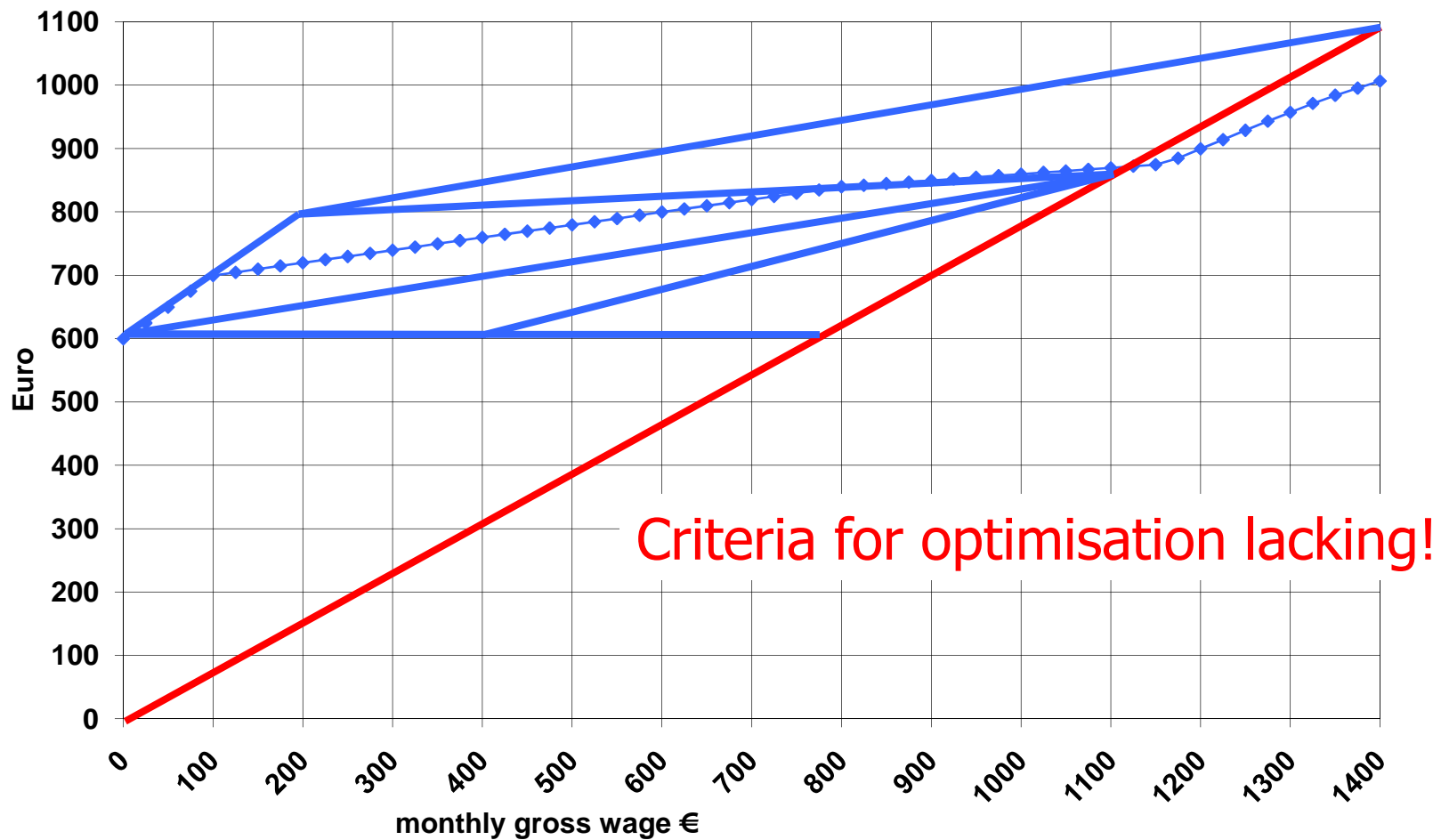
"Il semble en effet qu'il faille mettre sur pied une pédagogie du rSa..."

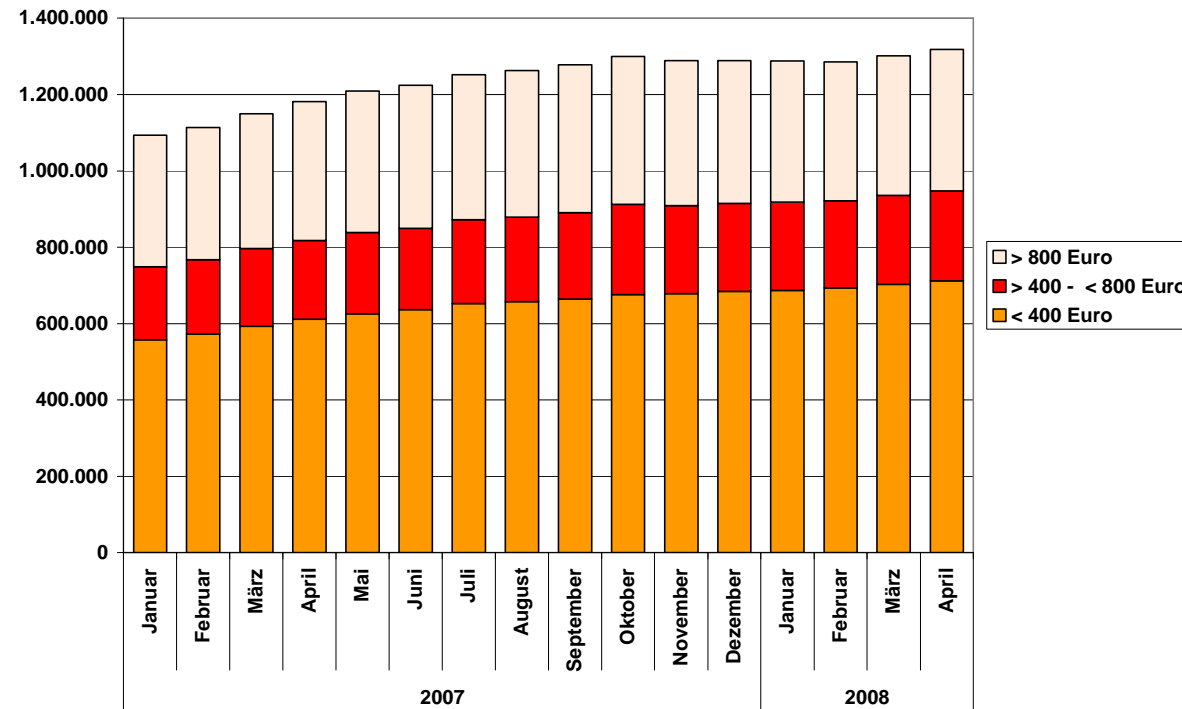
(Comité d'Evaluation des expérimentations (2008): Rapport d'étape sur l'évaluation des expérimentations rSa. Synthèse / septembre 2008, Annexe 4)

BIS as a Benefit Continued in Work: Example of Single Adult



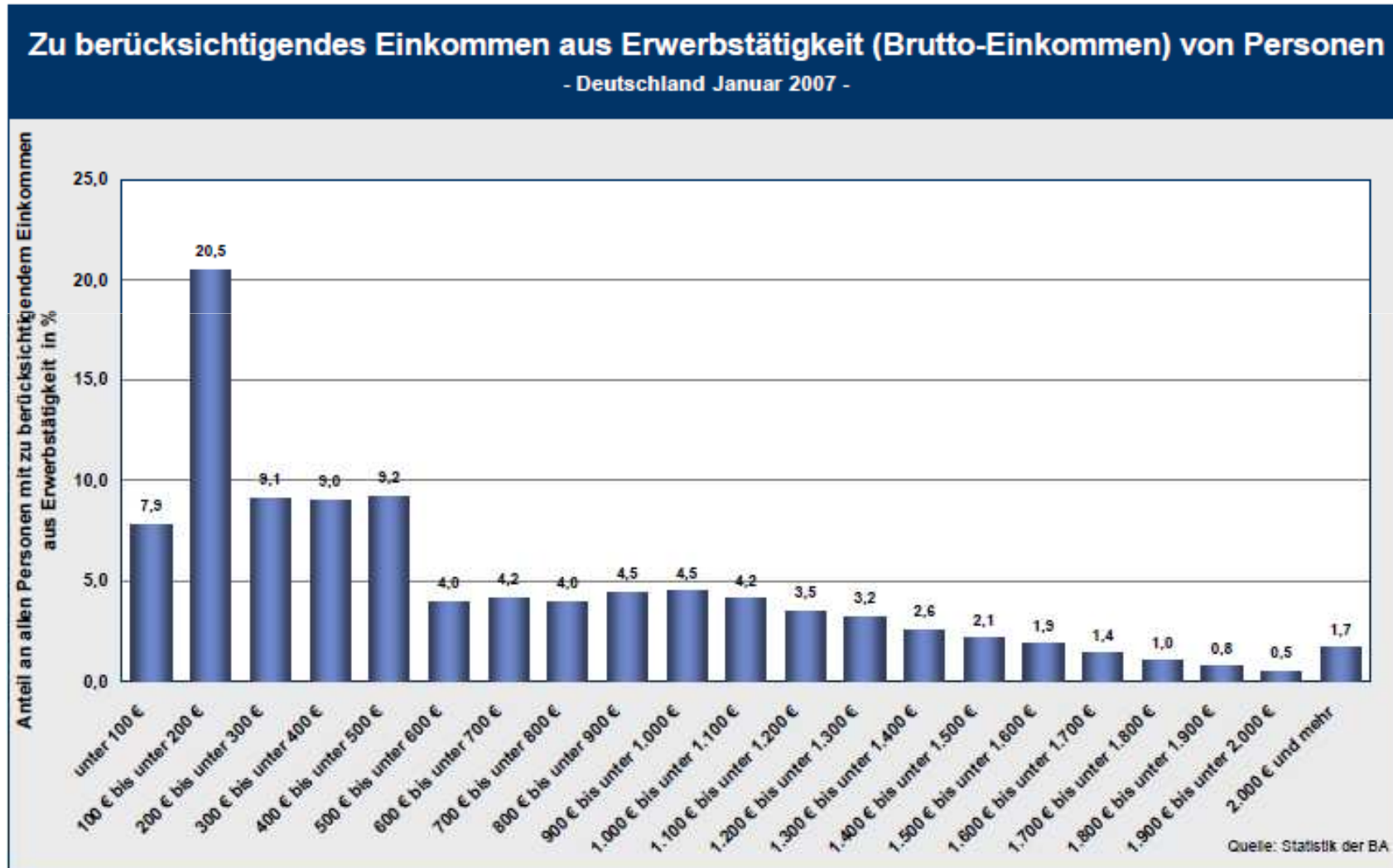
The Fundamental Incentive Dilemma of Benefits Continued in Work



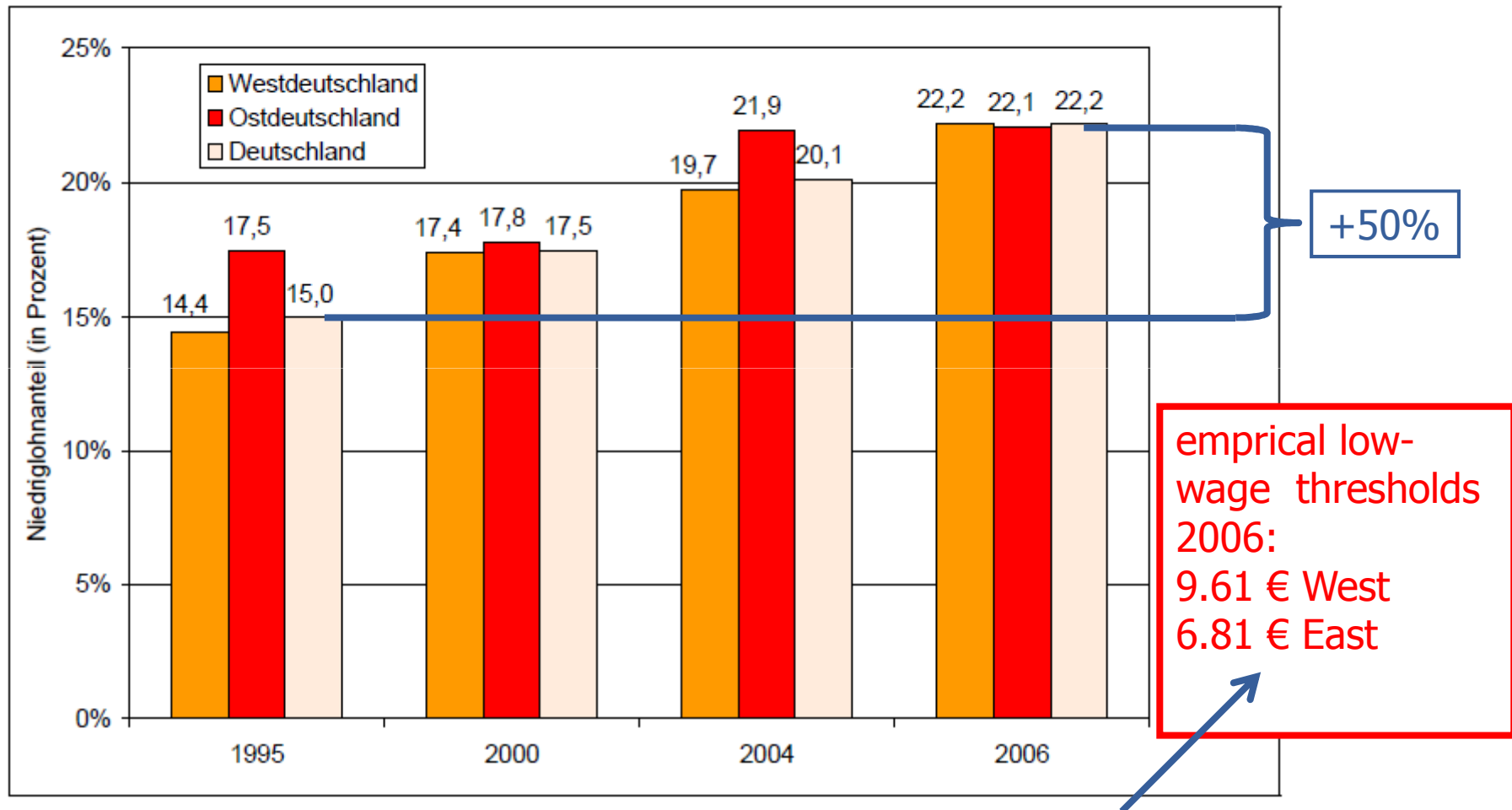


- 1.3 million \approx 25% recipients with earned income
- 20% of entries into supplementary benefit status only transitory: benefit bridges first month in work until wages are paid
- 'mini-jobs' (marginal part-time employment under 400 Euros/month) accounting for more than half of in-work benefits

Distribution of Declared Earned Incomes of BIS Recipients (Gross Income Values, January 2007)



Low-wage*) employment **West** / **East** / **Germany**



*) individual hourly wage < 2/3 median hourly wage (separate thresholds for East and West)

Source: German Socio-Economic Panel, calculations by IAQ

Weakening wage regulation

Percentage of workforce in establishments covered by collective agreement

	1996	2005
West	69%	59%
East	56%	42%

- constitutional autonomy for social partners in wage bargaining
- some collective agreements under low-wage threshold
- almost 50% of workforce not covered by collective agreements
- **no legal minimum wage**
- *erga omnes* regulation possible with consent of the concerned social partners – but without existing agreement to be extended no *erga omnes* possible

Fundamental Dilemma of In-Work Benefits in Absence of Effective Wage Regulation at Lower End

- Supplement justified because the wage is low?
- Wage low because supplement is available?
- ⇒ Subsidising **workers'** livelihoods or subsidising **employers'** labour costs?

Empirical Uncertainty – Lack of Evaluation of Flow Data:

- Low wage workers applying for supplementary benefit?
- Benefit recipients hustled into low-wage jobs?
- ⇒ 'Activating' labour market policy merely **compensating for** or **contributing to** fraying of wages at lower end?

Thank you for your attention!