

**Federal Republic of Germany**

**National Strategy Report on  
Old-Age Pension  
Provision 2005**

**(NSR 2005)**

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## **1. Foreword**

### **The open method of coordination in old-age pension provision**

Meeting in Gothenburg in June 2001, the European Council identified the ageing population as a major challenge within the European Union. The European Council noted a need for "a comprehensive plan to meet the challenges posed by an ageing society."<sup>1</sup>

For this purpose, the European Council decided, at its Stockholm meeting, to use the "open method of coordination" in old-age pension provision. Meeting in Laeken, the European Council finalised this decision and defined eleven common objectives and working methods for further co-operation. This cooperation is based on "National Strategy Reports" (NSRs), which present Member States' strategies for reforming their old-age pension systems. An initial report was submitted in 2002. At its Spring Summit, held in Brussels in March 2003, the European Council decided in the context of the Lisbon Strategy that the Member States were to submit a second National Strategy Report in 2005 dealing with old-age pension provision. In December 2004, the Member States adopted a common framework in the Social Protection Committee and agreed on a timetable. The results are to be incorporated into the joint report of the Commission and of the Council on social integration and social protection, which will be submitted to the European Council at its Spring Summit in March 2006.

### **The NSR: a major step towards European cooperation**

The old-age pension systems in the individual countries are the product of historical growth, and their structures therefore differ widely. There is no superhighway to modernisation of old-age pension provision which could be applied uniformly to all Member States. Each country must decide for itself which reform best suits its own old-age pension insurance system.

The open method of coordination however offers a framework of cooperation between Member States at European level which enables them to work together more closely. Agreeing on common objectives and working out "best practices" can help the Member States to recognise the strengths and weaknesses of their reform strategies. In this situation, the integrated approach of viewing social reforms simultaneously from a point of view of employment, economic and financial policy is regarded as particularly advantageous in both a European and a national context.

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<sup>1</sup> Item 43 of the conclusions of the Presidency.

The open method of coordination must continue to be applied in the spirit of subsidiarity. There must be no pressure for harmonisation, nor a shift of responsibilities. Responsibility for old-age pension provision must continue to rest with Member States.

### **Objective, subject and structure of the report**

The first part of the report will summarise the Federal Government's strategy in old-age pension provision policy. There will be no repeat explanation of the pensions system, reference being made to the first NSR 2002.

The second part of the NSR is devoted to a detailed description of the eleven common objectives.

Special examples and initiatives helping to meet a goal will be explained in boxed-in text passages.
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The individual reforms and their timetables will be described in Annex I, which lists all the reform legislation of the past 15 years. Individual reform steps explained in the Report can thus be viewed in their chronological context.

## **2. Summary: An overview of the Federal Government's old-age pension provision policy**

### **Meeting the challenges**

The Federal Government welcomes the focus of the Lisbon Strategy on promoting growth and employment, which are the main prerequisites for maintaining and refining the European Social Model. As decided by the European Council in March 2005, greater use must be made of all suitable means within the three dimensions of the Strategy - economy, social affairs and the environment – to make better use of its potential for synergy in the overall context of sustainable development.

Germany too is faced by the central challenge to increase economic growth and thus sustainably promote opportunities to create more employment. To amplify social cohesion, over and above this, people's knowledge must be converted to added value, innovation must be fostered and the human capital of all ages exploited. A successful solution to the problem of employment can only be found if it is understood as a task for all of society.

The "Agenda 2010" programme offers the Federal Government a coherent overall strategy for optimum use of the positive interactions of economic, employment and social policy. A major goal is to safeguard the financial foundation on which social security is based, and to reduce the ancillary wage costs. This national reform strategy is in line with the re-orientation of the Lisbon Strategy. The Federal Government has already completed reforms in this area which are among the most radical of German post-war history, thereby setting the stage for sustainable economic recovery.

Having said that, it is ultimately up to enterprises to create additional employment, and they are expected to innovate and invest in the future.

In conjunction with the other policy fields, the Federal Government's social policy makes a major contribution to promoting growth and employment. Social security is a productive economic factor which creates the major preconditions for a flourishing economy. Confidence to be able to rely on social security in case of disability, illness, need of long-term care, accident, reduced earning capacity and old age increases consumers' confidence and increases people's willingness to invest in their future and to face new vocational challenges.

The healthcare and social system, which continues to function at a high level, is a major motor for innovation and growth. Today, as many as one employee in nine is working in the healthcare system, and roughly three-quarters of these are women<sup>2</sup>. The ageing society in particular demands high-quality social services, as well as services in healthcare and in long-term care. Confidence in the system makes a major contribution towards social peace, and promotes an economic environment that fosters investment and innovation. Guaranteeing this cohesion for future generations as well is a central concern of the Federal Government's policy.

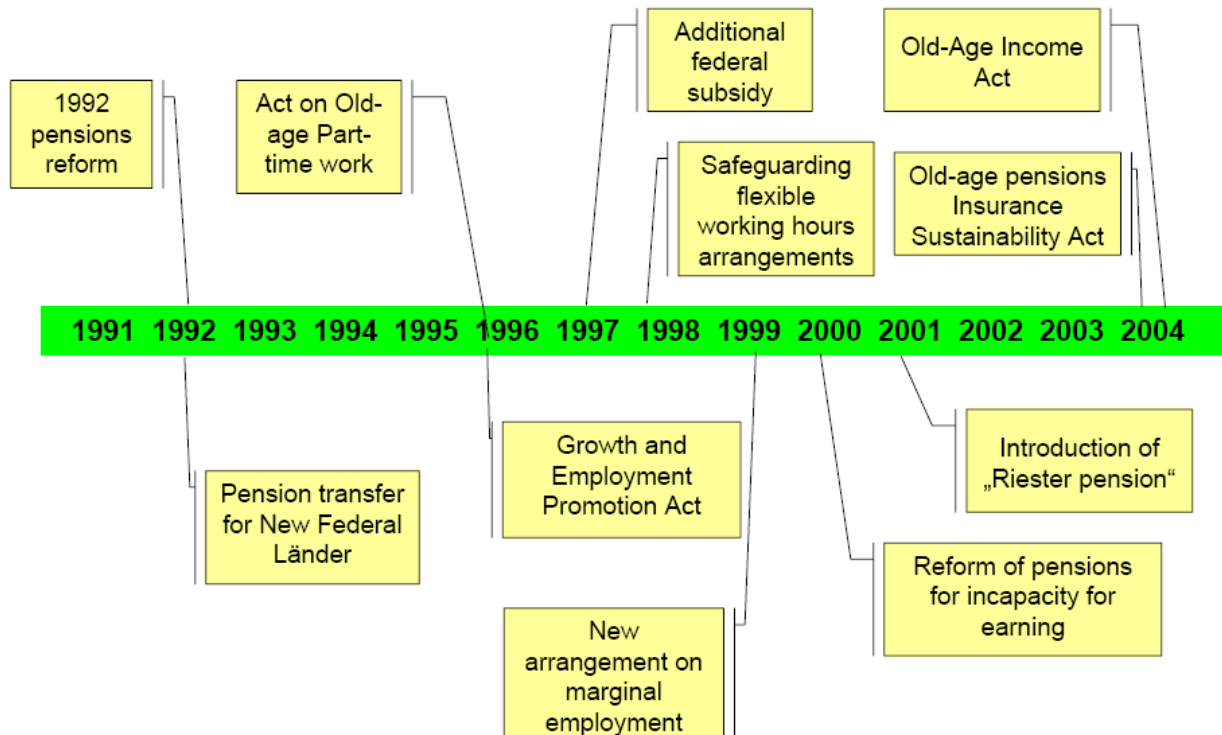
### **Building a line of defence for old-age pension provision against future demographic trends**

German old-age pension provision policy has for a number of years faced the broad-based public debate on the impact of demographic trends.

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<sup>2</sup> Federal Statistical Office, 2003

## Old-age pension provision policy since 1990



The Federal Government's latest reforms are in line with the philosophy of the outline principles established by the European Council in Gothenburg 2001: (1) to ensure that schemes are capable of meeting their social objectives; (2) to ensure that they are fundable and (3) to respond to changing social needs.

The Federal Government is consistently following the path started in the 2001 pension reform: By substantially expanding additional old-age pensions (introduction of the "Riester pension"), which receive considerable state support, adequate old-age pension provision is also guaranteed in the long term, whilst at the same time ensuring fundability.

The 2003/2004 reforms guarantee that statutory old-age pensions insurance will continue to be the first and most important pillar of old-age pension provision. The principles of statutory old-age pensions insurance are to be held on to: Funding is to be provided in a contributory procedure from equal contributions and federal subsidies, orientation of the amount of pensions to the insured parties' previous payments and pensioners' participation in the economic trends by adjusting pensions in line with wages.

With these reforms, the Federal Government has reacted to economic trends which were less favourable than could be presumed at the time of adoption of the 2001 pension reform.

What is more, the new population forecast<sup>3</sup> presented in 2003 brought to light a gratifying increase in life expectancy, as a result of which the presumptions on which the 2001 reform was based had to be revised in some instances. The measures adopted in 2004 are based largely on proposals put forward by the "Commission for Sustainable Funding of the Social Security Systems" set up by the Federal Government, the members of which included socially-relevant groups, in addition to representatives from the academic field.

## **Core concerns of the Federal Government's reform of old -age pension provision**

### **Statutory target values for pension levels and contribution rates**

- The Federal Government's pensions policy is orientated in line with clear, equal goals set in the long term until 2030 as to the contribution rate and the pensions level.
- With these targets, which are entrenched in legislation, the political arena has placed itself under a long-term obligation.
- The reforms that have been carried out in the field of old-age pension provision serve to ensure that pensions are fundable in the long term, and which are adequate, from the first pillar of statutory old-age pensions insurance. Despite the foreseeable demographic trends, the lower limit of the level of provision before tax should not go below 46 % until 2020 and 43 % until 2030<sup>4</sup>. From 2008, the Federal Government is also obliged to make proposals to the legislative bodies every four years demonstrating how to achieve this target level of provision beyond 2020 whilst at the same time maintaining stable contribution rates.
- The contribution rate is to be 20 % until 2020 and not to exceed 22 % until 2030.
- Regular duties incumbent on the Federal Government to report to Parliament ensure that the goals are met.
- The Federal Government must report for the first time in 2008 in the old-age pension insurance report on trends in the employment of elderly employees, and must give an assessment of whether an increase in the statutory standard age-limits is necessary, and whether such an increase is acceptable, to slow the rise in the contribution rate in the long term, taking account of the situation on the labour market, and of the economic and social situation of elderly employees.

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<sup>3</sup> "Bevölkerung Deutschlands bis 2050 – Ergebnisse der 10. koordinierten Bevölkerungsvorausberechnung", Report of the Federal Statistical Office, Wiesbaden, 2003

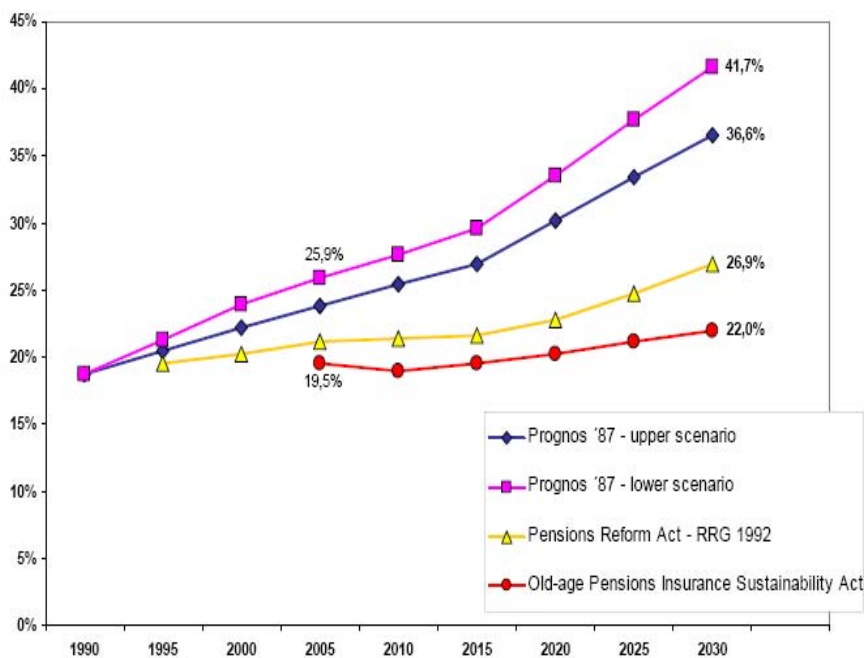
<sup>4</sup> The level of provision before tax is the ratio of the standard disposable pension to average disposable earnings (before tax and not including either the average contribution share to health insurance or the contribution to long-term care insurance). It is calculated for the so-called standard pensioner who has earned the average income for 45 years, paid appropriate contributions and retires at 65. Information on trends in the level of provision before tax can however be transferred to all income careers and the level of pension provision accrued.



### Safeguarding pensions in a manner promoting employment and growth

- Contribution rates that are stable in the long term safeguard employment. The pension reforms hence make a major contribution towards stabilising the ancillary wage costs and increasing employment. Without the measures that have been taken, the contribution rate would have been 1 contribution rate point higher in 2004 than the actual contribution rate, and in 2005 would have been 0.6 contribution rate points higher. By 2030, the contribution rate will be 2.3 contribution rate points lower as a result of the reforms.

#### Trends in contribution rates with and without reforms<sup>5</sup>



- The redefinition of the lower limit of the level of provision before tax reduces the burden on the federal budget. The room for manoeuvre thus created in financial policy can be used to consolidate the budget, for important future investments and to produce a further reduction in the burden of taxes and charges.
- By continuing to index benefits to wages and contributions, statutory old-age pensions insurance provides a direct incitement for insured parties to enter employment. Also in future, any period spent in employment directly increases the subsequent pension.

<sup>5</sup> The scenarios of Prognos '87 and the subsequent reforms of 1992 and 2004 are not fully comparable since they were based on different macroeconomic and demographic presumptions.

- This effect is amplified by actuarially-calculated reductions that are imposed in the event of early retirement, or bonuses in the event of retirement after the statutory standard age-limit, as well as by abolishing possibilities to take early retirement without incurring a reduction in pension.
- The figure for gainfully-employed elderly employees has increased in contradistinction to the general trend on the German labour market. The figure for gainfully-employment elderly employees was 41.2 % in 2004. This means an increase of 2.5 percentage points as against 2002 (38.7 %).
- It has also been possible to continually increase the actual retirement age from the end of the nineties onwards. The average age of old-age retirement increased from 62.2 to 62.9 in 1998 to 2003. These trends are based not lastly on the expiry of the possibilities to draw an old-age pension without reductions before reaching the age of 65.

#### **Expansion of additional old-age pensions**

- In order to prevent the measures applied to first-pillar contributory pension schemes to alter the level of provision before tax, leading to reductions in old-age pension provision, the gap which arises can be closed by additional private and occupational retirement provision. Massive state support is provided for such private or occupational retirement provision, the promotion measures ensuring in particular that those on low wages can also make provision to the envisaged degree. The Old-Age Income Act (*Alterseinkünftegesetz*), which entered into force on 1 January 2005, creates an attractive framework for additional old-age pensions.
- Conversion to downstream taxation decreases the burden on employee income, thereby releasing additional funds which are to be used for private old-age pension provision.
- The effect of the reforms on the expansion of additional old-age pensions can already be clearly seen. Occupational retirement provision in Germany has said farewell to decades of stagnation, and is experiencing a renaissance towards universal cover. 15 months after the entry into force of the reform (as on 31 March 2003), roughly 15.3 million employees already had occupational retirement provision entitlements, corresponding to roughly 57 % of all employees subject to social security payments. In addition, approx. 4.2 million private pension contracts ("Riester pensions") had been concluded by the end of December 2004, so that roughly 20 million citizens should already have state-promoted additional old-age pensions.

In addition to the "Riester contracts", to which downstream taxation is applied, contracts to which upstream tax is applied currently constitute a large portion of private pension contracts in Germany. Since the "Riester reform", roughly 11 million new private old-age pension insurance contracts<sup>6</sup> (incl. roughly 3.7 million contracts with "Riester promotion") were concluded in the insurance industry alone between the beginning of 2002 and the end of 2004. There are also roughly 550,000 "Riester contracts" in banking and fund management. These figures demonstrate that the paradigm shift in pensions initiated by the Federal Government in 2001 is under full steam, and that the share of private pensions among the universal spread of capital-covered pensions is considerable.

Strengthening supplementary old-age pension provision remains a long-term process. Because of the significant role played by the first pillar in Germany, an awareness of the need for additional old-age pensions is developing only slowly. The reforms need time to exert their full impact. The expansion to date is particularly pleasing because it took place in an economically difficult period.

### **Maintaining fairness between generations**

- The reforms ensure an adequate exchange between the generations. In order to limit the burden on employees as to contributions, the lower target value of the level of provision before tax is being moderately reduced. A sustainability factor has been introduced in the pensions adjustment formula (cf. objective 7) which accommodates the quantitative relationship between those drawing benefits and those employed subject to obligatory insurance. In addition, earnings-linked pensions are orientated in line with the gross wages and salaries on which the contributions are levied.
- At the same time, it is established that there must be no negative pensions adjustment solely due to the effect of the sustainability factor or of the proportion of old-age provision.
- The reforms ensure that statutory old-age pensions insurance also remains the most important element for future generations to safeguard the standard of living established in the earning phase.

### **Transparency of decisions**

- The insurers are involved in all reforms. The latter are independent and are only subject to the State's legal supervision.

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<sup>6</sup> Not including direct insurance policies and employer's pension liability insurance.

- The insured parties can exert a direct influence by means of regular social elections to the insurers' parliaments, the latest of which are to take place in 2005.
- The establishment of an independent "Commission for Sustainable Funding of the Social Security Systems" has prepared and exerted a strong influence on pensions reform in Germany.
- Social partners and associations have been constantly involved in the reforms.
- Transparency is also favoured by the considerable duties to report to Parliament that are incumbent on the Federal Government. Reporting encompasses in particular the annual old-age pension insurance report, the quadrennial old-age pension provision report and, from 2008, the quadrennial report on the situation of elderly employees.
- As an advisory body, the independent Social Advisory Board submits statements on the Federal Government's annual old-age pension insurance report.

#### **Predictability of subsequent pensions**

- Insured parties can where required request detailed information on their pension entitlement from their statutory old-age pension insurer.
- Over and above this, the insurers have been obliged since 2004 to send annual "Pension information" to all insured parties from the age of 27 which also contains a forecast of the likely pension.
- From the age of 54 onwards, insured parties receive specific pension information, indicating the conditions applying to their pension rights.

#### **Orientation of the reforms towards the principle of equal treatment**

- Over and above this, it is a principle concern for the Federal Government to actively promote the equality of women and men.
- Many provisions favour above all the accrual of personal entitlements for women. Particular attention focuses here on the possibility created in 2001 to split pension entitlements for spouses, and on the higher evaluation of employment periods in addition to child-rearing.
- The Old-Age Income Act prescribes unisex tariffs for the promoted additional private pensions from 2006 onwards.

### **3. The individual objectives – challenge and encounter**

#### **3.1. Adequacy of pensions**

**The Member States should safeguard the capacity of pensions systems to meet their social objectives. To this end against the background of their specific national circumstances, they should:**

##### **Objective 1**

**Ensure that older people are not placed at risk of poverty and can enjoy a decent standard of living; that they share in the economic well-being of their country and can accordingly participate actively in public, social and cultural life.**

##### **Integration is a task for all of society**

The German old-age pension insurance system is in principle structured such that the benefits enjoyed at retirement age correspond to the insured parties' contributions and that pensioners share in economic trends by means of wage-orientated pension adjustments. Old-age pensions hence symbolise replacement of the income from the previous wage-earning activity – they do not simply serve to provide minimum financial security. Over and above this, statutory old-age pensions insurance opens up comprehensive access to healthcare services and long-term care in old age<sup>7</sup>.

The total social security benefits, as well as locally-entrenched support for the elderly, form the financial and social basis for the maintenance of active participation in public, social and cultural life.

This perception of the task of integration spanning society as a whole is successful. If one presumes a relative definition of poverty, it is shown that the risk of low income among the elderly in Germany has already fallen noticeably since 1998. According to the weighting of the new 2003 OECD scale it is 11.4 %, and according to the old OECD scale it is 7.5 %, and thus lower than for the population as a whole (13.5 % and 13.1 % respectively). If one considers pensioners as a group, their poverty risk rate is 11.8 % and 7.8 % respectively (cf. Annex II).

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<sup>7</sup>On principle, starting to draw a pension gives rise to obligatory health and long-term care insurance for pensioners. This means that full health and long-term care insurance protection commences irrespectively of the amount of the pension payment. The contributions are levied as a percentage of the pension, are retained by the old-age pension insurer and transferred to the respective health/long-term care insurance fund. The old-age pension insurer provides half the health insurance contribution, whilst the pensioner pays the other half (average 7.15 %) and the full long-term care insurance contribution (1.7 %).

### **Basic insurance in old age and in case of reduction of earning capacity**

To achieve a minimum financial standard and to prevent covert poverty in old age, basic insurance in old age and in case of reduction of earning capacity was introduced in the beginning of 2003. Beneficiaries are persons from the age of 65, as well as those from the age of 18 onwards whose earning capacity is fully reduced in the long term for medical reasons. The basic insurance is not an old-age pensions insurance benefit, but a social assistance benefit. For this reason, benefits from basic insurance can only be drawn by those in need. Need applies if necessary subsistence cannot be acquired from available income and assets. In distinction to social assistance, there is no recourse to the children of the basic insurance beneficiary in order to reduce thresholds in claiming the benefit.

In order to be able to reach the target group of elderly people in need, who are nevertheless difficult to reach, old-age pensions insurers are obliged to indicate the benefits of basic insurance with newly-ascertained pensions the monthly amount of which is less than a certain amount (2005: Euro 705.51).

According to the data available to date, benefits totalling about Euro 1.46 billion were paid in 2003 to about 439,000 persons. About 59 % of the beneficiaries were 65 and older; in total, 1.8 % of all persons from the age of 65 received benefits.

### **Participation in society**

Financial security in old age is only one aspect of coping with demographic change. The expectation of ageing healthily and actively offers significant challenges not only to the pensions system, but also to the healthcare system and to statutory long-term care insurance.

As the number of elderly persons increases, the number of chronic diseases will also continue to rise. Their treatment is one of the laborious and hence very expensive tasks of the healthcare system. Through the Act to Boost Preventive Healthcare (Gesetz zur Stärkung der gesundheitlichen Prävention - Präventionsgesetz)<sup>8</sup> the onset of chronic diseases can be prevented and the burden of the disease minimised by increasing the preventive healthcare available (cf. Annex III on the Prevention Act).

Another consequence of demographic change will be the increase in the need for long-term care. Preventative healthcare can also help people here to lead a mobile and self-determined life for as long as possible and to take an active part in society.

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<sup>8</sup> The Act to Boost Preventive Healthcare was adopted on 22 April 2005 by the German Federal Parliament, and must still be adopted by the Federal Council.

## **Objective 2**

**The Member States should provide access for all individuals to appropriate pension arrangements, public and/or private, which allow them to earn pension entitlements enabling them to maintain, to a reasonable degree, their living standard after retirement.**

**Statutory old-age pensions insurance remains the first and most important pillar of the old-age pension provision in Germany.**

The recently-completed study of old-age pension provision in Germany in 2003 (ASID03) provides the following figures on this: In the old Länder, 91% of the male residential population aged above 65 have their own statutory pensions, the figure being 82 % among women. In the new Länder, the share is 99 % in each case. Over and above this, 87 % of widows aged from 65 onwards in the old Länder and 99 % of widows in the new Länder receive a surviving dependants pension from statutory old-age pensions insurance.

The significance of the individual systems within the overall structure of old-age pension provision can also be made clear by showing the composition of the volume of gross incomes. Accordingly, 66 % of all income of those aged 65 and older comes from statutory old-age pensions insurance. Here, the table shows considerable differences by civil status and area. As one would expect, the share of statutory old-age pensions insurance in the new Länder is much higher than in the old. There is also a higher share among single women than among single men or spouses. Income elements from private pensions still play a subordinate role, where they were stated by the respondents, in the new Länder in comparison to the old.

The most important sources of income of the population aged 65 and older (as a percentage of gross income volume)

Source of income	All	Spouses		Single men		Single women	
		West	East	West	East	West	East
Statutory old-age pensions insurance	66	57	89	60	87	68	95
Other old-age pension provision systems	21	26	2	26	5	22	2
Wage-earning activity	4	7	5	3	1	1	0
Interest, letting, life insurance et al.	7	9	3	9	6	6	2
Housing benefit/social assistance/basic insurance	1	0	0	1	1	1	1
Total	100	100	100	100	100	100	100

0 = less than 0.5, but more than 0, Deviations from 100 % in the total arise from rounding the figures.  
Source: Old-age Pension Provision in Germany (ASID) 2003 (ASID03), Federal Ministry of Health and Social Security

### **Safeguarding pensions in the long run**

The Old-age Pensions Insurance Sustainability Act 2004 continues the reform efforts from 2001 and, as an element of the Federal Government's Agenda 2010, forms a part of the programme to safeguard the social systems in the long term. The measures provided for in this Act are a reaction to the challenges presented by the demographic trends, and safeguard funding of old-age pensions insurance.

The core of the Old-age Pensions Insurance Sustainability Act is the introduction of the so-called sustainability factor in the pension adjustment formula. The quantitative ratio of beneficiaries and employees with obligatory insurance is therefore accommodated in adjusting the pensions. Additionally, to ascertain wage trends, greater emphasis is to be placed in future on the pensionable wage and salary total. As a result, the level of provision before tax will fall in comparison to today's level. The pension of an average earner with a normal working life will however also be much higher in future than the level of basic insurance.

A statutory clause to safeguard pension levels serves to ensure pension levels in the long term. The level of provision before tax should be maintained at a minimum of 46 % until 2020 and of 43 % until 2030. This level of provision before tax will have the same status as maintaining the contribution rate at a maximum of 20 % until 2020 and at 22 % until 2030, as also stated in the Act. To ensure that these goals are met, the Federal Government is to propose suitable measures to the appropriate legislative bodies.



In order to safeguard standards of living in old age, it is necessary to form an additional old-age pension in the shape of an occupational and/or private capital-covered pension, in addition to statutory old-age pensions insurance. Persons on a low or average income are particularly encouraged to seek such coverage.

### **Occupational retirement provision for all employees**

Access to occupational retirement provision has been markedly improved. Since 1 January 2002, employees have in principle been entitled to apply to their employers for accumulation of occupational retirement provision by paying contributions from their earnings ("remuneration conversion"). Employees may therefore take the initiative themselves if they are aware of a need for a pension. An additional incentive is available if employers for their part contribute financially towards building up their employees' occupational retirement provision. Immediate statutory vesting is introduced for entitlements gained through remuneration conversion. For entitlements which are funded by the employer, the statutory deadlines for statutory vesting have been shortened from ten to five years. Furthermore, occupational retirement provision has been strengthened by advantageous tax exemption and freedom from contributions.

The Old-Age Income Act entered into force on 1 January 2005, amongst other things expanding, standardising and simplifying fiscal promotion of fully funded occupational retirement provision. Fiscal promotion – not subjecting contributions to tax – is accompanied by partial exemption from social insurance contributions applying to contributions paid in the framework of remuneration conversion, this however only applying until the end of 2008. The new promotion measures, comprising tax breaks of about Euro 4,300 per year for new contracts from 1 January 2005, and with no social insurance contributions due on about Euro 2,500 per year, offer a strong argument for the further expansion of the second pillar. Additionally, promotion is also possible in the framework of occupational retirement provision, as described in the following section, as is also the case with private pensions ("Riester pension") by means of subsidies and additional deduction of special expenditure.

The legislature considers the best way of achieving across-the-board voluntary coverage to lie above all in the inclusion of occupational retirement provision in collective agreements. Another major argument for the further spread of occupational retirement provision is the cost and efficiency advantages resulting from collective implementation, which as a rule are superior to purely individual private pensions (cf. Objective 8).

The expansion of additional old-age pensions is a laborious process which is gradually accelerating. Current figures regarding the situation and trends of additional old-age pensions in the framework of the Federal Government's old-age pension provision report are to be

submitted by November 2005. On the basis of the new data, the Federal Government will decide whether, as provided in law, it will "propose to the statutory bodies suitable measures should it emerge that a sufficient spread cannot be achieved by the promotion of voluntary additional old-age pensions" (section 154 of Book Six of the Social Code [SGB VI]).

The available data are encouraging. An awareness is increasingly developing among the population of the need to make an active contribution towards old-age pensions. 15 months after the entry into force of the reform (on 31 March 2003) the share of employees in private industry with a right to occupational retirement provision had increased from 38 % to 43 %. Between January 2002 and March 2003, roughly 300,000 companies had introduced a new additional old-age pension or expanded their existing additional old-age pension scheme. On that date, therefore, roughly 57 % of all employees subject to social security payments (in private industry and the public service) had occupational retirement provision.

#### **Expanded deduction of special expenses for pension expenditure**

Expenses invested in a basic pension in old age are increasingly made tax-free by the Old-Age Income Act. These include in addition to the contributions to statutory old-age pensions insurance, to the agricultural old-age pension funds and to certain professional pension schemes, contributions to private annuity, if these meet the criteria for promotion.

#### **State-promoted private pensions**

Private capital-covered pensions ("Riester pension") are more flexible and citizen-friendly, with the Old-Age Income Act entering into force on 1 January 2005 above all by the introduction of a long-term bonus application, the reduction of the certification criteria, expanded possibilities to withdraw a lump sum and improved consumer information. Expenditure on pensions will also be increasingly tax-free from 2005 onwards, so that employees have more funds to invest in their additional old-age pensions.

The group of beneficiaries on principle includes everyone ultimately affected by the limited reduction in pension levels. In addition to employees, these include recipients of supplementary wage benefits, compulsorily insurable care personnel, non-earning parents caring for children, compulsorily insurable self-employed persons, as well as farmers and civil servants.

The beneficiaries pay their own contribution towards a suitable subsidised contract. The state subsidy is credited to their contract on request via the provider.

The pension subsidy consists of a basic subsidy and a child subsidy. Taxpayers can claim an additional deduction of special expenses for their pension contributions within certain limits by virtue of an examination to be carried out ex officio of the constellation which is most favourable for them.

After reaching the final phase of promotion in 2008, 4 % of the previous year's income is to be saved annually. This amount must not be contributed by the beneficiaries alone. It is made up of their own savings, to which is added the basic subsidy of Euro 154, and where appropriate the child subsidy of Euro 185 per child. Additionally, the personal contributions plus the subsidies can be deducted from tax to a maximum of Euro 2,100 per year. Depending on income and the number of children, promotion is between 24 % and more than 90 % of the amount saved.

Private pensions do not reach the highest promotion level until 2008, but they are already worthwhile today, as shown by an example: A family with two children had an income of Euro 20,000 subject to social security payments in 2004 (one-earner household). The personal contribution to be made by the family for 2005 is only Euro 64 (2 % of Euro 20,000 = Euro 400 minus subsidies [Euro 2 x 76 + Euro 2 x 92]). The family hence receives subsidies of Euro 336 for an individual contribution of Euro 64. This corresponds to a promotion rate of 84 %, on condition that both parents conclude a promoted pension agreement, and the sole-earner pays Euro 64 in personal contributions.

About 4.2 million private pension contracts were concluded by the end of 2004 in state-promoted capital-covered additional private pensions.

### **Objective 3**

**The Member States should promote solidarity within and between generations.**

Solidarity is, was and remains a characteristic of the German pensions system. This applies both to solidarity within and between generations.

### **Statutory old-age pensions insurance**

As is also the case with social insurance, which is obligatory for broad sections of the population, statutory old-age pensions insurance in Germany is also used to implement social policy objectives.

In addition to simple insurance risk compensation, redistribution within generations is based on the contribution measurement for insured parties which are included in insurance protection without accounting for any restrictions imposed by the state of health, the existence of other risks and gender. Above all, the risk of premature incapacity for earning is covered, regardless of previous illnesses or of the age of the insured parties.

Compensation based on solidarity also takes place for times in which no contribution payments were made, or in which contributions were insufficient. Since these redistribution measures can be regarded as a task for society as a whole, statutory old-age pensions insurance receives benefits from the Federal budget for this, but not only for this. Thus, for instance, federal subsidies and contributions from the Federation towards pensionable child-rearing times were approx. Euro 77.4 billion in 2004.

By taking account of the "proportion of old-age provision" factor in the pensions adjustment formula applicable since 2001, pensioners also make a contribution based on solidarity so that today's working generation is given financial scope to establish old-age assets. In addition to changes in the contribution rate to old-age pensions insurance, employees' expenditure on additional old-age pensions is also abstractly accounted for in ascertaining the adjustment rate. Tax changes and changes in the contribution rate not related to pensions are moreover no longer considered when adjusting pensions.

Additionally, the introduction of the sustainability factor in 2004 accommodated the ratio of beneficiaries and employees with obligatory insurance in the pension adjustment. Hence, a major contribution is made towards ensuring that contributors are not overburdened by demographic trends, and that the pension beneficiaries continue to share in economic prosperity.

### **Downstream taxation**

The Old-Age Income Act initiated the transition to downstream taxation of old-age income and towards tax-free pension expenditure. Downstream taxation means that old-age income is not taxed until disbursed to tax payers, in other words in old age. In return, contributions to pensions in the working phase remain untaxed up to a maximum annual amount. Younger insured parties then have more money available in net terms, which they should use to build up an additional occupational or private pension.

However, conversion to the new system does not take place overnight, but in annual steps for reasons of respect for conditions already granted and to avoid double taxation: A 20-year transitional phase is planned for the non-taxability of the old-age pensions insurance contributions in the working phase. In future, expenditure for pensions will be increased in steps up to a maximum of Euro 20,000, starting with the increase in 2005 to a minimum of 60 % of the contributions paid within the maximum amount, including the employer portion (Euro 12,000). This rate will be increased on an annual basis by two percentage points in each of the ensuing years, so that 100 % of expenses can be deducted from 2025. Accordingly, the maximum volume to be accommodated as special expenses will also increase from its starting level of Euro 12,000, up to Euro 20,000.

A 35-year transitional period is envisioned to convert pension taxation. From 2005 onwards, the fiscally covered share of pensions is 50 % for existing pensioners. For each year of pensioners added from 2006 onwards, this percentage is to increase in steps of two percentage points, to reach 80 % in 2020, and then in steps of one percentage point, reaching 100 % in 2040.

### **Additional old-age pensions**

Additional old-age pensions also encompass many solidarity-related elements. In addition to the unisex tariffs applicable from 1 January 2006 onwards (cf. on this at Objective 10) and occupational retirement provision agreements, which as a rule already provide for equal treatment for men and women (despite their different life expectancies) mention should be made here above all of the common pensions for incapacity for earning of occupational retirement provision.

In order to make it possible for employees with low and medium incomes to also spend money on additional capital-covered pensions, and over and above this to establish family policy elements in the additional capital-covered pensions, the State grants uniform subsidies which in the final phase from 2008 reach Euro 154 per adult per year and Euro 185 per child per year. These and other fiscal promotions are taken from the public budgets to which taxpayers contribute in accordance with their ability to pay. Also the second and third pillars are hence co-funded in Germany such that households with a high income help build up cross-generational old-age assets based on the principle of solidarity for those on a low income<sup>9</sup>.

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<sup>9</sup> The fiscal promotion of private capital-covered pensions is guaranteed by two overlapping elements: Firstly, by the deduction of special expenses for pension contributions, so that contributions can consequently be made from non-taxable income; secondly, via supplementary subsidies composed of basic subsidies and child subsidies. The needs in particular of those on low incomes and families with many children are accommodated by these subsidies. This orientation of the granting of subsidies serves to safeguard additional old-age income for persons who are very heavily dependent on supplementary income in old age, in addition to statutory pensions. Details are provided in Part 2 of Annex IV.

### **3.2. Financial sustainability of pension systems**

**Member States should follow a multi-faceted strategy to place pension systems on a sound financial footing, including a suitable combination of policies to:**

#### **Objective 4**

**Achieve a high level of employment through, where necessary, comprehensive labour market reforms, as provided by the European Employment Strategy and in a way consistent with the BEPG.**

There is a close connection between pensionable employment, economic growth and the financial sustainability of the social security systems. A high level of employment is a precondition for well-functioning old-age pension provision in a contributory procedure, and at the same time a guarantor for the suitability of future pension claims. Putting people in work is therefore a priority policy goal of the Federal Government.

After German reunification, employment levels in the group of 15 - 64 year-olds first dropped continuously, reaching their lowest point in 1997 at 63.7%. In the ensuing years, an upward trend set in, which continued until 2001. From 2001 to 2003, the figure for those in employment fell by 0.8 percentage points to 64.3 %. Despite the trends in recent years, Germany is confident that it can achieve the Lisbon target (70% by 2010).

Women's employment levels also rose continuously until 2001, and have been constant at 58.4 % since then. Thus, Germany already fulfils the interim target agreed in Stockholm (57% in 2005), and is sure to achieve the Lisbon target with a minimum of 60 % in 2010.

#### **Labour market reform**

The "Modern Services on the Labour Market" Committee of Experts established by the Federal Government, chaired by Peter Hartz, drafted specific proposals in 2002 for a comprehensive reform of the labour market. These proposals form the basis of the four Acts for Modern Services on the Labour Market (Gesetze für moderne Dienstleistungen am Arbeitsmarkt).

The First and Second Acts for Modern Services on the Labour Market entered into force in 2003 and help open up new employment opportunities and support the creation of new jobs. The altered legal framework and the conversion of the Federal Employment Agency which has been set underway will lead to a comprehensive improvement in the quality and speed of placement, and will re-structure the services offered by the job centres to make them customer-friendly. The most important new approaches are:

- setting up Personnel Service Agencies (PSAs),
- abolishing existing restrictions in the Act on Commercial Provision of Labour (Arbeitnehmerüberlassungsgesetz),
- re-defining the further training market,
- expanding self-employment in the shape of the "Me Inc." (Ich-AG),
- reforming mini jobs and introducing midi jobs (cf. Objective 9).

The Federal Government has amended the Redundancy Protection Act (Kündigungsschutzgesetz) and the Part-Time and Fixed-Term Employment Act through the Act Reforming the Labour Market (Gesetz zu Reformen am Arbeitsmarkt) in order to promote new appointments in small and newly-founded enterprises in particular.

The application threshold of the Redundancy Protection Act has been changed. In companies with ten or fewer employees, the Act on Protection against Redundancy does not apply to employees appointed from January 2004 onwards. Employees already in work in companies with more than five employees retain their previous redundancy protection. The new threshold value is intended to encourage tradespersons and small businesses to react to a favourable order book faster than was previously the case by taking on new people, and hence to open up better employment opportunities to those in search of work. Furthermore, fixed-term employment of employees has been made easier for start-ups (amendment to the Part-Time and Fixed-Term Employment Act). Fixed-term employment contracts for up to a period of four years can be concluded in the first four years of the existence of a newly-founded enterprise with no objective reason. Hence, many new businesses have easier launching conditions for a longer period of time, above all in the new Federal Länder.

The Third Act for Modern Services on the Labour Market was another step towards the modernisation of the labour market in Germany. It entered into force on 1 January 2004. Its core is the conversion of the labour organisation to become the Federal Employment Agency. It contains provisions on structural changes in the organisation and control of the Federal Agency, with which it enables the staff of the Federal Employment Agency to concentrate more on placing the unemployed.

The Fourth Act for Modern Services on the Labour Market combined unemployment relief and social assistance for those with earning capacity to create a new benefit, namely basic insurance for those in search of work (unemployment benefit II), as on 1 January 2005, in order to improve the integration opportunities for beneficiaries in non-promoted employment. The introduction of uniform basic insurance for those in search of work is the central element of the

new labour market policy. This is a standard benefit that is granted in accordance with requirement to provide subsistence to those in need who have earning capacity and to those dependants without earning capacity living in interdependent co-habitation with them (unemployment benefit II or social benefit). The focus of the new benefits system is rapid placement in suitable work in accordance with the "promote and challenge" principle. The new system has given roughly one million social assistance recipients with earning capacity access to promotion and placement services for the first time which were previously reserved to the recipients of unemployment relief.

Juveniles up to an age of 25 years will in future receive special care so that each one has the opportunity to enter the world of work. Anyone under 25 who applies for unemployment benefit II is entitled to be immediately placed in training, work, an internship, skill-building project or a measure preparing for work (promotional benefit).

New tools have been created in order to make it easier for the long-term unemployed to get back to work:

- The initial benefit offers an incentive to those seeking work to accept low-paid employment.
- The additional job ("One-Euro Job") helps those seeking work to open up new prospects, while making a full contribution to the community.
- In addition, by providing possibilities for additional earnings, incentives to take up employment have been planned which are to build a bridge to wage-earning activity.

### **Contribution rate stability as a productive factor**

As early as in the 2001 pension reform, statutory old-age pensions insurance was adjusted to the coming demographic trends and the possibilities of supplemental private and occupational provision improved by state promotion. By means of the amendments which the legislature already adopted in 2003, it was possible to prevent an increase in contribution rates that had been feared for the period from 2004 onwards on the basis of economic trends, and to avert the resulting damaging effects on growth and employment.

With the Old-age Pensions Insurance Sustainability Act adopted in 2004, further measures with medium- and long-term effect ensued to stabilise the financial basis of statutory old-age pensions insurance. The contribution rate can be stabilised at 19.5 % in the medium term by means of the reform measures, as well as by the supplementary measure in preparation to synchronise pension payments and contribution timetables.

Increasing the age limits for unemployed persons and part-time working in old age from 2006 to 2008 in monthly steps from 60 to 63 years will lead to temporary relief of up to 0.1 contribution rate points as to the contribution rate.



The measures provided in the Old-age Pensions Insurance Sustainability Act and other legal amendments can serve to stabilise the contribution rate in the medium term, and the fluctuation reserve can be increased to become a sustainability reserve. A contribution rate has been calculated for 2020 that is 1.6 points lower than in accordance with the law as it stands (contribution rate without measures 21.6 % / contribution rate with measures 20.0 %) while a contribution rate has been calculated for 2030 that is 2.3 contribution rate points lower than would be the case in accordance with the law as it stands (contribution rate not including measures 24.3 % / contribution rate with measures 22.0 %) - cf. also Fig. 2 in the summary. The contribution rate targets envisioned by law (not more than 20 % in 2020 and not more than 22 % in 2030) are hence complied with.

Committing the Federal Government to long-term contribution rate goals and transparent monitoring of the forecast developments in contribution rates (cf. also Objective 11) sends out reliable signals to the economy, and hence has a positive impact on the employment situation.

### **Promotion of active participation in the labour market**

To achieve a high level of employment, statutory old-age pensions insurance in Germany contributes to participation by the benefits it grants. Above all, these benefits promote employees' wage-earning activity in the second half of their working lives. With the benefits for medical rehabilitation and for participation in working life, it is possible in many cases to reduce or remedy limitations of the insured parties' earning capacity, and hence to prevent early reduction of earning capacity.

If a benefit is not promising for participation or was unable to successfully restore performance, the payment of a pension because of reduction of earning capacity can be considered. The pension is granted for a limited period (maximum of three years); once this deadline has passed, the continuation of the preconditions for benefit is examined.

Furthermore, the Act to Increase Preventative Healthcare, the adoption of which is planned for 2005, completes a paradigm shift in the healthcare system. Prevention and health promotion, including occupational health promotion, will be expanded to become a separate pillar of healthcare in addition to acute treatment, rehabilitation and care. The goal is to maintain and promote people's health, and hence to improve their quality of life, mobility and performance. This will make it possible to achieve optimum participation in working life (cf. Annex III).

### **Life-long learning**

Education and skill-building of elderly persons and employees who have already been working for a long time is continually gaining in significance. Amongst other things, there is also a need for close cooperation with the companies who have to shape work such that learning is possible both in terms of time and of content. This means for everyone closer orientation to the possibilities available to establishments and to elderly persons' specific learning prerequisites, learning needs and existing skills. Life-long learning is a central prerequisite both for employability in all phases of life, and also for willingness and ability to continue to participate in society to an advanced age.

Through promotion within projects, support was lent to this end to developing and testing specific further training concepts to accommodate the special learning and educational needs of elderly persons. The content of the projects focussed and continues to focus on the following, inter alia:

- support for self-organised learning activities,
- use of new media and information technologies (reducing access barriers),
- trends of the "learning location character" in existing self-help groups for elderly persons,
- transfer of individual vocational and life experiences to community activities,
- transfer of knowledge between the generations within further training facilities,
- support for "Learning in a social environment" (such as preserving elderly persons' skills in the event of unemployment).

It should be considered overall that life-long learning encompasses the career of a person from early childhood up to and including the phase of retirement.

In July 2004, the Federation and the Länder adopted the "Strategy for Life-Long Learning in the Federal Republic of Germany" in the Federation-Länder Commission for Education Planning and Research Promotion. This shows the fields of action which make life-long learning automatic in each educational biography in the educational areas of school, vocational training, higher education and further training.

### **Objective 5**

**Ensure that, alongside labour market and economic policies, all relevant branches of social protection, in particular pension systems, offer effective incentives for the participation of older workers; that workers are not encouraged to take up early retirement and are not penalised for staying in the labour market beyond the standard retirement age; and that pension systems facilitate the option of gradual retirement.**

In the early 1990s, elderly employees' share in gainful employment bottomed at 49.6% for the 55 - 59 age group (1993) and 17.6% for the 60 - 64 age-group (1994). Since then, the shares of both age-groups in gainful employment have risen steadily, and were 60 % in 2003 (55-59-year-olds) and 23.4 % (60-64-year-olds). Despite this positive development, Germany's proportion of 55 - 64-year-olds in wage-earning activity, at 41.2 %, is still far below the Stockholm target (50% by 2010).

Today's elderly generation has much better possibilities for activity than all previous ones. Elderly persons are healthier and more mobile; they have more education and greater experience, they have a broader spectrum of interests and skills, better financial situations and also a more positive attitude towards their own age. The usual division of life into three phases, namely an ever-longer educational and an ever shorter earning and an ever expanding "old phase" is outdated against the background of continually-increasing life expectancy, and must be corrected. This should include the extension of elderly persons' active contribution phase and greater integration of education, work, voluntary commitment and leisure time into careers.

With the support of the social partners and the Länder, the Federal Government has initiated many reforms and measures in recent years for greater employment of the elderly, as well as for increasing the effective average age of leaving working life (cf. National Employment Policy Action Plans). These can be largely sub-divided into three fields of activity:

- stabilising employment by reducing disincentives,
- improving integration opportunities through measures of labour market policy, and
- initiatives to launch a fundamental change of awareness and an experience of good practices.

The cumulative effect of measures in these three fields of activity are expected to considerably improve the employment opportunities and the share in wage-earning activity of elderly employees.

In the final analysis, however, the common objective that elderly persons can contribute more with their potential to the economy and society can only bear fruit if the social players take up the topic as their own cause. These are very largely enterprises and their associations, but also works and staff councils, as well as trade unions. If investments are made there in life-long vocational skill-building and development, the opportunities for elderly employees will improve.

### **Stabilising employment by reducing disincentives**

The Federal Government and the social partners have set themselves the goal of obtaining a larger share in wage-earning activity for elderly employees. The Alliance for Work, Education and Competitiveness introduced a change of paradigm to improve elderly employees' employment prospects (cf. German 2002 Employment Policy Action Plan) in March 2001.

The social partners are also supporting the Federal Government's employment policy for employment promotion and integration of elderly employees in the labour market through many initiatives and measures of their own (cf. German Employment Policy Action Plans 2003 and 2004).

In order to stabilise and increase elderly employees' share in wage-earning activity, the Federal Government has increasingly reduced the remaining disincentives for companies to cease encouraging early retirement.

These include reducing the benefit time for unemployment benefit for elderly employees to a maximum of 18 months (previously up to 32 months) and temporarily tightening up regulations on refunding unemployment benefit by employers if they let long-term employees go. For instance, the age threshold from when an employer can be obliged to refund expenditure on the unemployment benefit of elderly unemployed persons has been reduced from 58 to 57 years. The third structural tool that was frequently used for early retirement, structural short-time working benefit, was further developed to become transfer short-time worker benefit and the duration of promotion restricted to a maximum of twelve months (previously 24 months).

The Old-age Pensions Insurance Sustainability Act also reduced further incentives to take early retirement. For instance, the age limit to draw an old-age pension early because of unemployment or part-time working in old age was increased gradually from 60 to 63 for those born after 1946 and younger insured parties. For insured parties born after 31 December 1951, the possibility of drawing a pension earlier because of unemployment or after part-time working in old age or old-age pension for women has already been completely eliminated. In future, statutory old-age pensions insurance only offers the possibility to draw an old-age pension before the age of 65 for persons with disabilities and insured parties of long standing – with reductions applying when benefits are drawn early.

### **Improving integration opportunities through labour market policy measures**

The Federal Government has created new labour market policy promotion tools specific to the elderly by means of the First Act for Modern Services on the Labour Market. These include the so-called payment protection for elderly employees<sup>10</sup> and releasing the employer from contributions to unemployment insurance. The Third Act for Modern Services on the Labour Market refined the Act concerning Part-Time Working in Old Age, amongst other things<sup>11</sup>.

Employers who appoint an employee who is 55 or older are released from the obligation to pay the unemployment insurance contribution. For the employee themselves, full protection is retained in unemployment insurance. The provision is currently restricted to 1 January 2006, but is to be extended to the end of 2007.

### **Initiatives to introduce a profound change of awareness and exchange best practices**

In addition to the creation of new statutory framework conditions, the Federal Government, not lastly with the National Strategy for Sustained Development, has created a broad spectrum of projects and initiatives to promote a comprehensive change in awareness of elderly persons' social perceptions.

Amongst other things, a working party was set up within the Federal Government which, under the heading of "The potential of elderly persons in the economy and society", is to coordinate the different measures for elderly employees in the fields of the labour market, (further) training and health (focussing on prevention) and over and above this coordinate state and public measures with those of the social partners at federal level.

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<sup>10</sup> The tool of payment protection gives elderly persons looking for work from the age of 50 a financial incentive to accept work paid less well than their previous earnings. Payment protection takes place in the shape of a subsidy of 50 % of the difference in pay between the last and the new flat-rate net earnings. The payment protection subsidy is paid for the duration of the remaining unemployment benefit claim on taking up employment. In addition the old-age pensions insurance contributions are topped up to a certain degree on condition that there is still a remaining right to unemployment benefit for at least 180 days. The regulation is time-limited to 1 January 2006.

<sup>11</sup> The procedural and promotional provisions of the Act concerning Part-time Working in Old Age were simplified and a special insolvency security duty for part-time working in old age was entrenched in the so-called block model. By these means, the acceptance of part-time working in old age as a model of a sliding transition into retirement increases further among both employers and employees. The Act concerning Part-time Working in Old Age can hence make a still greater contribution towards the stabilisation of the share in wage-earning activity of elderly employees.

The "TeamWork for Germany" public relations campaign emphasises amongst other things a positive attitude of enterprises towards elderly employees, and enterprises are made aware of the success factors constituted by good personnel and labour market projects. The ideas of "Professionals of the Nation" are tackled, from the recommendations of the Committee of Experts for "Modern Services on the Labour Market". Roughly 1,000 enterprises are taking part in the network nationwide.

The New Quality of Work Initiative (INQA), a joint project of the business community, the trade unions, the social insurance organisations, foundations and the Federation and the Länder, is campaigning for a "New Quality of Work" as an important and promising task and a challenge, since workers' motivation, health and satisfaction are key factors for enterprises' innovation and competitiveness. In the framework of INQA, retaining and promoting elderly persons' employability is a key focal point. The INQA launched the "30, 40, 50 plus – healthy work into old age" campaign in autumn 2004 jointly with the social partners and enterprises. If the potential of the elderly at work is to be used, their working conditions, the promotion of their health and their life-long skill-building must start early. The guide here is the joint memorandum entitled "Demographic Change and Employment - Call for New Corporate Strategies". It contains a lot of practical pointers as to how to organise the world of work as well as personnel policy in a manner that accommodates age and is demographics-proof. Over and above this, INQA in particular offers advice to small and medium-sized enterprises in coping with demographic change at regional and situational level, and in line with their needs.

### **Employment incentives for elderly employees in statutory old-age pensions insurance**

As a rule, statutory old-age pensions insurance in Germany is designed such that considerable incentives exist to remain in wage-earning activity. The consequence of the major orientation to the principle of wage and contribution equivalence is that on principle each pensionable activity accrues additional old-age pension entitlements. In particular, German pension law has no provisions making the amount of the pension only dependent on income in the "best years" of individual careers and making wage-earning activity and the amount of the income in the other years irrelevant for the amount of the pension; irrelevant, and hence less attractive.

Over and above this, there are additional incentives towards wage-earning activity, specifically on the part of elderly employees. For instance, retirement before the statutory standard age-limit (aged 65; for persons with disabilities: 63) leads to percentage reductions from the amount of pension emerging from the usual pensions formula, while shifting retirement beyond the statutory standard age-limit is rewarded with a percentage pension bonus.

The reductions in old-age pensions applying to early retirement are 0.3 % for each month of retirement before reaching the age of 65; the bonuses with delayed retirement are 0.5 % for each month by which retirement is delayed beyond the statutory retirement age. Pension reductions and pension bonuses remain effective during the whole term of retirement, and also apply to any surviving dependants pension if one is paid after the death of the insured party (cf. on this also Annex X).

If insured parties retire before reaching the statutory standard age-limit, or if they delay retirement beyond the statutory standard age-limit, as a rule both effects described work together: With early retirement, on the one hand the reduced working phase leads to fewer pension entitlements being accrued, which are then reduced once more by the impact of the pension reduction. On retirement after the statutory standard age-limit, by contrast, additional old-age pension entitlements are accrued because of the longer working phase which are increased further by the pension additions.

The cumulated overall effect of these provisions, related to an average earner starting three years of vocational training at the age of 17 who then remains in pensionable employment without interruption is as follows: On retirement at 65, this insured party receives a monthly pension of about Euro 1,235 in accordance with the law as it stands. If however he/she retires at 63 (i.e. 2 years before reaching the statutory standard age-limit) his/her monthly pension is reduced by about 11 % to roughly Euro 1,097. Retirement at 67, by contrast, leads to a monthly pension of Euro 1,441, i.e. to almost 17 % more monthly benefits than on retirement at 65 (cf. Annex VI).

In total, hence, the provisions of German pension law provide incentives especially for wage-earning activity to elderly employees, in particular to avoid early retirement or delay the beginning of retirement beyond the age of 65.

The possibility to take a part-pension provides a further incentive for staying longer in working life. Instead of entering into full retirement as soon as the conditions for early retirement are met, claiming a full pension, the option exists of continuing to work at least part-time while drawing one-third, one-half or two-thirds of the pension. In addition to the part-pension, wage-earning activity is allowed to an agreed extent, i.e. an additional income may be earned up to three different limits. This allows insured persons to postpone receipt of the full pension. In this case, only the part-pension received is subject to reductions.

## **Objective 6**

**Reform pension systems in appropriate ways taking into account the overall objective of maintaining the sustainability of public finances. At the same time sustainability of pension systems needs to be accompanied by sound fiscal policies, including, where necessary, a reduction of debt. Strategies adopted to meet this objective may also include setting up dedicated pension reserve funds.**

A vital cause of the concern about sustainable finance policy is demographic change. Given the question of fairness between the generations and the challenges posed by the demographic trends, the Federal Government attaches considerable importance to this topic.

### **Measures to maintain the long-term sustainability of public finances**

Since 2001, the Federal Government has launched a large number of ground-breaking reforms in the areas of the labour market, health and pensions. The long-term sustainability of public finances has been considerably improved by this. The task of budgetary policy is to ensure that the further consolidation of public finances and debt-reduction do not subject future generations to additional burdens, but on the contrary create new opportunities to invest in the future. The general fundamental conviction has grown in recent years that there is no other way but to decisively continue to consolidate public budgets.

Trends in expenditure have been extremely restrictive in Germany since economic stagnation set in in 2000. Total public spending increased by an annual average of only +1.4 % p.a. in the period 2000-2004; the increase was hence lower than the annual average change in nominal GDP in this period. However, trends in tax revenue, being weaker than anticipated because of the poor economic trends, fully made up for the consolidation contribution on the expenditure side.

The consolidation line, which continues to be restrictive, is currently also reflected in the fall in the public-sector share by 1.2 percentage points in 2004. This is caused by the social policy reforms of Agenda 2010 in particular. Were the revenue ratio to have been constant, the deficit-to-GDP ratio would have fallen year-on-year to -2.6 % of GDP by virtue of the reduction in spending. This shows that the Federal Government consistently pursues the consolidation policy even in difficult situations.

In future, the continuation of the consolidation policy must however also include further considerations to improve the long-term sustainability of public finances as a whole. However, measures to improve the quality of public finances, by for instance investing in education, research and innovation, which lead to an increase in growth potential, are also suitable to counter the problem of demographic change. It should be considered in this "qualitative consolidation" that there is no more scope in public budgets to expand overall spending.



### **Statutory old-age pensions insurance in the public budget**

Payments from the federal budget to statutory old-age pensions insurance totalled approx. Euro 77.4 billion in 2004. This amount includes, in addition to the subsidies to general old-age pensions insurance (totalling Euro 54.4 billion) various payments of the Federation with a specific purpose. These are in particular contributions with which entitlements are anticipated for child-rearing for births from 1992, the deficit subsidy of the Federation to the Miners' Insurance Fund old-age pensions insurance, as well as refunds (e.g. for special pension benefits in the Federal Länder added by the reunification process). These payments amounted to Euro 23.0 billion in 2004. Federal subsidies to general old-age pensions insurance accounted for 27.5 % of pension expenditure in 2004. They accounted for a 24.2 % share in 2004 income (total of approx. Euro 224.7 billion).

Federal subsidies to general old-age pensions insurance on principle play a number of roles, as described by the definition of multifunctional nature of the federal subsidies. They play a special role in relieving burdens and providing compensation, as well as playing a general provision-securing function. The additional federal subsidy also serves the blanket coverage of non-contribution-covered benefits, as well as the goal of reducing additional wage costs – as shown by the reasoning for the statute. The community of statutory old-age pensions insurance operating in a spirit of solidarity was assigned a number of global tasks in the past which accordingly are to be borne by the community.

### **Objective 7**

**Ensure that pension provisions and reforms maintain a fair balance between the active and the retired by not overburdening the former and by maintaining adequate pensions for the latter.**

Achieving an improvement in fairness between the generations has been the primary goal of the pension reforms of recent years. The reforms prevented the rise in the contribution rate, which would otherwise have been made inevitable in the long term by demographic change, thus overburdening future generations.

### **Stabilising the contribution rate**

That this reform policy has been highly successful is made clear if one compares today's estimates on long-term trends in contribution rates with the estimates drafted at the end of the eighties – i.e. prior to commencement of the reform legislation: Whilst an estimate made in 1987 for 2030 forecast a contribution rate of roughly 36 to 42 %, the current estimates for the same year reach a contribution rate of only roughly 22 %. The additional demographic burden on the coming generation of contribution payers will hence be considerably alleviated by the reforms.

Fair distribution between the generations is however not attained solely by the contribution rate, and hence the contribution burden on the future generation, being reduced or its increase slowed. A low contribution rate can also be advantageous to the future generation of earners if what they can be anticipated to receive in return for this contribution payment is not suitable. In this respect, a sensible criterion for measuring fairness between the generations is only the comparison of value for money offered by statutory old-age pensions insurance, in other words the return, as presented for various generations.

### **Return expectations of statutory old-age pensions insurance**

According to current calculations, with a presumed long-term increase in fees of 3 %, the internal return of statutory old-age pensions insurance for insured parties retiring in 2004 was almost 4.5 % for women and almost 4 % for single men<sup>12</sup>. The return will however fall for the new pensioners of the next ten years, and it will be almost 3 % for new pensioners in 2020 for single men and about 3.5 % for women and married men.

The reforms that have been initiated will reduce the level of provision before tax. The ratio of beneficiaries and pensionable employees is accommodated in the pension adjustment by the sustainability factor that has been introduced in the latest reform carried out in 2004.

Furthermore, in future the pensionable wage and salary amount will be taken as a basis in ascertaining wage trends. The clause to safeguard pension levels should however prevent the average level of pensions falling below a certain limit in relation to workers' income.<sup>13</sup>

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<sup>12</sup> The return for married men is roughly the same as that calculated for women because the insured party pension is frequently added to by a surviving dependants pension and thus a larger amount tends to be paid out in return for the contributions paid in.

<sup>13</sup> In a Pay-as-you-go pension provision system, for the amount of the contribution rate, central significance attaches to its general benefit amount, the number of recipients, the number of contributors and the proportion of the funding from taxation. The long-term projections show a trend here to the detriment of funding of old-age pension provision. The sustainability factor tackles these emerging trends and passes them on to reduce the increase in the contribution rate in the longer term via lower pension adjustments by a lower pensions level. It was brought into operation via the change in the pensioners quotients as a defining value. The change in the number of 'equivalised pensioners' (translator's note: total pension volume divided by the standard pension) is measured to change the number of the equivalised contributors (translator's note: total pensionable wages divided by average remuneration). One-quarter of the quotient of the changes enters the adjustment formula. Thus, the sustainability factor reflects not only demographic processes, but also the trends on the labour market. For the first time, the sustainability factor is to be calculated in the 2005 pension adjustment. The impact of both the product of the contribution rate factor, which includes the input of the pensions insurance contribution rates and proportion of old-age provision, and of the

Against the background of the ever more manifest impact of demographic change, the Federal Government is continuing to pursue the goal of guaranteeing the long-term funding of the security-related objectives of the social welfare state, and hence making all systems of social security fit to face the future. For the revitalisation of the economy which is necessary in this context, however, it is initially indispensable to improve the overall economic framework by means of the measures of Agenda 2010 in order to retain the competitiveness of Germany as an industrial location and to promote employment growth.

### **Objective 8**

**Ensure, through appropriate regulatory frameworks and through sound management, that private and public funded pension schemes can provide pensions with the required efficiency, affordability, portability and security.**

#### **A regulatory framework leads to greater efficiency**

Additional old-age pensions need stable and reliable legal framework conditions. The regulatory framework in Germany combines in the additional old-age pensions a sufficient degree of investment security with considerable freedom of investment. Only those products are promoted which actually benefit old-age pension provision. The considerable degree of security of pension provision increases individuals' motivation to take the initiative themselves. In the area of occupational retirement provision, it is important for employers that the administrative effort and the liability and funding risks remain comprehensible.

The Federal Government also designs regulations with an awareness that private pensions are the responsibility of the individual. Only necessary, supportive regulations help those seeking pension provision. For this reason, investment security in Germany is restricted to minimum protection which is not detrimental to increasing expansion. This framework has helped create a welcome diversity of pensions systems, thus forming the basis for well-functioning competition in the additional systems (for details cf. Annex IV).

#### **Provision at a reasonable cost**

With contracts that are typically very long term, even small differences in the costs can have a major impact on the amount of the benefits. The necessary transparency of private pensions systems hence entails that the insured parties should be able to gain an impression of the costs

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sustainability factor is limited. If wage developments are positive, the product may not lead to negative pension adjustments, and may not further increase the negative pension adjustment if wage trends are negative. Because the negative effect of the contribution rate and sustainability factor was greater than the positive effect of wages from 2003 to 2004, there was a zero adjustment in 2005.

they have to bear. With the state-promoted "Riester pension", providers are obliged to inform customers before concluding the contract of the amount of the conclusion costs and of the management costs. Providers must inform customers of all pension contracts annually after conclusion of contract amongst other things about the management costs incurred.

The conclusion costs of life insurance contracts invoiced are limited by the supervisory authority. As a rule, no costs are incurred on conclusion of enterprise-based "Pensionskassen" in occupational retirement provision whilst, taken as an average over many years, the management costs are only 1 to 5 % of the gross contributions. The cost advantage of the group agreements customary in occupational retirement provision has a positive contribution towards their expansion.

### **Assistance in selecting pension products**

There is a diversity of possibilities to take up additional old-age protection in Germany. The right decision in an individual case depends for instance on civil status and income, possibilities of promotion and returns risks. Insured parties can avail themselves of various advisory services that are on offer when looking for the right solution. In addition to providers of additional old-age pensions, the statutory old-age pensions insurers also offer to provide information on the possibilities of an additional old-age pension for which state assistance is provided. Consumer advice centres, as well as trade unions and employers' associations, provide information to employees and employers. The government is implementing a major information campaign regarding the introduction of the new promotion systems, and is providing detailed information via the Internet amongst other means. Over and above this, the Federal Government is promoting programmes to improve general knowledge on matters related to pensions (cf. also the information provided at Objective 11 and in Annex VIII).

### **Liability and insolvency protection**

In the case of occupational old-age provision in Germany, it is always the employer who is liable for the occupational retirement provision agreement they entered into; a contribution agreement pure and simple is not possible. In the event that the employer has not commissioned an external organisation to implement their occupational retirement provision agreement and has become insolvent when the pension payments become due, or indeed prior to this, the mutual "Pensions-Sicherungs-Verein" steps into the obligation of the employer. If external implementation has been commissioned with supervision by a state authority ("Pensionskassen", pensions fund, direct insurance) the insured parties or beneficiaries receive benefits from the assets to cover the contractual obligations (guarantee assets). In addition, for direct insurance there is an obligatory (and with "Pensionskassen" an optional) security fund which must continue the insurance policy in the event of insolvency.

### **Regulations for sustainable capital investment strategies**

The supervisory framework for private providers of pension services is largely provided by European Community law<sup>14</sup>.

### **Achieving a broad impact on a voluntary basis**

The Federal Government presumes that the necessary universal spread of voluntary occupational retirement provision can be implemented above all via collective agreements and company regulations. The right of the individual employee to occupational retirement provision in the framework of remuneration conversion is subject to collective agreement on pension provision. Employers and trade unions can hence agree on a flexible, binding additional old-age pension scheme. Economies of scale create advantages here in the shape of efficiency and the low price for the individual which outweigh the disadvantage of the narrower selection of products available.

The partners to the collective agreements use this possibility: From 2002 to the end of April 2005, they have created the possibility of remuneration conversion for approx. 20 million employees in collective agreements. Many collective agreements provide for a financial contribution by the employer in such instances. Where this takes place, the growth rates are particularly high.

### **3.3. Modernising pension systems in response to changing needs of the economy, society and individuals.**

#### **Objective 9**

**Ensure that pension systems are compatible with the requirements of flexibility and security on the labour market; that, without prejudice to the coherence of Member States' tax systems, labour market mobility within Member States and across borders and non-standard employment forms do not penalise people's pension entitlements and that self-employment is not discouraged by pension systems.**

One of the major challenges of our time is the constant adjustment of the pension systems to the changing worlds of life and work. If the pensions system is to continue to function, it needs flexible, but nevertheless reliable structures meeting the preconditions of a high level of social protection, adapting to the changeable needs of society and not proving disadvantageous to individual plans.

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<sup>14</sup> Directive 2002/83/EC of the European Parliament and of the Council of 5 November 2002 concerning life assurance, Directive 2003/41/EC of the European Parliament and of the Council of 3 June 2003 on the activities and supervision of institutions for occupational retirement provision and the relevant banking directives

### **Security in special situations**

The German pension system provides many regulations for providing security in old age in different situations. The amount of income in old age is however primarily in line with wages earned for work for which corresponding contributions were paid towards statutory old-age pensions insurance. The particularities of atypical employment are nevertheless accommodated.

Thus, for instance, contributions are paid for people with disabilities according to the wages received if they undertake regular employment in approved workshops for persons with disabilities or other facilities, but at least using an assessment basis of 80 % of the reference amount<sup>15</sup>.

For times spent receiving unemployment benefit, contributions are paid on the basis of 80 % of the gross wage on which the benefit is based. For those receiving the new unemployment benefit II, which was introduced as on 1 January 2005, a uniform amount of Euro 78 per month is paid, corresponding to pensionable earnings of Euro 400. By virtue of the new regulation, former beneficiaries of social assistance with earning capacity are also covered who have not previously received benefits from unemployment insurance. Full contributions are paid to old-age pensions insurance for this group of individuals for the first time.

A reduction of working hours (part-time employment) due to care of children or others does not lead to unreasonable losses of pension entitlements because below-average wages in such cases are 'topped up' by 50% for pension calculation purposes - up to 100% of average income. This applies until a child is 10 years old and where nursing care is provided, it may even apply until the child is 18, provided on retirement the pensioner has a total of 25 years with pension allowable periods<sup>16</sup>. If wage-earning activity is impossible due to simultaneous care for two or more children, carers receive maximum credit.

In addition, since 1 April 1995 obligatory insurance in statutory old-age pensions insurance has existed for carers pro-bono caring for a person in need of long-term care for at least 14 hours per week if the carer is not engaged in gainful employment for more than 30 hours a week. Thus, in particular the value of family care of relatives is recognised under pensions law, and the interruption or reduction of wage-earning activity does not leave gaps in building up own pension entitlements. The long-term care insurance fund to which the person cared for belongs pays the old-age pension insurance contribution to statutory old-age pensions insurance for the

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<sup>15</sup> This corresponds in 2005 to monthly earnings of Euro 1,932 (West) and Euro 1,624 (East).

<sup>16</sup> The pension periods also include the times included because of child-care.

carer. In doing so, the amount of the contribution payment is in line with the necessary time and the extent of long-term care needed, which is determined by the long-term care insurance fund.

Over and above this, the right to statutory old-age pensions insurance for certain times in which the insured party was prevented from paying contributions provides for so-called creditable periods. Creditable periods are in particular times during which insured parties were unable to work because of illness, or when they received benefits for rehabilitation, times of pregnancy or maternity during the protected periods provided for in the Maternity Protection Act (Mutterschutzgesetz) and times of attending a vocational school.

### **Flexibility of additional old-age pensions**

The combination of flexibility in professional life and occupational retirement provision is a concern for German pensions policy. The attractiveness of the second pillar largely depends on the possibility to take it with you when you go, in other words on the portability of the capital accumulated when changing employers. Already by the 2001 pension reform, the so-called statutory vesting periods for entitlements for occupational retirement provision were considerably reduced, so that employer-funded entitlements are now vested if the pension agreement has existed for five years (previously ten years) and the employment ends after the age of 30 (previously 35). Entitlements from the new employee-funded remuneration conversion are vested immediately.

Portability has been improved further with effect from 2005. Previously, entitlements could only be taken over by a new employer by continuing the old agreement, which reduced portability. The Old-Age Income Act now introduces a simpler form of transfer. Here, the parties to the employment contract are no longer bound by the arrangement contained in the old agreement, but the entitlement can be converted into a capital amount and incorporated into the new employer's pensions system. This new possibility of capital transfer helps combine occupational entitlements with one employer even with frequent changes of employer.

Within certain limits, employees have also had the right since 2005 to avail themselves of the new capital transfer possibility. For reasons of legal certainty and clarity, this right however only applies to new agreements concluded since 1 January 2005 (on portability cf. Annex V).

Cross-border mobility is guaranteed in Germany by section 1b subsection 1 sentence 6 of the Occupational Retirement Provision Act (Betriebsrentengesetz)<sup>17</sup>, in accordance with which the entitlement of an employee who moves from Germany to another EU Member State is maintained to the same degree as for persons who remain in Germany after terminating employment.

### **Regulations applying to those on a low income**

Social insurance for "marginal" employment (mini-jobs) was reformed back in 1999 and once more extensively revised with effect from 1 April 2003. Particularly in this area, which is characterised by atypical employment, excessive bureaucracy should not be permitted to create incentives for employers to deviate towards other, illegal forms of employment.

By increasing the 'marginal employment' threshold for entering obligatory social insurance from Euro 325 to Euro 400 per month and removing the limit placed on weekly working hours (previously 15 hours) and the possibility, unlike in the past, to be able to exercise "marginal part-time" employment exempt from insurance, in addition to pensionable main employment, this form of employment was designed to meet future needs and to be attractive. Thus, the economy is given a flexible arrangement for marginal part-time employment, whilst at the same time employees' social security is maintained by virtue of inclusion in statutory old-age pensions insurance.

By voluntarily topping up the flat-rate employer contributions<sup>18</sup> the insured party obtains full entitlements in old-age pensions insurance. This option corresponds to people's different motives to take up marginal part-time employment: Anyone who already has adequate insurance and would simply like to earn a little extra towards their livelihood or family income will not be interested in an additional contribution payment. For others, however, topping up to full old-age pension insurance contributions offers an opportunity to top up the expected old-age pension or to meet the insurance law preconditions for receiving a pension at all. The topping up option is hence an opportunity for women in particular to improve their old-age pension provision. For employers, in any case, the obligation exists to inform employees of the topping up option.

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<sup>17</sup> The regulation implements Council Directive 98/49/EC of 29 June 1998 on safeguarding the supplementary pension rights of employed and self-employed persons moving within the Community.

<sup>18</sup> If an employee earning a marginal wage has renounced exemption from old-age pensions insurance, he/she must personally pay the difference between the 12-percent employer share and the full contribution, currently 19.5 %. The employer deducts this share from the wage and passes it together with its share to the Federal Miners' Insurance Fund as the collecting body. If the employee earns less than Euro 155 per month in his/her marginal part-time employment (or in several marginal part-time jobs together), in this instance he/she must personally top up the contribution to 19.5 % of Euro 155. The employer pays its share only of the wage actually paid.



In addition, the transition from exemption from insurance to the full charge burden was made much more attractive with the introduction of a sliding zone for incomes between Euro 400.01 and Euro 800 (midi-jobs). Employees with gross income between Euro 400.01 and Euro 800 may if they so wish pay lower contributions to pension, health, long-term care and unemployment insurance. In the sliding zone of between Euro 400.01 and Euro 800 it is no longer the actual income but a fictitious, lower income which is used to calculate the contribution for the employee share. The contribution burden for the employee is hence reduced. The previous charge threshold of the full social insurance contributions is clearly reduced to slightly more than half, namely at the beginning of the sliding zone, in order to clearly extend employment also in the low-wage area and to make it socially responsible.

### **Objective 10**

**Review pension provisions with a view to ensuring the principle of equal treatment between women and men, taking into account obligations under EU law.**

#### **Equal treatment is a policy goal**

The equal treatment of women and men and the possibility to acquire entitlements for equally adequate income in old age holds particular significance in Germany. Despite the fundamentally gender-neutral<sup>19</sup> wording of the pension law, there are major differences in reality between the pension entitlements of women and men which originate above all from women's shorter average working lives and lower income.

For instance, women and men today are exposed to poverty risks in retirement to different degrees. Whilst the poverty risk rate for women in this group was 13.5 % in 2003, the comparative value for men is only 9.8 %.

Both women and men receive surviving dependants protection through statutory old-age pensions insurance. Women however as a rule receive more surviving dependants pensions. The reason for this is that as a rule they have a lower independent income, and fewer reductions are applied to widows' pensions.<sup>20</sup>

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<sup>19</sup> An exception from the gender-neutral wording of pension law is old-age pensions for women because since the 1957 pension reform, women have been enabled on meeting the preconditions to receive a pension from the age of 60. From 2000 to 2004, the age limit for the deduction-free drawing of this old-age pension was increased from 60 to 65. Hence, from the year of birth 1945 this old-age pension can be only drawn unreduced from the age of 65. Women born from 1952 onwards can no longer draw an old-age pension for women.

<sup>20</sup> The widow's pension was reformed in 2001 and is 55 % of the insured party pension, plus a subsidy for children brought up. This subsidy is currently Euro 52.26 (and Euro 45.94 in the new Federal Länder) for the first child and Euro 26.13 (and Euro 22.97 in the new Federal Länder) for each further child; the amount of the subsidy is adjusted regularly in line with the other surviving dependants pension.

In order to reduce the remaining differences, an increase in women's share in wage-earning activity is being targeted in the framework of the Lisbon Strategy.

In the reforms in old-age pensions insurance, women's independent old-age pension provision is a major factor to counter disadvantages which above all affect women in social reality, in building up adequate income for old age.

The family-specific provisions of German pensions law have been modified and in some instances considerably expanded in recent years (cf. Annex VII). These regulations are to ensure that the bringing up of children does not lead to unreasonable deficiencies in the pensions of parents and guardians in pension law which is on principle orientated to the wage and contribution equivalence of pensions. Two approaches can be distinguished between in these regulations, which in other respects are independent of the gender of the parents and guardians: On the one hand, the independent old-age pension provision of the parents and guardians is improved, whilst on the other the provision for the parents and guardians in the event of the death of the spouse is increased.

#### **Pension splitting in statutory old-age pensions insurance**

Previously, pension splitting was only applied to the provision settlement to be carried out in the transfer on the occasion of a divorce. A major step towards expanding women's independent old-age pension provision is the general possibility of pension splitting created in 2001. Spouses both of whom were born after 1961 or whose marriage was concluded after 2001 can divide up their pension entitlements accrued during the marriage between them, and hence create independent old-age pension provision for both partners, which particularly serves to create independent old-age pension provision for women.

Pension splitting as agreed by spouses replaces the traditional pensions for surviving dependants. As a rule it takes effect during the lifetime of both spouses and favours the spouse who accrued fewer pension entitlements during the marriage. Unlike pensions for surviving dependants, income is not counted against personal pension benefits.

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Pension splitting can however only be carried out if both spouses have worked for at least 25 pensionable years. This avoids unfairly favouring persons whose main old-age provision is outside statutory pension insurance.

### **Unisex tariffs in additional old-age pensions**

In the area of private capital-covered additional old-age pensions, gender-neutral tariffs (unisex tariffs) are a precondition for promotion of pension contracts concluded from 1 January 2006.

The consequence for women of gender-specific tariffs which result from their higher life expectancy - lower monthly pensions in comparison to men from the same contributions – is hence avoided. German law goes further in this respect than the EU Equal Treatment Directive<sup>21</sup> adopted in December 2004, which continues to permit the application of gender-based actuarial factors if there are objective reasons for this. Most forms of classical occupational retirement provision make provision for unisex tariffs on a voluntary basis.

Since the beginning of 2005, there has been a new possibility, particularly for women, to avoid gaps in pension provision caused by interruptions in wage-earning activity as they occur with child rearing by creating a legal right for these cases to the continuation of occupational retirement provision with their own means.

### **Objective 11**

**Make pension systems more transparent and adaptable to changing circumstances, so that citizens can continue to have confidence in them. Develop reliable and easy-to-understand information on the long-term perspectives of pension systems, notably with regard to the likely evolution of benefit levels and contribution rates. Promote the broadest possible consensus regarding pension policies and reforms. Improve the methodological basis for efficient monitoring of pension reforms and policies.**

The government and the political arena are regularly faced by complex decisions relating to the need for reform in the area of social security. By means of broad-based public relations work, the population must be informed of the conflicts to be resolved and the existing challenges, and hence the stage set for acceptance of the potential reform options. The safeguarding of statutory old-age pensions insurance in particular depends on this very acceptance. The stronger personal responsibility of insured parties which is the goal of national pensions policy in pension-related matters can only be realised if the various organisations of old-age pension provision guarantee an optimal level of transparency and information.

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<sup>21</sup> Directive implementing the principle of equal treatment between women and men in the access to and supply of goods and services

### **Availability and spread of statistical information**

The Federal Government has a number of sources of information and observation instruments which offer detailed impressions of trends in (future) old-age income and present an important basis for political decisions in this area.

There are studies based on the results of questionnaires, reports and administrative statistics to be regularly submitted to Parliament.

- The pension information report prescribed by statute provides an annual update of trends in statutory old-age pensions insurance in the past, present and future. The core of the report is the advance calculation of trends in pension funding.
- Once per legislative period, a supplementary report to the pension information report must be submitted to the Federal Parliament (short: old-age pension provision report). In the third report after those of 1997 and 2001, to be submitted to the Federal Cabinet in November 2005, the degree to which the new promotion of the additional old-age pensions introduced in 2001 has been used in the second and third pillars of old-age pension provision will be reported for the first time, together with the spread of the additional old-age pensions achieved thereby. Furthermore, from 2005 onwards there will be a new section of the report ascertaining the total pension level for typical pensioners of individual retirement years (e.g. in 2020 and 2030). Income from supplementary private pensions will also be used, in addition to the statutory pensions, in calculating the total pension level; furthermore, the fiscal burden will be taken into account.
- In the Old-age Pensions Insurance Sustainability Act of 2004, the Federal Government was also obliged to report to the legislative bodies every four years from 2008 onwards regarding adherence to a target level of provision before tax of 46 % beyond 2020, and in the event of it being at risk to submit proposals to attain the goal, while maintaining contribution rate stability. The indicator "level of provision before tax" refers to the statutory pensions, and is hence not to be confused with the abovementioned total pension level.

- The study entitled "Old-age pension provision in Germany" (ASID) studies the circumstances and type, amount, spread and determinants of the income of elderly persons by examining individuals and spouses. The income levels resulting from the various old-age pension provision systems are analysed in detail. The study has so far been carried out four times; a fifth is currently running. The population from the age of 55 is covered by the study, including the institutionalised population, as well as foreigners in the new and old Federal Länder. Information is available for a total of more than 30,000 persons relating to 25 income components differing in type and amount.

Information relating to the pensions of future generations is obtained in the survey entitled "Retirement pension schemes in Germany" (AVID). The study (undertaken for the first time in 1996) documents careers and future incomes in old age for those with pension insurance born from 1936 – 1955 and their spouses until the age of 65<sup>22</sup>. A follow-up study was commissioned in 2002. The goal of the current study, in analogy to the previous one, is to obtain information for those born from 1942 to 1961. The results should be available at the beginning of 2007.

- The Federal Ministry of Health and Social Security has implemented an annual survey on attitudes among the population to fundamental health and social policy, initially from 2005 to 2008. Special questions relating to German old-age pensions insurance are provided for in the questionnaires of 2006 and 2008, and according to the planning to date relate to confidence in the institution, an evaluation of the equivalence principle, knowledge of their functioning, the objective (e.g. poverty avoidance or ensuring standards of living), various options to ensure funding and the estimation of the reforms carried out to date and the need for further reforms (cf. Annex IX).

### **Spread of skills and expert knowledge**

In addition to the transparent preparation of the statistical data on trends and amount of income in old age, the Federal Government would like to offer to those with private pensions ways of acquiring the knowledge early needed for careful provision of individual capital for old-age pensions.

The lack of information on personal security in old age and uncertainties in dealing with pension products, as well as the resulting lack of willingness to conclude such contracts, is to be

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<sup>22</sup>Until 1996, the data on pension entitlements and on biographies were obtained from the insurance accounts. For the ensuing years until the age of 65, the biographies were expanded with the assistance of suitable statistical procedures.

countered by offering courses. Particular attention is to be attached to offers targeting those who as yet have not thought about pensions.

The Federal Government, the old-age pensions insurers, the social partners and the Federation of German Consumer Organisations have launched the "Well-informed about pensions" information campaign in cooperation with the Association of German Adult Education Institutions. This series of courses is open to all to help to find the right path to an additional old-age pension. In particular, the education campaign is to consider the following questions: What will be my financial situation in old age? Should I take out an additional private or occupational old-age pension, or both?

At events to be held at about 500 evening schools, the course participants are enabled to estimate their financial requirements in old age and on the basis of this knowledge to structure their pension provision in line with their individual possibilities. The course also covers the legal basis, pension information, state promotion possibilities and further topics. Experts from German old-age pensions insurance organisations provide information which is provider-neutral and product-independent.

This educational campaign is flanked by active public relations work. Central significance in this context is attached to the uniform Internet presentation now under construction. In addition to providing contents and background information, there will also be password-protected access to an eLearning platform (cf. Annex VIII).

The Federal Government is undertaking further activities over and above this to provide a better orientation as to pensions, in cooperation with the financial service industry.

In general terms, anyone can avail themselves of the information and advice of the old-age pensions insurers, which is prescribed by statute. To this end, old-age pensions insurance has a broad network of regional advice facilities; the Federal Insurance Institute for Salaried Employees alone has a total of more than 370 advice centres all over Germany. More than 3.4 million personal advice sessions took place in these facilities in 2004, roughly 17 % of which were about information on private or occupational retirement provision eligible for bonuses. In the Act Introducing the "Riester Pension", the legislature also entitled insurers to provide information and advice on these topics. The increasing need for information and the interest among the population are expressed amongst other things by the fact that the number of advice sessions carried out at the Federal Insurance Institute for Salaried Employees in 2004 increased by more than 20 % in a year-on-year comparison.

Since 2002, insured parties may also deal with various services online on the Internet. This is contingent on their authenticating themselves with signature cards. The electronic signature stored on this card ensures that only those actually entitled can gain access to their personal data. Insured parties can then inspect their insurance careers or their pension information online. In future, it will also be possible to make an application for pensions or rehabilitation online.

### **Individual information**

However, it should also be possible for the individual to obtain comprehensive information on their individual rights and the amount of pension to be expected with a minimum of effort, and without becoming entangled in bureaucracy.

Since 1 January 2004, the organisations of statutory old-age pensions insurance have been obliged by law to inform all insured parties (from the age of 27) on an annual basis of their individual pension entitlements and the amount of the resulting pensions. A broad questionnaire of insured parties during the pilot phase confirmed the acceptance of this "pension information" by the insured parties, as well as its significance for planning individual additional pension requirements. In addition to providing a snapshot of future old-age pensions according to the current status, the pension information also contains extrapolations taking account of future pension adjustments amounting to 1.5 and 2.5 %. From 1 January 2005, the pension information to be sent out was revised to further increase comprehensibility. The newly-included indication of the loss of purchasing power of the earnings-linked pension amounts recorded has considerable significance and is also given concrete form in an individual example calculation. Hence, statutory old-age pensions insurance assumes a pioneering role among institutions which dispatch the pension information on old-age pension provision. For the first time, insured parties will be enabled to apply individual weighting and to evaluate both the earnings-linked amounts contained in the pension information, and the amounts shown in nominal values in the remaining pension information.

Providers of private old-age pensions and operators of the external implementation channels of occupational retirement provision are obliged in accordance with the Insurance Supervision Act (Versicherungsaufsichtsgesetz) to provide annual information on the status of the insurance account.

Furthermore, in the second and third pillars, transparency is a major element in the creation and maintenance of acceptance and understanding in the population for supplementary pensions. The enterprises offering private pensions are obliged to place the emphasis in their customer information on guaranteed benefits and to indicate clearly those areas where information on future benefits is not guaranteed. A violation of this obligation can lead to actionable

compensation claims<sup>23</sup>.

A high level of adjustability is also guaranteed in the promoted private pension products by the fact that the insurance providers can be changed at any time, taking the accrued capital on to the new provider. The statutory requirements are governed by the Pension Contracts Certification Act (Altersvorsorgeverträge-Zertifizierungsgesetz). As of 1 January 2005, the obligations have been expanded as to the information that must be provided prior to conclusion of contract. Providers must now provide information on possible investments, the structure of the portfolio and the risk potential. In each case, information is also to be provided in future on the accommodation of ethical, social and ecological concerns. Furthermore, standard calculations by the providers should enable consumers to compare products better. These calculations should show the respective credit after a term of ten years before and after deduction of the change costs (cost of changing to another pension contract) based on alternative interest of 2, 4 or 6 % p. a.

After conclusion of contract, the providers must provide information in writing on an annual basis on the use to which the contributions paid have been put, on the capital formed to date, on the proportional conclusion and sales costs withheld, on the cost of the management of the accrued capital and the return achieved.

Employers or the insurer must inform employees who have occupational retirement provision in writing on request of the amount of the vested entitlement to an old-age pension accrued to date on reaching the age limit provided for in the pension agreement, and of the level of the transfer value on transfer of the entitlement. The new employer or the insurer must inform employees on request in writing of the amount of the transfer value of a right to an old-age pension, and whether an invalidity or surviving dependants pension would exist.

### **Modernising the old-age pensions insurers**

A further goal of the Federal Government was the organisational reform of statutory old-age pensions insurance adopted in 2004. By allocating the information and advice centres to the Land insurance agencies, in future to be referred to as "Regional organisations", all insured parties now have one single, accessible local point of contact; the out-of-date distinction between wage-earners' old-age pensions insurance and salaried workers insurance was abolished and replaced by a uniform definition of the "insured person" in the framework of general old-age pensions insurance. In this way, transparency and closeness were strengthened.

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<sup>23</sup> The duties to provide information are in line with the provisions laid down in European Directives 2002/83/EC concerning life assurance and 2003/41/EC on institutions for occupational retirement provision.



From 1 October 2005, all old-age pensions insurers will carry the joint designation "German old-age pensions insurance" in their names. The statutory introduction of benchmarking, and the bundling of major fundamental and cross-sectional tasks in the German Federation of Old-age Pensions Insurance, will make a major contribution to greater economic viability and effectiveness of old-age pensions insurance. From 2010, the Act aims to save 10 % of the annual management costs as against 2004. This is about Euro 350 million.

## **Annex**

### **to the National Strategy Report on Old-Age Pension Provision 2005**

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## **Annex I      Timeline of the most important social policy events of the past 15 years**

1990   German Unity (3 October)

Conversion of existing pensions in the acceding territory from GDR Marks to DM, adjustment to trends in remuneration in ensuing years

Introduction of a social insurance identity card

1991   Adoption of the "Treaty on European Union" in Maastricht with institutional reforms, the introduction of a European currency by 1999 at the latest, and new tasks allocated to the EU

1992   Entry into force of major elements of the 1992 Pensions Reform Act (Rentenreformgesetz - RRG '92):

- reorganisation of periods without contributions
- pensions adjustment in accordance with net wage trends
- extension of the allowance of childcare years to three years for births after 1991
- introduction of a ten-year childcare period
- link of the federal subsidy to trends in the contribution rate
- incremental increase of age limits from 2001 onwards
- introduction of actuarial reductions
- reorganisation of the law on foreigners' pensions
- revaluation of pensions in the new Federal Länder as on 1 January 1992

1994   Entry into force of the European Single Market

Expert report on organisation commissioned by old-age pensions insurance

1994   Establishment of the European Monetary Institute in Frankfurt am Main

Agreement on the European Economic Area (EEA) with SF, N, S, A and IS, and hence expansion of the area of application of the EC's social security regulations

1995   Introduction of statutory long-term care insurance:

- obligatory contributions from 1 January 1995; start of benefits from 1 April 1995
- contribution payments to statutory old-age pensions insurance for carers

1995   Prognos expert report '95 "Outlook of statutory old-age pensions insurance for Germany as a whole in a changed political and economic framework"

1995 Incremental transition of contribution supervision to old-age pensions insurance (3rd Act to Amend the Social Code [3. SGB-ÄndG]) in 1996-98

A, S and SF accede to EU.

Liechtenstein accedes to the EEA.

1996 Act Promoting a Sliding Transition into Retirement (Gesetz zur Förderung eines gleitenden Übergangs in den Ruhestand), Growth and Employment Promotion Act (Wachstums- und Beschäftigungsförderungsgesetz - WFG) and Act to Reduce the Contribution Burden (Beitragsentlastungsgesetz - BeitrEntlG):

- Increase in the age limit for old-age pension because of unemployment brought forward
- Savings in training periods or in evaluating the first years worked
- Savings with pensions in accordance with the Act on Foreigners' Pensions (Fremdrentengesetz - FRG)
- Changes to the due dates of contributions (primarily for employers in the public service)
- Savings in the field of rehabilitation (capping)
- Abolition of the student privilege in obligatory old-age pensions insurance

1996 Pension commission of the Federal Ministry of Labour and Social Affairs (Blüm Commission)

1996 Gradual transition of employer audits to the organisations of old-age pensions insurance by the end of 1998

1997 1999 Pensions Reform Act (RRG '99):

- Demographic factor added to the pension adjustment formula (planned entry into force 1999)
- Reorganisation of the pension for reduced earning capacity (planned entry into force 2000)
- Additional federal subsidy
- Higher evaluation and additive allowance of childcare periods

1997 Expansion of the Maastricht Treaty to include an Employment Chapter and the Stability Pact

United Kingdom accedes to the EU Social Agreement

Reorganisation of employment promotion in Book III of the Social Code (Sozialgesetzbuch - SGB III)

Flexible working hours regulations safeguarded under social insurance law

1998 Prevention of an increase in the contribution rate to statutory old-age pensions insurance to 21 % by increasing value-added tax (from 15 % to 16 % from 1 April 1998)

Prognos expert report '98 "Effects of changed economic and legal underlying conditions on the German statutory pension insurance"

European Central Bank in Frankfurt am Main from 1 July 1998

Reform of the Data Collection and Transmission Ordinance (Datenerfassungs- und -übermittlungsverordnung - DEÜV)

1999 Pensions Correction Act (Rentenkorrekturgesetz):

- Suspension of the demographic factor
- Suspension of the reorganisation of pension for reduced earning capacity for 2000
- Payment of Federation contributions for childcare periods from June 1999
- Refunding expenditure for unification-related benefits without offsetting against the additional federal subsidy; reduction in the regular federal subsidy
- Easier inclusion of 'paper' self-employed persons in social insurance; inclusion in old-age pensions insurance of self-employed persons similar in status to employees
- Withdrawal of the offsetting of statutory continuation of payment in the event of illness or of rehabilitation benefits, as well as withdrawal of the offsetting of holiday in the case of in-patient rehabilitation
- Reduced contribution rate to old-age pensions insurance from 1 April 1999 onwards

1999 Act Reforming Marginal Employment (Gesetz zur Neuregelung der geringfügigen Beschäftigungsverhältnisse):

- Flat-rate employer contribution payment for marginally-paid employment exempt from insurance
- Possibility of the insured party to waive exemption from old-age pensions insurance
- Marginality threshold in social insurance set at DM 630 per month

1999 Budget Consolidation Act (Haushaltssanierungsgesetz):

- Orientation of pension adjustment in 2000 and 2001 to the inflation rate
- Participation of old-age pensions insurance in eco-tax revenue by increasing the additional federal subsidy (increase amount) whilst reducing the previous payment amount of the additional federal bonus for 2000 to 2003 to consolidate the budget
- Lower assessment of contributions for unemployment by assistance beneficiaries and those on military service or in civil defence
- Contribution rate set at 19.3 % from 1 January 2000

- 1999 Act to Promote Self-Employment (Gesetz zur Förderung der Selbständigkeit):
- Clearer line drawn between dependent employment and self-employment, as well as modification of the pre-conditions for obligatory old-age pensions insurance of self-employed persons with only one client retroactively to 1 January 1999
- 1999 Start of European Monetary Union with eleven participant countries (B, D, SF, F, I, IRL, L, NL, A, P, E)
- 2000 Act to Reform Pensions for Reduced earning capacity (Gesetz zur Reform der Renten wegen verminderter Erwerbsfähigkeit):
- Abolition of pensions for occupational disability, but transitional retention of occupational protection for those born in 1960 and before
  - Replacement of the pension for occupational disability and reduced earning capacity by two-tier pension for reduced earning capacity
  - Retention of pensions for closed labour market, on principle granted as a temporary annuity
  - Increase in the age limit for old-age pensions for severely disabled persons
  - Introduction of reductions and extension of the added pension allowable period for reduced earning capacity pensions on retirement after 31 December 2000 (incrementally)
- 2000 4th Euro Introduction Act (Euro–Einführungsgesetz):
- Conversion of all DM amounts to Euro
  - Conversion of all existing pensions from DM to Euro (as on 1 January 2002)
  - Modification of the offsetting of income with pensions ex mortis
  - Modification of the creditable periods because of schooling in addition to employment
  - Modification of the accommodation of credits from flexible working hours agreement with pensions calculation
  - Arrangement on the use of credits from flexible working hours agreements for occupational old-age provision
  - Modification of the treatment of interruptions with flexible working hours agreements (e.g. block model with part-time working in old age)
- 2000 EU Nice Summit
- Supplement to the EU Treaty and increased cooperation in social policy
- 2001 Act Supplementing the Old-Age Assets Act (Altersvermögensergänzungsgesetz - AVmEG):

- Reduction of the level of pensions by modified pensions adjustment (from 1 July 2001), at the same time relinquishing the inflation adjustment for 2001 from the Budget Reform Act. Relevance now attaches to trends in gross wages, to trends in the contribution rate and to the proportion of old-age provision. Changes in the fiscal burden on wages are no longer taken into account.
- Upgrading of childcare (higher evaluation of low wages and interruption of earnings when caring for several children)
- Modification of the offsetting of income with pensions ex mortis
- New widow's/widower's pension with child component
- Limitation of the right to the minor widow's/widower's pension to two years, as well as right to widow's/widower's pension as a rule only after one year of marriage
- Gaps in employment at the beginning of working life closed under pension law
- Introduction of pension splitting between spouses

2001 Old-Age Assets Act (Altersvermögensgesetz - AVmG):

- Creation of promoted capital-covered (voluntary) additional old-age pension provision ("Riester pension")
- Introduction of tax-free employer contributions to "Pensionskassen" and pension funds
- Legal right to remuneration conversion and further amendments to the law on occupational pensions
- Arrangements for the approval of financial service products for state promotion (Pension Contracts Certification Act [Altersvorsorgeverträge-Zertifizierungsgesetz – AltZertG])
- Improved information service by the statutory old-age pensions insurance (pensions information from 1 January 2004)
- Safeguarding subsistence in old age and with reduction of earning capacity via basic insurance as needed without recourse to children (from 1 January 2003)

2001 Ninth Book of the Social Code (SGB IX):

- Entry into force as on 1 July 2001
- Greater transparency of the rehabilitation system by combining the legal provisions of several social benefits areas (old-age pensions insurance, health insurance, accident insurance, unemployment insurance, war victims' compensation and war victims' assistance, social assistance and youth assistance organisations)
- Joint service units
- New procedure to clarify competences

- Extended wishes and options for those undergoing rehabilitation
  - Benefits abroad
  - New: Incremental reintegration, work assistance, bridging benefit and sign language
- 2001 Act to Improve the Law relating to Surviving Dependants (Gesetz zur Verbesserung des Hinterbliebenenrechts):
- increase in the child component with the new widow's/widower's pension
  - Expansion of the competence of the Federal Miners' Insurance Fund (previously 60 months' membership of the Insurance Fund, new: One month's membership of the Insurance Fund is sufficient.)
- 2001 Act to Reform the Labour Market Policy Tools - Job-AQTIV Act (Gesetz zur Reform der arbeitsmarktpolitischen Instrumente - Job-AQTIV-Gesetz):
- obligatory unemployment insurance for beneficiaries of pensions for reduced earning capacity and during childcare periods from 1 January 2003
- 2001 Act to Determine the Fluctuation Reserve in Old-age Pensions Insurance for Wage-earners and Salaried Employees (Gesetz zur Bestimmung der Schwankungsreserve in der Rentenversicherung der Arbeiter und der Angestellten):
- Reduction of the lower limit of the fluctuation reserve from 100 % to 80 % of one month's expenditure from 1 January 2002
- 2001 Stockholm European Council  
Adoption of Employment Guidelines for elderly employees
- 2001 Laeken European Council  
Adoption of the structural indicators in the area of social integration
- 2002 Act to Safeguard the Contribution Rate (Beitragssatzsicherungsgesetz - BSSichG):
- increase of the contribution rate to 19.5 %
  - increase of the contribution assessment limits to twice the average earnings
  - re-determination of the range of the fluctuation reserve to 0.5 (minimum fluctuation reserve) to 0.7 (maximum fluctuation reserve) month's expenditure
- 2002 First and Second Acts for Modern Services on the Labour Market (Gesetze für moderne Dienstleistungen am Arbeitsmarkt):
- reform of marginal employment from 1 April 2003; minijobs up to Euro 400 are exempt from social charges for employees with no time limit, also in addition to main employment that is subject to obligatory insurance
  - Creation of a sliding zone for low-paid jobs with earnings from Euro 400 to Euro 800 with reduced employee social insurance contributions



- Introduction of obligatory insurance on drawing a start-up bonus
- 2002 Judgment of the Federal Constitutional Court on the taxation of pensions  
Obligation incumbent on the legislature to enact reforms by January 2005
- 2002 Start of the dispatch of pensions information to insured parties
- 2002 Barcelona European Council  
Adoption of the objective to increase the working market exit age by five years by 2010
- 2002 National Strategy Report on Old-Age Pension Provision
- 2003 Brussels European Council  
Adoption of the Joint Commission/Council report on adequate and sustainable pensions  
Further application of the open method of coordination in the area of old-age pension provision, initially until 2006
- 2003 Committees of experts submit their final reports  
Commission for Sustainable Funding of the Social Security Systems  
Committee of experts to reform the fiscal treatment of old-age pension provision expenditure and old-age remuneration  
Social partners, old-age pensions insurance and a working party of the competent State Secretaries of the Federation and the Länder determine the goals and core elements of a reform of the organisational structures of old-age pensions insurance
- 2003 Second and Third Act Reforming Book VI of the Social Code:
- measures to avoid an increase in the contribution rate anticipated for 2004
  - suspension of the pensions adjustment in 2004
  - pensioners to pay the full contributions to long-term care insurance from 1 April 2004, abolition of the contribution bonus to long-term care insurance
  - changes in contribution rates in statutory health insurance to be quickly transferred to pensioners
  - pension payment date moved to the end of the month for new pensions from 1 April 2004, and overall payment day moved by one day
  - restriction of the exemption of Board members of PLCs from exemption from insurance from 1 January 2004 onwards
  - reduction of the minimum fluctuation reserve from 50 % to 20 % of a month's expenditure from 2004

- 2003 Act on Reforms on the Labour Market (Gesetz zu Reformen am Arbeitsmarkt):
- shortening the duration of the right to unemployment benefit to twelve months with exceptional arrangement for the elderly (over 55s)
- 2003 Third and Fourth Acts for Modern Services on the Labour Market:
- Re-organisation of the Federal Employment Service to become the "Federal Employment Agency" from 1 January 2004
  - Introduction of basic insurance for those seeking work from 1 January 2005  
Combination of unemployment assistance and social assistance for those in need and those with earning capacity to become so-called unemployment benefit II with obligatory contributions to old-age pensions insurance based on Euro 400 per month
  - Amendment of the part-time work in old age arrangement as on 1 July 2004
- 2004 Fourth Act Reforming Book VI of the Social Code:
- Land insurance facilities can be merged between Länder.
- 2004 Old-age Pensions Insurance Sustainability Act - Act to Safeguard Sustainable Funding in Statutory Old-age Pensions Insurance (RV-Nachhaltigkeitsgesetz [Gesetz zur Sicherung der nachhaltigen Finanzierungsgrundlagen der gesetzlichen Rentenversicherung]):
- Modification of the pension adjustment formula as from the 1 July 2005 adjustment, including the introduction of a sustainability factor slowing the pensions adjustment
  - Increase of the age limit for the earliest possible drawing of old-age pension because of unemployment or after part-time work in old age to 63 between 2006 and 2008
  - Exclusion of a change to other types of old-age pension from 1 August 2004
  - Reform of the evaluation of periods of school and professional training
  - Orientation of the fluctuation reserve to a "sustainability reserve" with 1.5 months' expenditure as an upper target value
  - Target values for the contribution rate and pensions level: Upper limit of the contribution rate of 20 % until 2020 and of 22 % until 2030 and lower limit of the pre-tax pensions level at 46 % until 2020 and at 43 % until 2030
  - Obligation incumbent on the Federal Government to report on the need to increase the age limit to slow the increase in the contribution rate and adherence to the minimum security goals, as well as on measures to retain a target level of provision of 46 %.

2004 Old-age Income Act:

- Incremental conversion of contributions and pensions of statutory old-age pensions insurance, the professional pension schemes, the agricultural old-age funds and certain types of private annuity insurance to downstream taxation in a transitional phase from 2005 to 2040
- Introduction of a procedure to notify the drawing of a pension to ensure that pensions are taxed
- Conversion of direct insurance to downstream taxation
- Weakening of the tax privilege of capital life insurance
- Simplifications in promoted capital-covered additional old-age pension provision

2004 Act to Promote Training and Employment of Persons with Disabilities (Gesetz zur Förderung der Ausbildung und Beschäftigung schwerbehinderter Menschen)

- Detailed arrangement on the procedure to clarify competences in accordance with section 14 of Book IX of the Social Code, from 1 May 2004
- Clarification that transitional benefit continues to be paid with incremental reintegration following benefits for medical rehabilitation, from 1 May 2004

2004 Act Reforming the Organisation of Old-age Pensions Insurance (Gesetz zur Organisationsreform der Rentenversicherung - RVOrgG):

- Old-age pensions insurance in Germany is to be reorganised and designated "German old-age pensions insurance" ("DRV") plus the name of the respective regional organisation (e.g. Baden-Württemberg) or of the two federal organisations: "Federation", which is to be created by merging the Federal Insurance Institute for Salaried Employees (BfA) and the Federation of German Pension Insurance Institutes (VDR), and the "Knappschaft-Bahn-See", the central collection agency for miners, railway and maritime workers.
- Uniform definition of "insured party" replaces the traditional distinction between wage-earners and salaried employees.
- The sub-division of insured parties takes place by issuing an insurance number in accordance with a quota determined by statute: 55 % of insured parties are cared for by the regional organisations, 40 % by the DRV Federation and 5 % by the DRV Knappschaft-Bahn-See.
- The DRV Federation also carries out fundamental and cross-sectional tasks for the entire old-age pensions insurance system, in addition to the tasks of a pensions organisation.

## Annex II At-risk-of-poverty rates in Germany (modified OECD scale)

Group-specific at-risk-of-poverty rates<sup>1)</sup> (modified OECD scale)  
and further key numbers

Population group/Indicator		1998	2003
Group-specific at-risk-of-poverty rates <sup>1)</sup> (in %)			
Broken down by gender			
Men		10.7	12.6
Women		13.3	14.4
Broken down by age			
0 to 64		11.9	13.8
of whom:	Men	10.9	13.2
	Women	12.8	14.4
65 and older		13.3	11.4
of whom:	Men	9.8	8.2
	Women	15.8	13.7
Pensioners		12.2	11.8
of whom:	Men	9.7	9.8
	Women	14.2	13.5
Further key numbers			
Median old-age income of 65 to 74-year-olds <sup>2) 2)</sup>		886 €	983 €
Median old-age income of 75-year-olds and older <sup>2) 3)</sup>		784 €	829 €
Median income of employees aged from 50 to 59 <sup>2) 4)</sup>			
	only full-timers	2,467 €	2,691 €
	full-timers and part-timers	2,172 €	2,298 €
Ratio of the median old-age income of 65 to 74-year-olds and older to the median income of employees aged from 50 to 59			
	only full-timers	35.9%	36.5%
	full-timers and part-timers	40.8%	42.8%
Ratio of the median old-age income of 75-year-olds and older to the median income of employees aged from 50 to 59			
	only full-timers	31.8%	30.8%
	full-timers and part-timers	36.1%	36.1%
Net equivalised median incomes of 65-year-olds and older		1,330 €	1,510 €
Net equivalised median incomes of 0 to 64-year-olds		1,385 €	1,570 €
Ratio Q5/Q1 for 65-year-olds and older <sup>5)</sup>		3.6%	3.5%
Ratio Q5/Q1 for 0 to 64-year-olds <sup>5)</sup>		3.6%	3.7%

<sup>1)</sup> At-risk-of-poverty threshold 60% of the median equivalised disposable income

<sup>2)</sup> Individual median monthly income within the group, gross (no equivalisation!).

<sup>3)</sup> Only personal income from old-age pension provision (statutory old-age pensions insurance, civil servants' pensions, supplementary old-age and dependants' benefits in the public service and occupational pensions) of persons who were pensioners during most of the survey period. Bonuses from the old-age pensions insurers to voluntary and private health insurance, as well as to long-term care insurance with voluntary or private health insurance, were not taken into account.

<sup>4)</sup> Gainful income (gross) of persons who were wage-earners, salaried employees or public servants during most of the survey period. Not incl. employer shares of the social insurance contributions; not incl. income from ancillary activities, part-time work incl. marginal employment

<sup>5)</sup> Corresponds to Laeken Indicator No. 2 (S80 / S20): Ratio between the income share received by the top and bottom income quintiles.

Source: Becker/Hauser, Verteilung der Einkommen 1999 - 2003, Expert report for the 2nd Wealth and Poverty Report of the Federal Government, as well as supplementary special evaluations by Dr. Irene Becker in April 2005.

### **Annex III Act to Boost Preventive Healthcare (Gesetz zur Stärkung der gesundheitlichen Prävention - Präventionsgesetz)**

In cooperation with the Länder and the municipalities, as well as in the framework of a foundation operating at federal level, statutory health insurance, statutory old-age pensions insurance, including farmers' old-age pension provision, statutory accident insurance and social long-term care insurance will be funding, adopting and implementing joint measures of primary prevention in future in the area of social insurance by virtue of the Act to Boost Preventive Healthcare.

There will be three levels of activity in primary prevention, each with their own tasks, based on uniform definitions and descriptions of benefits:

- at federal level, comprising a joint foundation combining health, old-age pensions, accident and long-term care insurance, in which overarching tasks will be carried out;
- at Land level, at which health, pensions, accident and long-term care insurance will be implemented together with the Länder, involving concrete projects and measures directly targeting citizens;
- the level of the social insurers, at which health, pensions, accident and long-term care insurance carry out the prevention tasks ascribed to them on their own responsibility.

Whilst the individual social insurers very largely have the necessary structures at their disposal, new structures are being created at Land and federal level to facilitate expedient cooperation. To this end, a foundation is to be established at federal level under public law the members of which will be the social insurers, whilst at Land level cooperation is to be regulated via framework agreements between the Länder and statutory health insurance, statutory old-age pensions insurance, including farmers' old-age pension provision, statutory accident insurance, and social long-term care insurance.

This arrangement holds on to the existing division of tasks between the State and social insurance. It will continue to be the case that the Federation, Länder and social benefit organisations must themselves meet their respective responsibilities for citizens' health and fund their tasks from separate sources of finance. The further development of social insurance tasks will be exclusively orientated towards the original mandates of the community of insured parties. There will be no shifting of state tasks to social insurance.

It has for many years been the task of social insurance where possible to work to avoid insurance risks and not to restrict their activities to providing subsequent compensation once risks have arisen; accident prevention is just as much a part of the classical mandate of

statutory accident insurance as, for instance, the principle of putting rehabilitation before granting a pension is a part of the concept of statutory old-age pensions insurance and statutory accident insurance. This is the orientation followed by the Act. It lends greater detail to mandates for preventive healthcare in the area of social insurance and obliges the social benefit organisations to improve cooperation with the state territorial administrative authorities on this basis.

## **Annex IV Description of the second and third pillars of old-age pension provision in Germany**

### **1. The second pillar - occupational retirement provision**

#### **Occupational retirement provision: implementation**

Occupational retirement provision is a voluntary system. Since the 2001 pensions reform, employees have had a fundamental right to remuneration conversion (employee-funded occupational retirement provision). It is nevertheless for employers to decide by what means occupational retirement provision is to be implemented. There are collective agreements in many areas providing for obligatory occupational retirement provision or financial incentives for employees for income conversion. Institutions for occupational retirement provision in the private sector are basically fully funded.

In Germany the "Act to Improve Occupational Retirement Provision" (Gesetz zur Verbesserung der betrieblichen Altersversorgung - BetrAVG) provides for five implementation types (book reserves, "Unterstützungskasse", direct insurance, "Pensionskasse" or pension fund), within which employers can organise occupational retirement provision.

Of these five implementation types, direct insurance, "Pensionskassen" and pension funds are under the supervision of the Federal Financial Services Supervisory Institute (BaFin). Pension funds were approved for the first time in 2002.

On principle, employers select the implementation type. However, restrictions in the selection of the implementation type and the selection of the institution for occupational retirement provision may also be imposed by collective agreement arrangements if these apply to employers and employees alike.

#### **Book reserves**

In the case of book reserves, the employer undertakes to provide employees with occupational retirement provision benefits directly without using a pension facility to secure the promise. Employers may form pension reserves to fund their promise, thus reducing profit. This must be shown in the balance sheet.

### **"Unterstützungskasse"**

A "Unterstützungskasse" is a legally-independent institution which grants occupational retirement provision without providing a legal right to its benefits. The obligation to pay benefits to employees remains with the employers, who must avail themselves of the "Unterstützungskasse" to meet their pension obligations. Employees themselves do not receive a statutory benefit claim against the "Unterstützungskasse". The "Unterstützungskasse" is not subject to insurance supervision. It may dispose freely of the collected capital, and may for instance loan it to the employer.

### **Direct insurance**

If the employer as the insured party concludes life insurance for the lives of its employees, and if the employees or their surviving dependants are entitled to draw on it, this is referred to as direct insurance. It should be taken into account that employers may not withdraw the right to draw benefits once the requirements for vestedness are met.

### **"Pensionskasse"**

"Pensionskassen" are pension facilities with legal capacity which implement occupational retirement provision and grant to employees or their surviving dependants a legal right to this provision. They are supported by one or several enterprises, and are subject to insurance supervision.

### **Pension fund (Pensionsfonds)**

Pension funds are pension facilities with legal capacity which implement occupational retirement provision and grant to employees or their surviving dependants a legal right to this provision. They are supported by one or several enterprises, and are subject to insurance supervision.

Pension funds were introduced in 2002, and are intended to combine the advantages of the security offered by a "Pensionskasse" with the yield hoped for of an investment fund. They differ from "Pensionskassen" above all through their more liberal investment conditions and the concomitant obligation to have insurance cover against insolvency.



Implementation paths for occupational retirement provision

	Book reserves	"Unterstützungskasse"	Direct insurance	"Pensionskasse"	Pension fund
Individual claim against the pension facility	no pension facility	No	Yes	Yes	Yes
Legal right to continuation with individual contributions on termination of employment	No	No	Possible	Possible	Possible
"Riester promotion"	No	No	Possible	Possible	Possible
Guaranteed minimum interest rate	No	No	Yes	Yes	No
Collection of assets	Internal	External	External	External	External
Investment restrictions	None	None	Yes	Yes	Virtually none
Balance sheet-neutral	No	Yes	Yes	Yes	Yes
Insolvency insurance by the Pension Security Association	Yes	Yes	Subject to conditions**	No	Yes
Supervision	No	No	Yes*	Yes*	Yes*

\* Supervision of domestic facilities as a rule by the Federal Financial Services Supervisory Institute (BaFin).

\*\*Protection against insolvency exists if the employer has pledged, assigned or borrowed on the direct insurance, or the employee was only granted a revocable drawing right.

**Occupational retirement provision: Promotion for new promises from 1 January 2005**

As with pensions of the first pillar, the Old-Age Income Act (Alterseinkünftegesetz) also introduces downstream taxation for pensions from capital-covered occupational retirement provision in the long term for the entire course of the policy. This thus standardises and simplifies the fiscal framework of occupational retirement provision. To achieve standardisation, contributions to direct insurance are also exempt from tax in accordance with section 3 No. 63 of the Income Tax Act (EStG), as already applies to payments to a "Pensionskasse" or a pension fund. At the same time, the flat-rate taxation of contributions to build up capital-covered retirement provision is abolished with direct insurance or "Pensionskasse". In the case of new pension agreements, the tax-free maximum amount (previously 4 % of the contribution assessment limit in general retirement pensions insurance) increased by a fixed amount of Euro 1,800 per calendar year so that approx. Euro 4,300 could be spent tax-free on occupational retirement provision in 2005.

That the contributions to direct insurance are now also made exempt from income tax benefits employees in small and medium-sized enterprises in particular for whom there are no collective occupational pensions. A representative survey from 2003 revealed that, to date, offers for occupational retirement provision are especially lacking in small enterprises with fewer than ten employees. The amended legal provisions will enable occupational retirement provision to spread more easily among small enterprises.

Tax-free allowances to "Pensionskassen", pension funds or direct insurance in accordance with section 3 No. 63 sentences 1 and 2 of the Income Tax Act will remain exempt from social charges in statutory retirement pensions insurance in the calendar year up to a total of 4 % of the contribution assessment limit; included amounts from remuneration conversion are exempt from contributions until 31 December 2008. Rights to occupational retirement provision can be transferred more easily on changing jobs from 2005 (details in Annex V).

### **Occupational retirement provision: Dissemination and significance**

The possibility for remuneration conversion has been created in collective agreements for roughly 20 million employees (April 2005). This corresponds to roughly 80 % of employees in the economic activities for which any collective agreements have been concluded in Germany.

- About 15.3 million employees had occupational retirement provision at the end of March 2003 (roughly 10.3 million in private industry; about 5 million in the public facilities providing supplementary old-age and dependants' benefits). This corresponds to roughly 57 % of all employees subject to compulsory social insurance.
- Although the absolute number of employees subject to compulsory social insurance in private industry has fallen by about 870,000 persons, the number of employees with occupational retirement provision increased by roughly 0.9 million in the 15 months from January 2002 to March 2003 (from roughly 14.4 million to about 15.3 million).
- The increase is particularly pronounced in the new federal Länder and among women, the figure rising from 19 to 27 % among employees in the new federal Länder, and from 20 to 29 % among female employees.
- Roughly 300,000 companies (about 15 % of companies) introduced a new supplementary retirement and dependants' benefit or expanded an existing one between January 2002 and March 2003. In addition to improving employee motivation, the introduction of the right to remuneration conversion, as well as the new fiscal promotion, were named as the most important reasons for this.
- At the end of March 2003, the new exemption of remuneration conversion from tax and (continuing until 2008) from social insurance was used by roughly 1.1 million employees (in accordance with section 3 No. 63 of the Income Tax Act up to 4 % of the contribution

assessment limit in statutory retirement pensions insurance). The average amount converted was roughly 900 Euro per year.

- Whilst only one company in four with fewer than five employees offers occupational retirement provision, the number increases to 72 % in companies with 20 to 50 employees, and reaches 94 % with companies employing 200 to 500 employees. Occupational retirement provision is available in almost all companies with more than 1,000 employees.
- One of the most dynamic trends can be observed in industries in which collective agreements have been reached which are either obligatory or highly favourable from the employees' point of view. For instance, an increase from 10 to 21 % can be observed in the hotel and restaurant industry, and from 30 to 47 % with foodstuffs and beverages and tobacco.

### **Occupational retirement provision: funding**

There is a trend when it comes to funding away from the exclusively employer-funded forms (from 54 to 47 %) towards mixed employer and employee-funded implementation forms (from 27 to 36 %).

With so-called remuneration conversion, the employee forfeits part of the remuneration already agreed for work to be done in the future which is used by the employer to acquire an equivalent entitlement to occupational retirement provision. Employees may demand from their employer that the latter converts at least 1/160 of the monthly reference value per year, in accordance with section 18 subsection 1 of the Fourth Book of the Social Code (SGB IV), to their occupational retirement provision – accounting for Euro 181.13 in 2005. The maximum amount is 4 % of the contribution assessment limit in statutory old-age pensions insurance (2005: Euro 2,496).

### **Occupational retirement provision: scope and profitability**

Information on the amount of capital for occupational retirement provision is only available for the implementation path of "Pensionskassen" and pension funds. For "Pensionskassen", the capital investment is Euro 75.4 billion as on 31.12.2003, whilst for pension funds it is Euro 266 million. Pension funds were only approved in the course of the 2002 business year. 23 pension funds were subject to federal supervision at the end of 2003.

With "Pensionskassen", the net interest for 2003 (all yields from capital investments minus all expenses for capital investments related to the average stock of investments) was 4.8 %.

## **2. The third pillar - private old-age pension provision**

### **2.1 Additional capital-covered old-age pension provision: implementation**

Since the 2001 pensions reform, there has been a new form of state-promoted additional private capital-covered old-age pension provision in Germany which has been promoted in four incremental steps since 2002. Promotion consists of two components. All beneficiaries can receive a bonus independent of progression, plus an additional deduction of special expenses can be claimed as a tax advantage.

#### **Private old-age pension provision: Changes by virtue of the Old-Age Income Act**

- The permanent allowance procedure, which will be paperless in future, is becoming much less bureaucratic and hence more citizen-friendly. Beneficiaries will no longer have to file a new bonus application every year. They can also still empower their providers to file the bonus application for them electronically for the contribution year 2003. A corresponding entitlement can already be issued to the provider when the contract is concluded and applies until revoked.
- The number of criteria which private old-age pension provision must meet to be able to receive state promotion was reduced from eleven to five. Amongst others, a one-off payment of 30 % of the capital will be permitted by law. This gives the Riester products flexibility and makes them attractive.
- Consumer protection is being improved. In the context of the information which must be provided prior to conclusion of the contract, providers will have to provide information on the investment possibilities, the structure of the portfolios and the risk potential. Furthermore, an obligatory standard calculation from the provider enables consumers to compare products more easily.
- From 2006 onwards, gender-neutral tariffs, so-called "unisex tariffs", are obligatory for old-age pension provision contracts. Women and men receive the same monthly benefits for the same contributions.

#### **Private old-age pension provision: Promotion in detail**

The structure of private old-age pension provision or occupational old-age provision is accompanied by tax support, which particularly aids those on low incomes and families with children. The statutory provisions on this – like the arrangement for child benefit – are anchored in the Income Tax Act (Einkommensteuergesetz) as a combined allowances-/special expenses provision.

### **Addressees of promotion**

The beneficiaries include amongst others all persons who pay obligatory contributions to statutory old-age pensions insurance and remuneration recipients.

Self-employed persons, who build up their own private old-age pension provision, are the largest group not included among the beneficiaries, as well as those with voluntary insurance and the vast majority of employees in marginal employment. Those with obligatory insurance in professional pension schemes are also not beneficiaries, as they are released from obligatory statutory old-age pensions insurance.

If only one spouse is among the group of individuals eligible for support, in contradistinction to the above, the spouse not eligible for support may also receive the allowances if he/she concludes their own contract.

### **Principles of promotion**

The Federal Financial Services Supervisory Institute (BaFin) examines whether old-age pension provision products offered meet the prescribed promotion criteria. This certificate is not a state seal of approval which confirms the quality of the product as to profitability and security.

- In accordance with this Act, on principle only investments are promoted which are tied up until the beneficiary has reached the age of 60 and which may not be borrowed on or otherwise used.
- The forms of investment must ensure from commencement of payment a constant or increasing life-long monthly annuity; alternatively, appropriate payments are possible from fund or bank credits which are tied to old-age pensions insurance in the payment stage from the age of 85. A partial lump sum payment of capital is possible, however, up to a total of 30 % of the capital available at the beginning of the payment stage.
- At the beginning of the payment stage, at least the amounts that have been paid (individual contributions and allowances) must be guaranteed by the provider. The investment contracts can be linked to a pension for reduction of earning capacity and/or a surviving dependant's pension without reducing the amount of promotion.
- During the savings stage, the investments are protected by law against pledging or being offset in awarding social assistance and employment benefit II.
- Gender-neutral tariffs (so-called "unisex tariffs") are strictly prescribed for contracts concluded from 1.1.2006.

### **Forms of investment eligible for support**

Private old-age pensions insurance, fund and bank saving schemes are eligible for support in the framework of private capital-covered old-age pension provision. Fund and bank saving

schemes must be linked to payment plans and a residual pension for the highest age stage. Furthermore, occupational old-age provision can be promoted in the shape of direct insurance, "Pensionskassen" and pension funds.

### **Inclusion of real estate**

To create or acquire owner-occupied domestic real estate, capital already saved from an old-age pension provision contract may be removed up to an amount of between Euro 10,000 and Euro 50,000. The amount taken out is to be repaid to the contract in monthly instalments by the age of 65.

### **Promotion concept**

The contribution to old-age pension provision consists of individual contributions and allowances. To relieve the burden on citizens, the beneficiary pays only their individual contributions; on request by the beneficiary, the state allowance is credited directly to the beneficiary contract by the Federal Insurance Institute for Salaried Employees as the central agency. Over and above this, the total old-age pension provision cost can be claimed in the framework of an additional deduction of special expenses. If the tax saved by the deduction of special expenses is greater than the allowance, the difference is additionally credited to the taxpayer. In doing so, the right to the allowance is offset. It is therefore not sufficient to apply for the promotion solely with the tax declaration, even if the fiscal advantage is evidently more favourable than the allowance. Instead, it is necessary to apply for the allowances.

### **The amount of the allowance**

The allowance is composed of a basic allowance and a child allowance.

The basic allowance is

in the assessment periods 2004 and 2005	Euro 76,
in the assessment periods 2006 and 2007	Euro 114,
from the assessment period 2008 annually	Euro 154.

The child allowance per child is

in the assessment periods 2004 and 2005	Euro 92,
in the assessment periods 2006 and 2007	Euro 138,
from the assessment period 2008 annually	Euro 185.

The party which also receives the child benefit is on principle entitled to the child allowance. For children of spouses living together, the mother is however entitled to the child allowance unless the spouses apply for it to be assigned to the father.

Examples:

A sole wage-earner spouse with two children and gross earnings of Euro 30,000 receives for individual expenditure amounting to Euro 522 in 2008 an annual allowance of Euro 678 (2 x Euro 154 + 2 x Euro 185) from the state, hence achieving annual savings of Euro 1,200 (= 4 % of 30,000).

A sole-parent salaried employee with one child not drawing a pensionable income during child-raising leave receives an allowance of Euro 339 (Euro 154 + Euro 185) from the state for a minimum individual contribution of Euro 60 per year in 2008, thus attaining annual savings of Euro 399. The state allowance accounts for 85 % of the total savings in the case.

An overview of the Riester pension

	2005	2006/2007	from 2008
Deduction of special expenses	up to € 1,050	up to € 1,575	up to € 2,100
Basic allowance	€ 76	€ 114	€ 154
Child allowance per child	€ 92	€ 138	€ 185
Minimum individual contribution	2 % <sup>1)</sup> minus allowances	3 % <sup>1)</sup> minus allowances	4 % <sup>1)</sup> minus allowances
maximum	€ 1,050 minus allowances	€ 1,575 minus allowances	€ 2,100 minus allowances
but at least	€ 60	€ 60	€ 60

1) of the previous year's income

Old-age pension provision is built up using untaxed income. For this reason, the later payments are subject to tax (downstream burden).

### Private old-age pension provision: spread and significance

- Additional state-promoted private old-age pension provision is on principle open to all employees who are subject to compulsory social insurance, as well as to public servants.

In detail, those subject to obligatory insurance include the following:

- employees and trainees,
- farmers and family members employed in family businesses,

- recipients of unemployment benefit, unemployment assistance until 31 December 2004 (including beneficiaries whose benefits are suspended because of offsetting of income or assets), unemployment benefit II since 1 January 2005, sickness benefit, injury benefit, pension sickness benefit, transitional benefit, maintenance benefit or early retirement benefit,
  - certain groups of the self-employed – e.g. craftsmen, teachers, midwives, artists and self-employed persons with only one client,
  - those on military service or in civil defence,
  - child carers during childcare periods,
  - carers not acting commercially, and
  - persons in marginal employment ("mini jobs") who have renounced exemption from obligatory insurance.
- 
- A total of roughly 30 million citizens are thus eligible for support.

### **Scope and profitability**

Roughly 4.2 million certified old-age pension provision contracts have been concluded since the introduction of the new promotion tool as in January 2002. Promoted private old-age pension provision contracts have only been in existence since 2002, so that information on typical yields cannot yet be provided. As a result of the high promotion rates, returns are likely to be far higher than average.

## **2.2 The expanded tax deduction of special expenses for private old-age pension provision**

As on 1 January 2005, the Old-Age Income Act added a new capital-covered private basic pension, in addition to classical old-age pensions insurance. The requirements of this basic pension are similar to statutory old-age pensions insurance. Above all, it is to enable the self-employed who are not insured in statutory old-age pensions insurance to insure for their old age, whilst taking advantage of tax breaks. In order to qualify for fiscal promotion of the contributions to a corresponding insurance product, it must not be possible to borrow on the accrued entitlements, they may not be inheritable, transferable or saleable, and it may not be possible to carry them as assets. Such insurance may only be paid out as a monthly lifelong annuity, and not before reaching the age of 60. It is possible to conclude supplementary surviving dependants insurance or insurance for occupational incapacity/reduction of earning capacity.



The contributions, together with contributions to statutory old-age pensions insurance and to professional pension schemes, must on principle be deductible up to Euro 20,000 per year as special expenses. With spouses who are assessed jointly, the amount doubles to Euro 40,000. In the context of a transitional arrangement, a total of 60 % of the contributions made may be tax-deducted in 2005 within these maximum amounts. This proportion will increase by two percentage points per year in the following years, so that the whole contribution will be deductible in 2025.

In accordance with the principle of downstream taxation, the fiscal promotion of the contributions is in line with the taxation applied to the benefits. 50 % of the pension will be taxable on retirement in 2005. The taxable share increases by two percentage points per year for each birth-year of pensioners added until 2020, and after that by one percentage point per year, so that the whole pension will be taxable from retirement in 2040.

## **Annex V Portability in occupational retirement pension provision**

In the context of the Old-Age Income Act, the portability of occupational retirement provision has been reformed in Germany as from 1 January 2005, and a right has been introduced for employees to take occupational pension entitlements with them. Accordingly, employees may demand from their former employers that the value of the vested occupational pension entitlements they have accrued be transferred to the new employer.

However, in order to avoid overburdening both the old and the new employer, as well as the participating insurance facilities, this right does not apply without restrictions. For reasons of legal clarity, and to enable parties to carry out long-term planning, this only applies to new promises. The right also does not exist if the occupational retirement provision was implemented through book reserves or "Unterstützungskasse". Employers should not be forced to cash in early those reserves that are tied up in the enterprise for the old-age provision of their employees should they leave early. The claim is also limited to entitlements the value of which does not exceed the contribution assessment limit applicable to statutory old-age pensions insurance in the transfer year (the contribution assessment limit is Euro 62,400 in 2005). If this limit is exceeded, there is no right to partial portability; this would contradict the fundamental concept of portability to bundle entitlements and not to sub-divide them thereafter. Furthermore, the right can only be asserted towards the old employer up to one year after leaving.

On condition of agreement by the old and new employers, as well as the employee, an agreed export of the occupational pension entitlements is always possible in addition to this.

The new rules for portability apply to the facilities of the public service providing supplementary old-age and dependants' benefits only if they are fully funded entitlements or recurrent benefits. Further, the new arrangement does not apply if the entitlements or recurrent benefits to be transferred from these systems are completely or partly pay-as-you-go or budget funded. Pay-as-you-go entitlements are not based on capital which one could take away.

## Annex VI Description of the link between retirement age/amount of pension

Basis for calculating the information used in the text

Age	Element	Years	Income position	Income points	Monthly pension	Reduction/increase
<b>a) Retirement at 65</b>						
17-19	Vocational training	3	0.2	2.25		
20-64	Pensionable employment	45	1.0	45		
from 65	Old-age pension					
	Total	48		47.25	€ 1,234.64*	
<b>b) Early retirement at age 63</b>						
17-19	Vocational training	3	0.2	2.25		
20-62	Pensionable employment	43	1.0	43		
from 63	Old-age pension					
	Total	46		45.25		
	7.2 % reduction			41.992	€ 1,097.25*	€ -137.39 (-11.13 %)
<b>c) Delayed retirement at 67</b>						
17-19	Vocational training	3	0.2	2.25		
20-66	Pensionable employment	47	1.0	47		
from 67	Old-age pension					
	Total	50		49.25		
	12.0 % bonus			55.16	€ 1,441.33 *	€ +206.69 (+16.74 %)

\*on the basis of the current applicable pension value of Euro 26.13 (West)

## **Annex VII Evaluation of childcare in statutory old-age pensions insurance**

It is the following provisions above all which provide an improvement in independent old-age pension provision for carers:

- On principle, three years are credited as an obligatory contribution period for care for a child ("childcare period"); (for children born before 1992, one year). These times give rise to pensions entitlements equivalent to those of an average earner; the corresponding contributions are paid by the Federation to the old-age pensions insurance. If a job is held at the same time in addition to childcare, the corresponding additional pension entitlements are also accrued.
- The childcare period until the child reaches the age of ten is credited as childcare time. These times by themselves do not give rise to any pension entitlements, and do not directly increase the pension, but they are allowed if certain waiting periods are complied with; they maintain the reduction of earning capacity and have a positive impact on the evaluation of contribution-free periods.
- With carers who are in employment subject to compulsory social insurance during the first ten years of their child's lives, but earn less than the average (for instance because they work part-time), these income times are given a higher pension evaluation than corresponds to the actual earnings. In concrete terms, the actual income is increased by 50 % in this case, but to a maximum of the average income. This is contingent on the carer showing a total of at least 25 years with pensionable periods. This support also benefits carers who are unable to work in many cases because of caring for a child in need of long-term care. Here too, the obligatory contribution time to be recognised for the carer is upgraded by 50 % when calculating the pension, but up to a maximum of the value emerging from 100 % of the average earnings, indeed until the child in need of long-term care has reached the age of 18.
- If no gainful employment is carried out due to simultaneous care for two or more children under the age of ten, and hence it is not possible to upgrade contribution times, a credit of pension entitlements is granted as compensation. This credit corresponds to the maximum additional pension entitlement which can be attained by upgrading employment times with below-average earnings, whilst at the same time caring for a child.

## **Annex VIII Old-age pension provision education campaign**

### **Goal of the campaign**

Statutory old-age pensions insurance as the basis for old-age pension provision is the starting point from which the rationale of and the necessity for additional provision is explained. Educational support is to counter the lack of willingness to conclude pension contracts which arises from a lack of information on one's own security in old age and insecurities in dealing with pension products. The campaign is to be used to increase knowledge of one's own old-age pension provision and to point to possibilities of acquiring additional security in old age. A central concern here is to offer a uniform picture of old-age pension provision and to reduce prejudices.

The primary target group of the courses is to be the age group of 30 to 45-year-olds, without excluding other interested parties. There is also the special goal of reaching those who have not yet considered old-age pension provision.

### **Cooperation partners**

The goal of a broad-based educational campaign for old-age pension provision can only be achieved if the Federal Government works together with partners who can appear towards citizens both as experts in matters related to old-age pension provision, and as provider-independent advisors. At the same time, the partners must be able to act all over Germany. In light of these criteria, the old-age pensions insurers and the Association of German Adult Education Institutions are particularly suitable partners in implementing an educational campaign related to old-age pension provision. The advisory structures of old-age pensions insurers and the roughly 1,000 evening schools provide an infrastructure which can be activated with little effort to implement a broad-based educational service.

### **Campaign approach**

In the framework of the educational campaign of old-age pension provision, the working title of which is "Well-informed about pensions", is to stress the significance of statutory old-age pensions insurance, as well as publicising occupational and private old-age pension provision. At the same time, citizens are to be enabled to comprehend the claims made by statutory old-age pensions insurance in terms of old-age pension provision as a whole, and to find the type of additional old-age pension provision which suits them best. The courses at the evening schools form the core of this service in which modern public relations work seeks to spread knowledge of supplementary private and occupational provision and acceptance of statutory old-age pensions insurance. This approach enables participants to assert their ideas effectively, together with other players, in order to achieve a public relations impact. For instance, the social partners have also been included in the campaign.

### **Concepts of the courses**

The courses are to take place over six evenings (of two hours each) and teaching the basic knowledge of statutory old-age pensions insurance and the supplementary private old-age pension provision and occupational old-age provision. The information taught will accommodate the needs and interests of the participants. It is not planned to provide individual advice to participants. For instance, no specific statements will be made with regard to specific products, and no concrete offers will be made by financial service-providers. However, the training would involve statements on product categories and their respective advantages and disadvantages. Consumer protection is discussed insofar as it is necessary to teach the participants what they themselves can do. In this, the accompanying material has many uses as a source of information.

At the same time, course participants are to be better informed about their current level of provision when it comes to statutory old-age pensions insurance. It is only on the basis of well-founded knowledge of the level of old-age provision available from statutory old-age pensions insurance that rational decisions can be taken on the amount and form of supplementary private old-age pension provision or occupational old-age provision. It is also a goal for participants to be able at the end of the course to successfully plan for themselves a consultation with a provider of private or occupational old-age pension provision products.

### **Accompanying material**

The material on the courses is to contain background information and checklists which, firstly, increase their useful value for the participants and, secondly, introduce supplementary information which cannot be provided in the necessary detail by the speaker. In addition to the printed material, password-protected access is to be created in the campaign's Internet presentation to an internal area providing background information and decision-making aids (standard letters, legal information, factsheets, checklists, etc.). The drafting of the teaching material will be managed by the old-age pensions insurance providers.

### **Speakers**

The speakers are to be provided by the old-age pensions insurers. The latter can contribute their broad knowledge of statutory old-age pensions insurance and on the promoted forms of supplementary old-age pension provision to the courses. This guarantees that broad knowledge is available and the training needed for the speakers can be much reduced. Furthermore, speakers' particular skills can be used to increase the quality of the courses.

On the basis of the specific skills profile of the speakers provided by the old-age pensions insurers, it however remains necessary to provide training (presence training, as well as locally

supplemented by e-Learning) to ensure that all courses are implemented according to the same content and didactic concepts. Furthermore, this ensures that the specific requirements of courses of adult education as to didactic support of the material are properly taken into account.

### **Timetable**

The pilot phase of the project is to be launched in the second half of 2005. It will serve to examine the "fitness for purpose" of the concept, the materials and the advertising strategies.

The main phase of the project will take place in 2006. This means that the courses will be offered in the spring and autumn programmes of the evening schools involved. These will take place from February 2006 to February 2007, followed by an evaluation of the experience gained in the main phase.

The project is to be structured such that the evening school courses will become self-administrating after the main phase of the campaign. Parallel to the evaluation, other courses are already being taken on as elements of the standard offering in the evening school programme.

Over and above this, in cooperation with the financial services industry the Federal Government is taking on further activities to improve general financial education and the orientation knowledge on old-age pension provision:

The new information portal on money matters ([www.kursraumgeld.de](http://www.kursraumgeld.de)) established by the Finance Initiative Germany (IFD) targets teachers and school pupils. In addition to providers of additional old-age pension provision and their associations, the initiative also includes the Federal Government (Federal Ministry of Finance). In addition to current teaching materials on topics related to old-age pension provision and other financial topics, the portal also offers information on choice of profession, as well as on projects, seminars and events for school pupils and teachers. Teachers can request speakers on specific topics centrally via the IFD portal.

## **Annex IX      Representative cross-section analysis**

The Federal Ministry of Health and Social Security has implemented an annual study, initially from 2005 to 2008, on fundamental health and socio-political attitudes among the population. The study comprises three modules:

- Launch study (amongst other things giving concrete shape and operationalising the research questions, testing the survey tools); this phase is complete;
- Annual representative cross-sectional studies on health and socio-political attitudes among the population with changing foci (telephone interviews with standardised questionnaires and a targeted net sample size of 5,000 respondents, foci: 2005 and 2007 health/social assistance; 2006 and 2008 pensions/long-term care/accident);
- Accompanying trend analyses (three times per year in three to five groups of between six and twelve participants each, studying current trends in the opinions, attitudes and the state of information of the participants; this is gained through moderated and guideline-aided group discussions).

The research goal has three objectives:

1. To ascertain the fundamental attitudes among the population, as well as of individual population groups, on the acceptance of the social welfare state, as well as identifying attitudes towards individual social security sub-systems (amongst others on the old-age pension provision system) and on alternative concepts. Five areas of attitude are studied: circumstances among the players (market, state, civil society), goals, instruments, results and costs of social policy.
2. To survey the factors and experiences impacting the development of and changes in attitudes on the social security systems. The influence of economic contexts, of objective situations and subjective well-being is calculated, as is the significance of normative basic orientations (such as ideas of justice) and the perception of social equality and inequality affecting the acceptance of the social welfare state.
3. To study the change in attitudes towards the social welfare state over time. There are efforts towards longer-term comparison perspectives making it possible to judge stability and change in the study period more accurately. This is achieved amongst other things by selecting replication of questions from surveys which in part already led to relevant results on this topic in the seventies.

According to the current plan, the questions on German old-age pensions insurance for the respondents from 2006 and 2008 relate to

- confidence in the institution,



- an evaluation of the equivalence principle,
- knowledge of how it works,
- the goal (poverty avoidance, safeguarding standard of living, et al.),
- various options to safeguard funding, and
- the assessment of the reforms to date and the need for further reforms.

## Annex X Increasing age limits in Germany

Types of old-age pension and age limits		Retirement																						
		1996 and earlier	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013 and later					
Old-age pension because of unemployment or after part-time work in old age	Age limit for earliest possible retirement <u>without</u> reductions	60	60 to 61	61 to 62	62 to 63	63 to 64	64 to 65	65	65	65	65	65	65	65	65	65	65							
	Age limit for earliest possible retirement <u>with</u> reductions		60	60	60	60	60	60	60	60	60	60 to 61	61 to 62	62 to 63	63	63	63							
Old-age pension for women	Age limit for earliest possible retirement <u>without</u> reductions	60	60	60	60	60 to 61	61 to 62	62 to 63	63 to 64	64 to 65	65	65	65	65	65	65	65							
	Age limit for earliest possible retirement <u>with</u> reductions					60	60	60	60	60	60	60	60	60	60	60	60							
Old-age pension for persons with disabilities	Age limit for earliest possible retirement <u>without</u> reductions	60	60	60	60	60	60 to 61	61 to 62	62 to 63	63	63	63	63	63	63	63	63					63	63	63
	Age limit for earliest possible retirement <u>with</u> reductions						60	60	60	60	60	60	60	60	60	60	60					60	60	60
Old-age pension for insured persons of long standing	Age limit for earliest possible retirement <u>without</u> reductions	63	63	63	63	63 to 64	64 to 65	65	65	65	65	65	65	65	65	65	65	65	65			65		
	Age limit for earliest possible retirement <u>with</u> reductions					63	63	63	63	63	63	63	63	63	63	63	63	63 to 62½	62½ to 62			62		

Source: Federal Ministry of Health and Social Security