



# **Peer Review on “Minimum income benefits – securing a life in dignity, enabling access to services and integration into the labour market”**

**Host Country Discussion Paper - Germany**

**Minimum Income Benefits in Germany**

**Germany, 15 – 16 November 2018**

**DG Employment, Social Affairs and Inclusion**

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## **1 Executive Summary**

In Germany, there are three systems to guarantee a minimum income for different groups of recipients, (1) *Basic Income Support for Employment Seekers* (Social Code Book II), (2) *Social Assistance with the Basic Income Support in Old Age and in the Event of Reduced Earning Capacity* and the *Livelihood Assistance Benefit* (Social Code XII) and (3) *Benefits for asylum seekers*.

The minimum income benefits systems must meet the requirements of the German Constitution (Basic Law), as interpreted by the Federal Constitutional Court. The constitution ensures to each person in need of assistance the material prerequisites which are indispensable for his or her physical existence and for a minimum of participation in social, cultural and political life. This binds the legislative authority and the administration.

Assistance includes a lump sum standard needs, actual costs of adequate accommodation and heating, additional benefits for specific situations and benefits for education and social participation. The standard needs are calculated using a statistical model. Calculation is based on the spending patterns of people with low income. The reference group consists of the 15 % of the households with the lowest income; households receiving minimum income benefits with no additional income are excluded from the reference group in order to avoid circular reasoning. Certain expenditure categories which are not considered as basic-needs-relevant are not considered. Different basic need levels are applied to single adults, two adults who run a joint household, adult members of a benefits community and juvenile and children.

In principle, recipients of *Basic Income Support for Job Seekers* and *Basic Income Support in Old Age and in the Event of Reduced Earning Capacity* are subject to compulsory insurance in the statutory health and long-term care insurance fund. Needs for accommodation and heating are not included in the standard needs; these costs are covered additionally as far as they are considered reasonable. Supplementary needs are provided in special circumstances and situations. Children, juveniles and young adults from families receiving *Basic Income Support for Job Seekers*, child allowance, housing benefits or asylum seekers benefit are entitled to benefits for education and social participation.

The Social Code Book II was adopted at the height of unemployment in Germany and came into force at the beginning of 2005. Reducing unemployment and creating stronger incentives to take up work were the main objectives of the reform policy.

If earnings are insufficient to ensure the minimum subsistence level, employees and self-employed in need are entitled to receive complementary *Basic Income Support for Employment Seekers*. In order to create stronger incentives to take up work, not all income from work is deducted when calculating the entitlement to benefits. When the Social Code II was passed, a special child allowance for employees with low earned income was introduced. It is granted to those employees with children (for whom they receive child benefits) who can cover their own needs and those of their partners, but not the needs of their children. The idea behind this has been that nobody who can take care of him- or herself should depend on complementary *Basic Income Support for Employment Seekers* just because he or she has to care for children.

There is a political debate about the level of basic needs. If proposals to increase basic needs were to be implemented, the number of recipients would substantially increase. In the German debate on poverty this might cause paradoxical effects as the rate of recipients of minimum income benefits is used as a poverty indicator.

The political and academic debate addresses the high effective marginal 'tax' rate for those earning an income which is not high enough to end their dependence on complementary *Basic Income Support for Employment Seekers* or other forms of support. There is a debate on how to better combine the different instruments (child benefit, child allowance, advance payment of maintenance for children living in single parent families and housing benefit) in order to better support families whose parents are employed but need supplementary assistance to cover the needs of their children.

## **2 A brief overview of the minimum income benefits systems**

### **2.1 Overview**

In Germany, there are three systems to guarantee a minimum income for different groups of recipients. These systems are at large:

- *Basic Income Support for Employment Seekers* outlined in Social Code Book II (Grundsicherung für Arbeitssuchende, Sozialgesetzbuch II)
- *Social Assistance* (Sozialhilfe), with the *Basic Income Support in Old Age and in the Event of Reduced Earning Capacity* (Grundsicherung im Alter und bei Erwerbsminderung) and the *Livelihood Assistance Benefits* (Hilfe zum Lebensunterhalt) in Social Code Book XII (Sozialgesetzbuch XII)
- Benefits for asylum seekers under the corresponding legislative act (Asylbewerberleistungsgesetz, AsylbLG).

If the person in need is not eligible for asylum seekers benefits, then the following rule applies for the assignment to the other two systems:

#### **Basic Income Support for Employment Seekers:**

A person, who

- is older than 15 years and has not yet reached the statutory standard retirement age,
- has his/her regular residence in Germany,<sup>1</sup>
- is capable to work for at least three hours a day under the usual conditions of the labour market, and
- is in need of support (depending on a means test).

is entitled to *Basic Income Support for Job Seekers*. Such persons and their spouses, partners and certain relatives living together form a so-called benefits community ('Bedarfsgemeinschaft'). Members of such a benefits community, who are unable to work and therefore not considered as employable, receive benefits, too - the *Sozialgeld* (social benefit), if they are not entitled to other forms of assistance.

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<sup>1</sup> Foreigners from other EU Member States entering Germany solely to search for work have no entitlement to *Basic Income Support*. They only acquire entitlements to benefits in the relevant benefit system after five years of residence. Those who have no entitlement to social welfare benefits can apply for assistance for one month and for a loan to cover the costs of returning to their home country. The underlying principle is that they must apply for that basic income support in their home countries.

## **Social assistance, especially Basic Income Support In Old Age And In The Event Of Reduced Earning Capacity**

Persons who are neither entitled to *Basic Income Support for Job Seekers* nor belong to a benefits community are covered by social assistance as regulated by Social Code Book XII. Social assistance includes various forms of assistance for different situations of need. Among these is the *Basic Income Support in Old Age and in the Event of Reduced Earning Capacity*. These benefits were implemented in 2003 to reduce the number 'hidden poor' among the elderly. Although minimum income benefits were available before 2003, also for this group, a number of elderly people shied away from applying for it, fearing that recourse might be taken from their children.

The following persons are entitled to the Basic Income Support in Old Age and in the Event of Reduced Earning Capacity:

- above the statutory standard retirement age,
- who are permanently not able to work or only less than three hours a day.

There are additional statutory provisions for persons in need who are covered neither by the *Basic Income Support for Employment Seekers* nor the *Basic Income Support in Old Age and In the Event of Reduced Earning Capacity*. This assistance, called *Livelihood Assistance Benefits* (Hilfe zum Lebensunterhalt) is granted, for example, if it has not yet been recognised that a person of working age is permanently unable to work and therefore entitled to *Basic Income Support in the Event of Reduced Earning Capacity* (Schwengers / Ehmann, p. 322).

The three minimum income benefit systems are tax-funded. In contrast, unemployment insurance is financed by contributions from employees and employers (one pillar of the social security system).

The public employment agency together with the communal authorities bear responsibility for assisting recipients of Basic Income Support for Job Seekers. They cooperate and form joint institutions, the so-called Jobcentres. Some of the Jobcentres are run by the county/municipality alone (municipal Jobcentres). On any decision an official notification is given in writing. In case of disagreement, the applicant can file an administrative appeal within one month after receipt of the notification. If the appeal does not lead to an amendment of the decision in the applicant's favour, he or she may appeal to the Social Court.

## **2.2 Constitutional Obligations**

The minimum income benefits systems must meet the requirements of the German Constitution (Basic Law), as interpreted by the Federal Constitutional Court in a fundamental judgement of 9 February 2010 (1 BvL 1/09, 1 BvL 3/09, 1 BvL 4/09): 'The fundamental right to the guarantee of a subsistence minimum that is in line with human dignity from Article 1.1 of the German constitution (Grundgesetz – GG) in conjunction with the principle of the social welfare state contained in Article 20.1 of the Basic Law ensures to each person in need of assistance the material prerequisites which are indispensable for his or her physical existence and for a minimum of participation in social, cultural and political life.' This right 'is not subject to the legislature's disposal and must be honoured; it must however be lent concrete shape, and be regularly updated, by the legislature, which has to orientate the benefits to be paid towards the respective stage of development of the polity and towards the existing conditions of life.' (Headnotes No. 1 and 2; Translation by the Federal Constitutional Court).



### **2.3 How to calculate the standard needs?**

The following explanations are limited to the *Basic Income Support for Employment Seekers* (Social Code Book II) and the *Basic Income Support in Old Age and in the Event of Reduced Earning Capacity* and the *Livelihood Assistance* benefits (Social Code Book XII). For asylum seekers, especially those who are not yet recognised, who have lived in Germany less than 15 months, as well as those living in shared accommodation, significantly different rules apply in parts (Frings, 2017).

Assistance includes:

- lump sums for standard needs ('Regelbedarf');
- actual costs of adequate accommodation and heating;
- additional benefits for specific situations (such as pregnancy, single mother/father, disability, need for a special diet);
- benefits for education and participation.

The calculation of the standard needs is based on the **sample survey of income and expenditure (Einkommens- und Verbrauchsstichprobe, EVS)**, carried out every five years by the Federal Statistical Office. Roughly 60 000 private households participate. For a period of three months they note all income and expenditure in a household diary. One fifth of the participating households also records all expenditure on food, beverages and tobacco goods by volume and prices in detail. The spending patterns of people with low income are recorded statistically based on the households in the so-called reference group. It consists of the 15% of the households with the lowest income; households receiving minimum income benefits with no additional income are excluded from the reference group in order to avoid circular reasoning. Households that would be entitled to receive minimum income benefits but do not apply for it ('hidden poor') are not excluded. This is being discussed critically, since these households can usually only spend less than the sociocultural minimum, which is calculated based on the expenditures of the reference group. Based on the sample surveys of EVS or others, an exact calculation of the share of the 'hidden poor' is not possible; however, there are several proposals to approximate the size of this group (Institut für Arbeitsmarkt- und Berufsforschung, 2013). To date, none of these proposals have been implemented.

Based on the EVS sample survey, **the basic-needs-relevant consumer spending** is calculated. Benefits for adults are calculated based on the data of households of single persons and the benefits for children on the basis of data of family households (couple with one child). Certain expenditure categories which are not considered as basic-needs-relevant are deducted (e.g. tobacco, cut flowers and indoor plants, canteen food, dry cleaning). Although appropriate motor vehicles owned by job seekers are not to be taken into account as assets, the current expenditures for a car are not considered as basic-needs-relevant. Instead, expenditures on the mobility needs by public transport are considered. Instead of spending on alcoholic beverages, the corresponding expenditure on non-alcoholic drinks is calculated.

Based on the EVS 2013, the basic-needs-relevant-consumer spending for a single-person household was calculated and determined by law (Gesetz zur Ermittlung der Regelbedarfe nach § 28 des Zwölften Buches Sozialgesetzbuch 22.12.2016; Bundesregierung 2016): see Appendix.

The basic-needs-relevant consumer spending of € 394.84 (2013) for a single adult was adjusted by a mixed index based on price trends (70%) and wage/salary trends (30%). Accordingly, the amount was € 409 in 2017 and € 416 in 2018

**Different basic need levels are applied:**

1	Adult who is either single or a single parent and runs its own household	€ 416
2	Two adults who run a joint household as married couple or as partners (married like or partner-like arrangement)	€ 374
3	Adult members of a benefits community, who are fit for work, and adults living in a social institution	€ 332
4	Juvenile aged between 14 and below 18	€ 316
5	Children aged between 6 and below 14	€ 296
6	Children below six	€ 240

In principle, recipients of *Basic Income Support for Job Seekers* and *Basic Income Support in Old Age and in the Event of Reduced Earning Capacity* are subject to compulsory insurance under the statutory health and long-term care insurance fund. Payments are made by the Jobcentre. There are separate rules for those who were a member of a private health insurance scheme before receiving assistance.

## **2.4 Needs for accommodation and heating and further needs**

**Needs for accommodation and heating** are not included in the standard needs. These costs are covered additionally as far as they are considered reasonable. Amounts depend on the local authority's guidelines and reference values. If costs for accommodation are considered to be too high, the beneficiary's household is obliged to reduce costs, e.g. moving to a cheaper accommodation. In this case higher costs will be paid only for a limited period of time, usually not longer than six months. The scheme to cover the costs of housing and heating requires costs to be checked and paid for each household individually.

**Supplementary needs** are provided in special circumstances and situations such as allowances for single parents (e.g. € 150 in case of one child under the age of 7 years), for expectant mothers from the 13<sup>th</sup> week of pregnancy or for people who require cost-intensive dietary food. Costs for domestic hot water generation are to be considered separately in case of non-central hot water generation, as this is not included in accommodation costs. Beneficiaries are entitled to receive on-off payments for initial furnishing and fittings for their home (including appliances) and for initial supply of clothing and items needed in pregnancy and after the birth of a child.

Children, juveniles and young adults from families receiving *Basic Income Support for Job Seekers*, child allowance, housing benefits or asylum seekers benefit are entitled to **benefits for education and social participation**. This covers school trips, personal school supplies (€ 100 euro annually), learning grants for private lessons if the school confirms the need and allowance for lunches if offered by child day-care centres or schools (parents contribute one euro per day). A school travel allowance is usually given to those pupils who cannot reach the nearest secondary school on foot or by bicycle. For the membership in clubs or the participation in cultural activities, an amount of € 10 per month is provided. With the exception of personal school supplies, all benefits must be applied for (Bundesagentur für Arbeit, 2017b, p. 52 f.).

## 2.5 Deduction of income and consideration of assets

When calculating the benefits community's need of assistance, the **incomes of the household members** are taken into account. This includes income from dependent employment and self-employment,<sup>2</sup> wage compensation payments such as employment benefits, parental benefits or sick pay, alimony payments by the divorced spouse, child benefit, capital and interest earnings, pensions of all kinds, non-recurring income like tax refunds, severance payments or inheritances and vocational training assistance, as well as grants based on the German Federal Law on Training and Education Promotion (Bundesagentur für Arbeit 2017 b, p. 46).

**Assets** are considered to determine whether a household is eligible for assistance. There are significant differences between *Basic Income Support for Job Seekers*, *Basic Income Support in Old Age and in the Event of Reduced Earning Capacity* and *Livelihood Assistance Benefits*. In all these systems, to a certain extent, assets do not rule out or reduce the need for assistance. For *Basic Income Support for Job Seekers*, the following deductions are made:

- basic allowances of € 150 per year of life,
- pension provision from 'Riester' investments, a tax-subsidised pension scheme,
- allowance for other pension provision of € 750 per year of life in case realisation before retirement age is excluded,
- allowance for necessary purchases in the amount of € 750,
- appropriate household goods, an appropriate motor vehicle and a reasonable owner-occupied flat or house are not to be taken into account (Bundesagentur für Arbeit 2017 b, p. 50 f.).

## 2.6 Obligations and sanctions

The Social Code Book II was adopted at the height of unemployment in Germany and came in to force at the beginning of 2005. The main objectives of the reform policy were to reduce unemployment and create stronger incentives to take up work. Recipients of *Basic Income Support for Employment* carry certain obligations, especially to undertake efforts to find a job or otherwise reduce or end their need for public welfare. If such obligations are violated, the benefits received may be reduced; in the case of repeated violations, the benefits may be withdrawn completely. Young people under the age of 25 are subject to harsher sanctions than persons above the age of 25.

## 3 Allowance for gainful employment and Child Allowance

### 3.1 Allowance for gainful employment

Being unemployed is not a prerequisite for receiving *Basic Income Support for Employment Seekers*. If earnings are insufficient to ensure the minimum subsistence level, employees and self-employed in need are entitled to receive complementary *Basic Income Support for Employment Seekers*. In order to create stronger incentives to take up work, not all income from work is deducted when calculating the entitlement to benefits. The first € 100 of earned gross income are exempt. 20 % of the income over € 100 and up to € 1000 and 10 % of the income over € 1000 and up to € 1200 income (in benefits communities with at least one child up to € 1500) are exempt, too. All income over € 1200 (respectively € 1500) is fully deducted.

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<sup>2</sup> See also the remarks on the allowance for gainful employment, p. 6

Before the introduction of the *Basic Income Support for Employment Seekers*, the regulations on the deduction of income from employment in calculating the assistance entitlement were much more restrictive. Consequently, the incentives to take up a job were low as long as no income could be raised that was high enough to overcome the dependence on assistance. The regulation in force now ensures that those who work have a higher disposable income than those who receive *Basic Income Support for Employment Seekers* without working. With a gross income of € 1500, which is a full-time job slightly above the minimum wage, the difference is € 300 (with child: € 330). Those who have never been unemployed also receive supplementary *Basic Income Support for Employment Seekers*, if they earn less than the assistance they would be entitled to in case of unemployment, in addition to the allowance for gainful employment. If this were not the case, those who start to work after having been unemployed and have previously received *Basic Income Support for Employment Seekers* would have a permanent advantage compared to those who start and continue to work without periods of unemployment.

### **3.2 Child Allowance**

As shown, *Basic Income Support for Employment Seekers* as regulated in Social Book II supports far more people than just long-term unemployed and their families. There is a constant debate in Germany to strengthen other parts of the social security system (family allowance, child allowance for low-earning employees, housing benefit) in order to reduce the dependence on complementary *Basic Income Support for Employment Seekers* or other minimum income benefits.

When the Social Code II was passed, a special child allowance for employees with low earned income was introduced. It is granted to those employees with children (for whom they receive child benefits) who can cover their own needs and those of their partners, but not the needs of their children. The idea behind this has been that nobody who is capable of taking care of him- or herself should depend on complementary *Basic Income Support for Employment Seekers* just because he or she has to care for children. In its current form, the child supplement meets this requirement only partially; especially single parents working part-time are not reached.

## **4 Integration into the labour market**

Besides ensuring minimum income benefits, the primary objective of the Social Code Book II is to integrate job seekers into appropriate employment as fast as possible. As mentioned, Social Code Book II was adopted when the unemployment rate in Germany was about twice as high as today. Before receiving assistance, recipients of *Unemployment Benefit II* (Arbeitslosengeld II, ALG II) were either not working or only working for very short time, or if they worked for longer periods before becoming unemployed, the eligibility to receive unemployment insurance benefits ended. The recipients are by no means a homogeneous group. There is a significant turnover of people who are overcoming the need for assistance and others who are receiving *Unemployment Benefit II* for the first time or repeatedly.

Part of the active labour market policies for job seekers are traditional employment promotion instruments. All Jobcentres provide a standard service to their job seekers, including:

- an individual (qualified) contact person for each recipient;
- assessment of employment potential (profiling);
- agreement on an individual action plan (IAP);

- access to the full spectrum of active-labour-market-policies-measures, in the sense that the target group is eligible for such measures, but the contact person has discretion to decide whether a person is allowed to participate in a measure or not;
- provision of job offers; and
- regular follow-up of the profiling-IAP process (with a contact interval of three to six months) (Host Country Discussion Paper 2016; p. 11 f.).

Since the mid-2000s, the employment situation in Germany has improved markedly, also for the long-term unemployed. However, among the group of recipients there is a large group of people who have been unemployed for many years, the persistent nucleus of unemployment. They only have a chance to enter or return to the labour market with special support tailored to their individual situation. Access to social services like debt counselling centres or addiction counselling centres are essential too.

Many persons in the persistent nucleus of unemployment are without (or without an up-to-date) vocational training, with health problems or insufficient knowledge of the German language. There are some programmes for employment on the secondary labour market, so far with limited success (see in detail Host Country Discussion Paper 2016).

There are still major reticence and objections against the secondary labour market, where jobs are subsidised by public funding, especially in the craft sector and in parts of the trade unions. In the first few years following the German reunification, in the *New Länder*, secondary labour instruments were extensively used. Since the majority of the unemployed at that time had good qualifications and no health or other personal restrictions, secondary employment did replace regular employment. Today, the situation is very different. If the target group of these programmes is consequently restricted to long-term unemployed with severe personal limitations, the risk of replacing regular employment is small. However, incentivising employers to support these programmes is a big challenge.

## **5 Difficulties and constraints**

### **5.1 Political debate on the amount of standard needs**

The statistical procedure used in setting the social security standard rates satisfies the requirements of the Federal Constitutional Court; it has not been objected to in recent judgments of the Court. The Court accepts a broad scope of assessment by the legislator. It stated that it cannot be said that the standard rates are 'evidently inadequate', however, the legislator has to ensure that identifiable risks of underfunding of minimum income benefits will not occur (Decision, July 23, 2014, 1 BvL 10/12, Rz. 86).

Beyond constitutional considerations, there is a political debate about the level of the minimum income benefit. According to *Caritas Germany* (the welfare organisation of the Catholic Church), the statistical procedure is appropriate at large, but *Caritas Germany* calls for the removal of the 'hidden poor' from the reference group and the extension of the reference group up to 20 %. It is also criticised that the statistical procedure would not be consistently applied to some expenditure categories. *Caritas Germany* proposes a 'flexibility reserve' in addition to the standard rates in order to enable aid recipients to be more flexible in their way of life (Deutscher Caritasverband, 2015). *Caritas Germany* expressed doubts as to whether the amount calculated for household electricity is sufficient (Aigeltinger et.al., 2015). *Diakonisches Werk* (the

welfare organisation of the Protestant Church) proposed an alternative calculation method to be based on the expenditures of middle income recipients (third quintile). Different deductions are proposed for different types of goods (food up to 15 %, clothing and other essential goods up to 25 %, other requirements up to 40 %). This procedure would lead to a significant increase in the minimum income standard rates, especially for single adults (Becker, 2016).

If these proposals were implemented, the number of recipients would substantially increase. In the German debate on poverty, this might cause paradoxical effects. The rate of recipients of minimum income benefits is used as a poverty indicator, in addition to the at-risk-of-poverty rate. Higher levels of assistance can lead to the public misconception that poverty has increased. This happened after 2003 when the *Basic Income Support in Old Age and in the Event of Reduced Earning Capacity* was introduced. Prior to 2003, poor old citizens received Social Assistance and the Social Assistance offices had recourse to their children. Therefore, many poor old citizens did not apply for these minimum income benefits and were hiddenly poor. In 2003, the recourse to the children was abolished (it only applies to children with an income over € 100 000 per year). In the following years, the number of recipients increased sharply. This was often interpreted as an indication of growing problems, although it was a result of an improvement in the minimum income system. The number of recipients would further increase if 'hidden poverty' were tackled more intensively and all old people eligible for minimum income benefits would apply for it.

## **5.2 Is everything much too bureaucratic?**

There is an intense debate in Germany as to whether the minimum income benefits system is far too bureaucratic. However, there is a tension between simplicity and justice. This is illustrated by the rules on reimbursement of housing and heating costs for recipients of minimum income benefits. The amount of costs considered to be reasonable is subject of numerous judicial proceedings. There are constant complaints that the regulations of the *Basic Income Support for Employment Seekers* are too complicated and thus cause too much administrative burden (Alt 2017). So far, efforts to simplify the system have had limited effects. This is due, on the one hand, to the fact that all substantive changes require an agreement between the Federal Government and the *Länder*, and that consensus with the municipalities must be reached. On the other hand, requirements to meet the conditions of each individual case as fairly as possible must be weighed against administrative considerations. Rents vary greatly by region and also within the same region, and whether a tenancy has existed for a long time or was contracted recently also plays a role. Moreover, the energy standards of apartments and thus the heating costs differ widely. A lump sum to cover costs for accommodation and heating would either have to be rather high in order to meet the needs of most households. On the other hand, a low lump sum would bear the risk that a part of the households would be unable to meet their needs and would have to finance part of the costs for accommodation and heating from the social security standard rate (which do not cover these costs) at the expense of other needs.

## **5.3 Does Basic Income Support for Employment Seekers promote poverty wages?**

As a result of the regulation on the allowance of gainful employment, there are numerous employees who receive supplementary *Basic Income Support for Employment Seekers*. They and their family members are counted in the statistics of the recipients of *Basic Income Support for Employment Seekers* and "Sozialgeld". In 2017, 1.1 million employees received complementary *Basic Income Support for Employment Seekers* (Bundesagentur für Arbeit, 2017a, p. 24). In solidified public

perception, this is evidence that the *Unemployment Benefit II* would subsidise poverty wages. But a closer look is necessary.

Nearly 400 000 of the 1.1 million have marginal employment only (up to € 450). For these so-called 'Minijobs' the employees do not pay taxes and social security contributions. Whatever the wage rate per hour might be, when working as Mini-jobbers exclusively, employees never earn more than € 450. In these cases, recipients of *Basic Income Support for Employment Seekers* supplement their income by work on a very limited scale; if paid at minimum wage level, about 12 hours a week. Improving incentives to do so was an explicit objective of the labour market reforms mid-2000s.

Another 600 000 are employees covered by the social security system, but 400 000 of them work part-time. A part-time job often is not enough to make a living, in particular if a partner and/or child are to be cared for. The other 200 000 out of 600 000 work full-time. However, before concluding that they all are badly paid, one should consider the family context. 26 000 of those working full-time are single parents. 29 000 live together with a partner and no children; presumably their partners do not work or a few hours only. Another 83 000 employees covered by the social security system live in a benefits community together with their partner and children, and their full-time jobs are not enough to support themselves and their families. 47 000 are single, working full-time who, despite full-time work, depend on supplementary assistance. The existence of a group of singles working full-time and receiving complementary *Basic Income Support for Employment Seekers* is an indication that there are still shortcomings in enforcing the minimum wage.

#### **5.4 Very high marginal 'tax' rates**

The political and academic debate addresses the high effective marginal 'tax' rate for those earning an income which is not high enough to end their dependence on complementary *Basic Income Support for Employment Seekers* or other forms of support (Peichl et. al., 2017a.). The marginal tax rate 'indicates what proportion of every additionally earned euro has to be deducted whether in the form of the withdrawal of social welfare benefits, through income tax, or as social security contributions from the total amount of income directly available to the earner.' (Peichl et.al. 2017 b, p. 1).

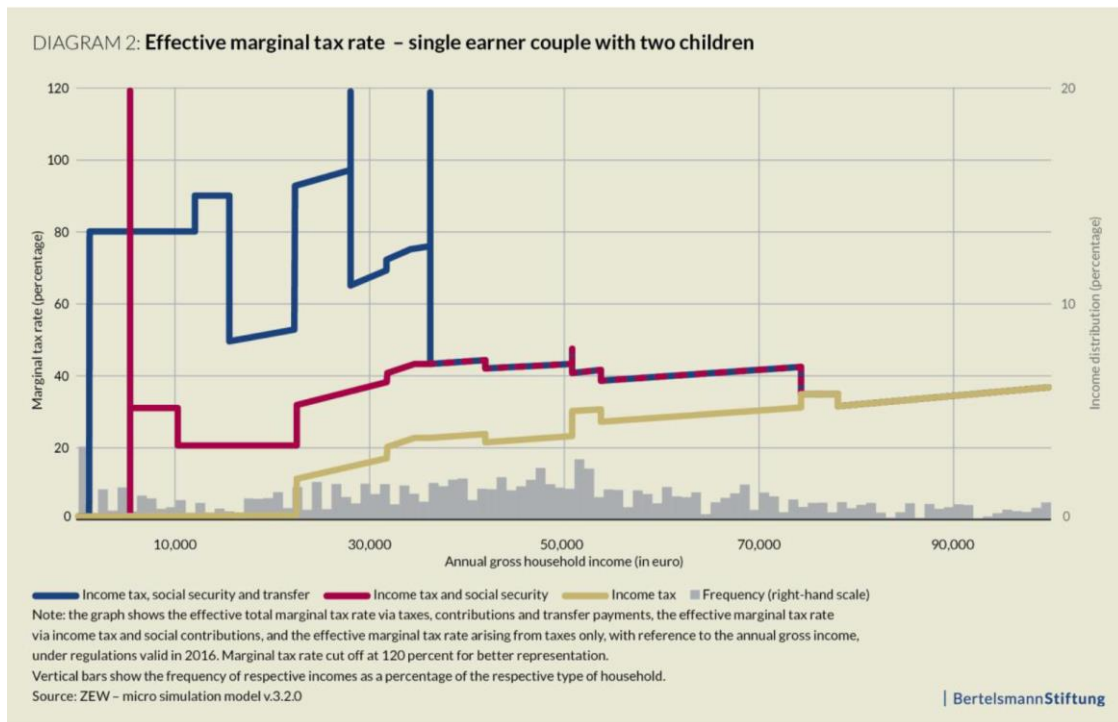
As explained, the transfer-withdrawal rate associated with *Basic Income Support for Employment Seekers* for earnings is 80% for earnings between € 100 und € 1000 and 90% for earnings between € 1000 und € 1500. Peichl et. al. explains the progression of the effective marginal tax rate for a single earner couple with two children as shown in the below diagram:

The transfer-withdrawal rate "never jumps to 100 % because a priority check between the basic social-security claim and an alternative claim for supplementary child benefits [child allowance] and housing benefits comes into effect beforehand (from about € 15,700 [per year]). ... For incomes higher than about € 15,700, the marginal tax rate then stands at about 50 %, because only the housing-related portion of the benefits received is offset by higher incomes and thus gradually withdrawn. However, when the additional transfer withdrawal associated with the supplementary child benefit comes into effect as annual income reaches about € 22,400, the marginal tax rate at first increases to 92 %. At the same time, it is in this range that the obligation to pay income tax sets in. ... For higher incomes ranging from € 22,400 – € 28,000 per year, the marginal tax rate then stands at more than 95 %, because in addition to the withdrawal of housing benefits and supplementary child benefits, income tax also has to be paid. For gross incomes of about € 28,100, the upper threshold for supplementary child-benefit eligibility is exceeded, which is why this is suddenly

omitted, and the marginal tax rate again clearly exceeds the 100 % mark." (Peichl et.al, 2017b, p. 3 f.).

In the coalition of the Federal Government it is agreed to better combine the different instruments (child benefit, child allowance, advance payment of maintenance for children living in single parent families<sup>3</sup> and housing benefit) in order to better support families whose parents are employed but need supplementary assistance to cover the needs of their children (Koalitionsvertrag, 2018, lines 688–702).

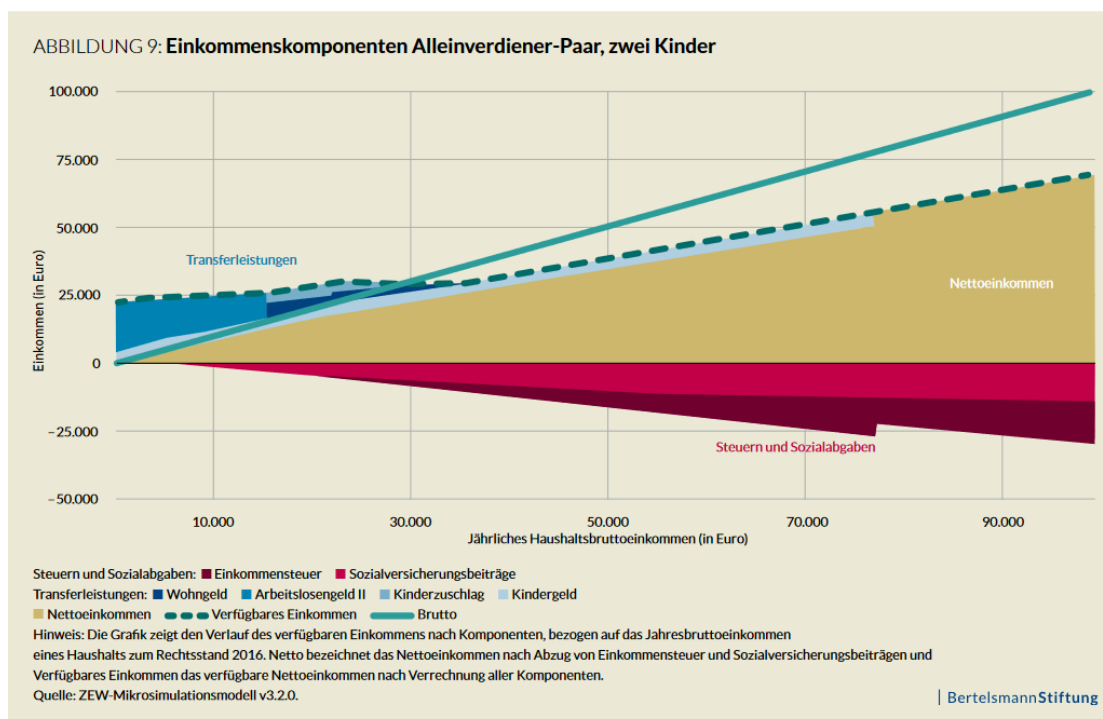
Figure 1. Progression of the effective marginal tax rate for a single earner couple with two children (Source: Peichl et. al., 2017a, p. 22 )



<sup>3</sup> Unterhaltsvorschuss



Figure 1. Income components for a single earner couple with two children<sup>4</sup>  
(Source: Peichl et. al., 2017b, p. 4.



## 5.5 Use of benefits for education and social participation not yet satisfactory

The use of the benefits for education and social participation by the families entitled for them is still not satisfactory; only about half of them use it, sometimes even very irregular. Many families are not or only insufficiently informed about the benefits. The intensity of use greatly depends on how effectively the programme is supported by local authorities, schools and other educational institutions. It is proposed to simplify the application process considerably and to intensify counselling (SOFI & IAB 2016). In their coalition agreement the political parties forming the present Federal Government agreed to reform the benefits for education and social participation. It is agreed in future to grant allowances for school lunches and school transport without raising a parental contribution (Koalitionsvertrag 2018, lines 720–728). This may make it possible for schools to be directly supported to cover these costs, to avoid detailed applications and to reach more children than today.

## 5.6 Low wage employment, pensions and basic income support

Employees who have been working full-time at minimum wage level throughout their working lives need supplementary *Basic Income Support in Old Age* if they do not live together with a better-off partner or have access to other income or assets. The *Basic Income Support in Old Age* is needs-tested; the statutory pension is credited in full. The supplementary *Basic Income Support in Old Age* covers exactly the difference between the pension received and the minimum income level. The person who is

<sup>4</sup>Tax and social contributions: Dark red: income tax; red: social security contributions; dark blue: housing allowance; blue: unemployment benefit II; light blue: child allowance; very light blue: child benefits; yellow: net income (employment); dotted green line: available income (including all social benefits), green line: gross income (employment).

dependent on supplementary assistance is not better off than if he or she had not worked.

A general increase in the pension level is of little use to the recipients of *Basic Income Support in Old Age*. The small effect results from the equivalence principle of old-age pension insurance. If there were an increase, the recipients of high pensions would receive significantly more, while people with low pension entitlements would only receive small surcharges. A few would be raised above the threshold of the socio-cultural subsistence minimum and the situation of those who live in hidden poverty, as they do not assert their claims, would also improve. Most of the current and future recipients of *Basic Income Support in Old Age* would continue to be dependent on supplementary aid.

This problem has been recognised by the political parties that form the government. Already in the last legislative period it was regulated by law that income from additional state-subsidised old-age provision ('Riester pension') and occupational pension schemes should not be fully credited.

The coalition agreement of the current government provides for a basic pension (*Grundrente*) to be paid to those receiving basic benefits and who have 35 years or more of pension insurance contributions (*Beitragszeiten*), periods of child-raising or nursing care. It should be 10 % higher than the *Basic Income Support in Old Age*. The rules on asset recognition are to be changed so that recipients of state aid can keep a self-occupied property.

## **6 Success factors and transferability**

It is a characteristic of the basic security system in Germany that there are **strict constitutional requirements** that bind the legislative authority and the administration. 'The principle of the social welfare state contained in Article 20.1 of the Basic Law, in turn grants to the legislature the mandate to ensure a subsistence minimum for all that is in line with human dignity, the legislature receiving a margin of appreciation in the unavoidable valuations linked to determining the amount of the subsistence minimum.' (Constitutional Court judgement of February 9, 2010, 133). Political decisions on the design of the minimum income system can be reviewed by the constitutional court; and in order to make this possible, the system must be set in a transparent procedure. As the Federal Constitutional Court says:

'The valuing decision as to what expenditure is counted among the subsistence minimum is to be taken by the legislature handing down the provision in an expedient, justifiable manner. Reductions in expenditure items in the divisions of the sample survey on income and expenditure require an empirical basis for their justification. The legislature may only regard expenditure which is made by the reference group as not relevant if it is certain that it is covered elsewhere or is not necessary to secure one's livelihood. ... To make it possible to examine whether the valuations and decisions taken by the legislature correspond to the constitutional guarantee of a subsistence minimum that is in line with human dignity, the legislature handing down the provision is subject to the obligation to reason them in a comprehensible manner; this is to be demanded above all if the legislature deviates from a method which it has selected itself.' (Constitutional Court judgment of 9 February 2010, 171).

The minimum income benefits system stands in the **tension between administrability and the requirement to do justice to individual cases**. Standard rates are calculated as lump sum (differentiated according to different groups of recipients), but additional benefits must be provided in special cases:

'The legislature may cover the typical needs to ensure a subsistence minimum that is in line with human dignity by means of a fixed monthly amount, but must grant an additional benefit for securing a special need beyond this which is irrefutable, recurrent and not merely a single instance.' (Constitutional Court judgment of 9 February 2010, Headnote 4).

Costs for housing and heating are usually reimbursed individually (if they are recognised as appropriate). This leads to a considerable administrative burden and also to court disputes about the appropriate amount in the individual case. But a system that works solely with lump sums would be far less fair.

There have been political efforts to improve the **fit between the minimum income system and the labour market**. Incentives to take up work are now higher than before labour market reforms in the mid-2000s. A system that guarantees the subsistence minimum in line with human dignity including the material prerequisites for a minimum of participation in society, combined with high withdrawal of transfers (high marginal 'tax' rates, see 5.4.) can lead to a low additional net income from employment, especially for people with low vocational qualifications working in the low-wage sector. This problem is particularly virulent for single earners who care for their partner and children. Lower transfer withdrawal rates would significantly expand the group of persons entitled to supplementary benefits.

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## 8 Appendix

### Basic Needs-Relevant Consumer Spending for a Single-Person Household (EVS 2103)

<b>EVS Section</b>	<b>Basic needs-relevant share in %</b>	<b>Basic-needs-relevant consumer spending in €</b>
Food, non-alcoholic beverages, [tobacco] (01 and 02)	No tobacco, substitution of alcoholic beverages by mineral water, remaining categories: 100%	137.66
Clothing, shoes (03)	Dry cleaning excluded, other items: 100%	34.60
Housing, utilities and home maintenance (04)	Without rent as rents are covered separately; special assessment for electricity; other items: 100%	35.01
Furniture and fixtures, household appliances and other items (05)	100%	24.34
Health care (06)	Some expenses are not considered as recipients are eligible for reimbursement; other items: 100%	15.00
Transport (07)	Expenditure for cars and motorbikes excluded, special assessment of mobility costs based on households with no car to cover higher costs for public transport. Employed EB II-recipients who need a car to reach their working place are entitled to deduct costs from the income to be taken into account.	32.90
Communication (08)	The average costs of households with a landline (or mobile) network connection and internet are included.	35.31
Recreation, entertainment, culture (09)	Excluded are gardening, camping, cut flowers and indoor plants, pets. Excluded are radio and television fees, as the aid recipients are exempt. All other items: 100%	37.88
Education (10)	Included are courses (e.g. adult education) outside formal education.	1.01

Hotel services, restaurants (11)	Overnight stays are excluded as holiday trips are considered as non-basic-needs relevant. 34.1 % of the costs of food and drinks consumed in restaurants are considered (pure input costs of the consumed goods without service).	9.82
Services of any kind (12)	100%	31.31

