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Uwe Fachinger

**New Forms of Employment and the Social Security System:
The Case of Germany**

IMPRESSUM

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ZUSAMMENFASSUNG

Ziel des Beitrags ist die Analyse der sich ändernden Arbeitsmarktstruktur auf das soziale Sicherungssystem. Es wird aufgezeigt, dass die Restrukturierung des Arbeitsmarktes eine große Herausforderung für die Sozialpolitik darstellt und erheblich stärkere Wirkungen auf das soziale Sicherungssystem haben wird als die demographischen Veränderungen.

Zahlreiche neue Erwerbstätigkeitsformen sind durch den Prozeß der Tertiarisierung entstanden. Darüber hinaus wurde diese Entwicklung politisch unterstützt und finanziell gefördert. Allerdings bedingen diese neuen Formen der Erwerbstätigkeit spezifische Risiken. Aus individueller Sicht entsteht das Problem einer nicht ausreichenden Absicherung gegenüber den finanziellen Folgen des Eintritts von sozialen Risiken (z. B. Arbeitslosigkeit, Invalidität, Krankheit oder der Möglichkeit für eine adäquate Alterssicherung) innerhalb des sozialen Sicherungssystems. Aus institutioneller Sicht wird die finanzielle Basis des Systems der sozialen Sicherung geschwächt, da sich mit der sukzessiven Reduzierung der Anzahl der Pflichtversicherten zwangsläufig auch die Einnahmen der Institutionen verringern.

Als ein vorläufiges Ergebnis der Analyse kann festgehalten werden, dass – falls sich die Entwicklung weiter fortsetzt – nicht die erwarteten Auswirkungen des demographischen Wandels das gravierende Problem darstellen. Vielmehr ist die zunehmende Anzahl an Personen problematisch, die über eine nur geringe Absicherung gegenüber den materiellen Folgen des Eintritts sozialer Risiken verfügen und damit auf die armutsvermeidenden Leistungen des sozialen Systems angewiesen sein werden.

ABSTRACT

The aim of the study is to analyse the consequences of the changing structure of the labour market for the social security system. It will be shown that in the future the restructuring of the labour force will yield a main challenge for social policy and will have much bigger consequences for the social security system than the demographic changes.

Numerous new forms of employment were caused by the economic process of tertiarization. Furthermore, these kinds of employment were politically demanded and financially supported. However, those forms of employment have their shortcomings. From an individualistic point of view there is a shortage in the protection against the financial consequences of social risks (e.g. unemployment, invalidity, illness, or the possibility to save for an adequate pension) within the social security system. From an institutionalistic point of view the financial basis of the social security systems becomes weaker and weaker as the

reduction of the number of employees with a compulsory membership within the social security systems will inevitably reduce the contribution revenue of the institutions.

As a preliminary conclusion it may be said that if the development continues we will not be confronted with the expected costs of the demographic changes but with a growing number of people with no or a low coverage against social risks. These people will depend on a basic system of poverty prevention.

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1 Introduction

Over the last years many new forms of employment emerged – often seen within the context of the development of the so called new economy. This however is the result of two different processes: 1. the tertiarization of the economy and 2. political decisions. Therefore, the increase in new forms of employment is not a consequence of a law of nature - it is the result of conscious political influence on the economy to reduce state expenditures and wage costs of firms. In addition the demand side of the labour market took advantage of the liberalisation fostering the structural change.

The causes for the numerous measures in economic policy, fiscal policy, social policy, or labour market policy are the alleged or real economic shortfalls. The following aspects belong to these shortcomings

- Too low economic development,
- Lack of international competitiveness,
- Missing innovations,
- Insufficient modernisation of the economy and
- Too high unemployment rate

Remarkable social and distributional aspects are virtually missing. This is symptomatic for the agenda of political actors, where distributional effects – with the exception of the catchword “generational equity” – are at least officially ignored. Therefore it is no wonder that many aspects of social security which are strongly connected with the above listed points are not taken into account.

For example if looking at the measures to reduce the unemployment rate, the lack in comprehensive view and the ignorance of the interdependence of the social security systems becomes obvious. Within the scope of reshaping the economy to redress the mentioned shortcomings the new forms of employment did not reduce unemployment or support the increase of employment as expected, but instead existing forms of employment were often substituted. This is especially to be seen in the decrease of employees with compulsory insurance in the social security system and in the increase of self-employed people¹. As a result forms of employment have arisen over the last years, which mean special challenges for the social security systems.

¹ See for example Bögenhold and Fachinger, 2007.

2 Structural changes of employment

The change in employment forms and statuses, which in a welfare state supposed to be long since gone, affects dependent workers as well as self-employed people. In the field of dependent employment, the following occupations belong to the new forms: Employees with contracts for work, subcontracted workers, temporary workers, low income jobs, mini-jobs, midi-jobs, low paid jobs, 1 Euro jobs, full time low income jobs, marginal employed people, occupation with partial retirement, capacity oriented working time, job sharing, part-time employees, short term occupations, disguised employment.

These terms are not clearly defined and not differentiated from each other. It is a bundle of more or less appropriate characterizations, which are used within scientific discussions, in laws, and reports, and the contents are partially overlapping. So sometimes the amount of earnings, the working hours, or the legal form of employment are used for differentiation. Regarding this confusion of tongues as an expression of the heterogeneity of employment, a categorization and systematization according to distributional criteria is necessary.

Concerning the increase of self-employment, the terms, which are used in literature, are also heterogeneous. However in principle they refer to three forms of self-employment: self-employed people with and without employees, and employed people, which are additionally self-employed as a secondary activity. As expression for the first category the following terms are coined:

Solo self-employed, sole entrepreneur, one person entrepreneur, firms without employees, one-man start ups (Ich-AG), family start ups (Familien-AG), founder of a new business, freelancers.

The development of those kind of employment stem from effects, which are the consequence of two targets of economic policy. In principle the measures should produce two outcomes:

1. Reduction of unemployment and increase of employment respectively through a so called transition to a flexible labour market.
2. Promotion of self-employment to support general economic growth, to obtain an increase in welfare, and to survive the international competition on the basis of innovations.

3 Development of employment since the 1990s

To get an idea about the amount of labour market changes, some statistics are presented in the following. It will be shown that an ever-increasing circle is carrying out those as new characterized forms of employment.

3.1 Employees

A particularly striking development over the last years occurred for the employees, which are liable for social insurance. Between 1992 and 2006 a reduction in the absolute numbers of about 11 percent took place. Also the quota with respect to all employed people dropped down by approximately 13 percent from 77.1 to 67.4.

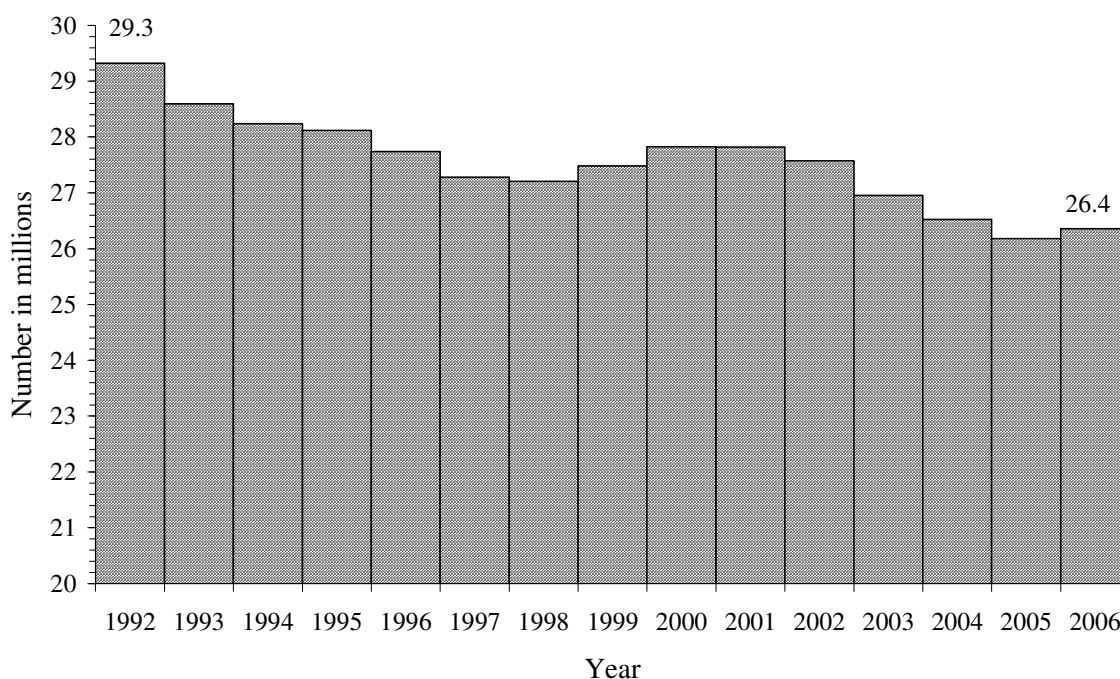


Figure 1. Compulsory Insured Employees in Millions

Source: Bundesagentur für Arbeit, Beschäftigungsstatistik.

The number and share of employed people which are not compulsory liable for social insurance and which are therefore without any direct protection of the social security system mirror imaged the decline. The absolute number increased around 46 percent from 8.7 to 12.8 million. As a result today approximately 32.6 percent of all employed people in Germany are not integrated in the social security system.

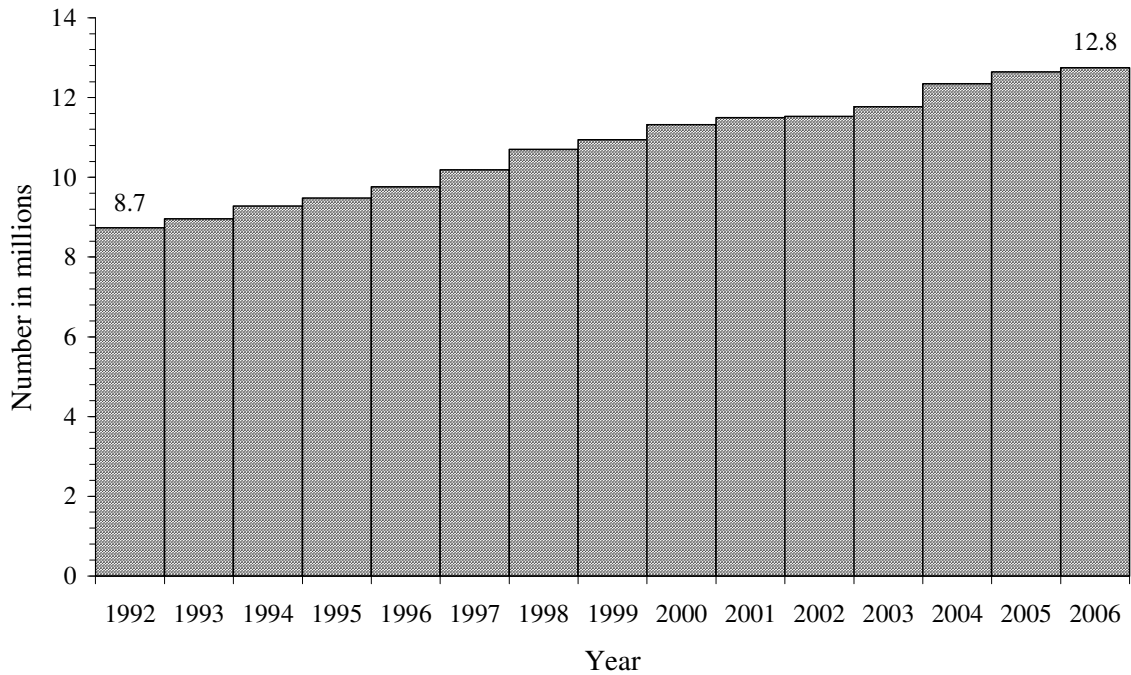
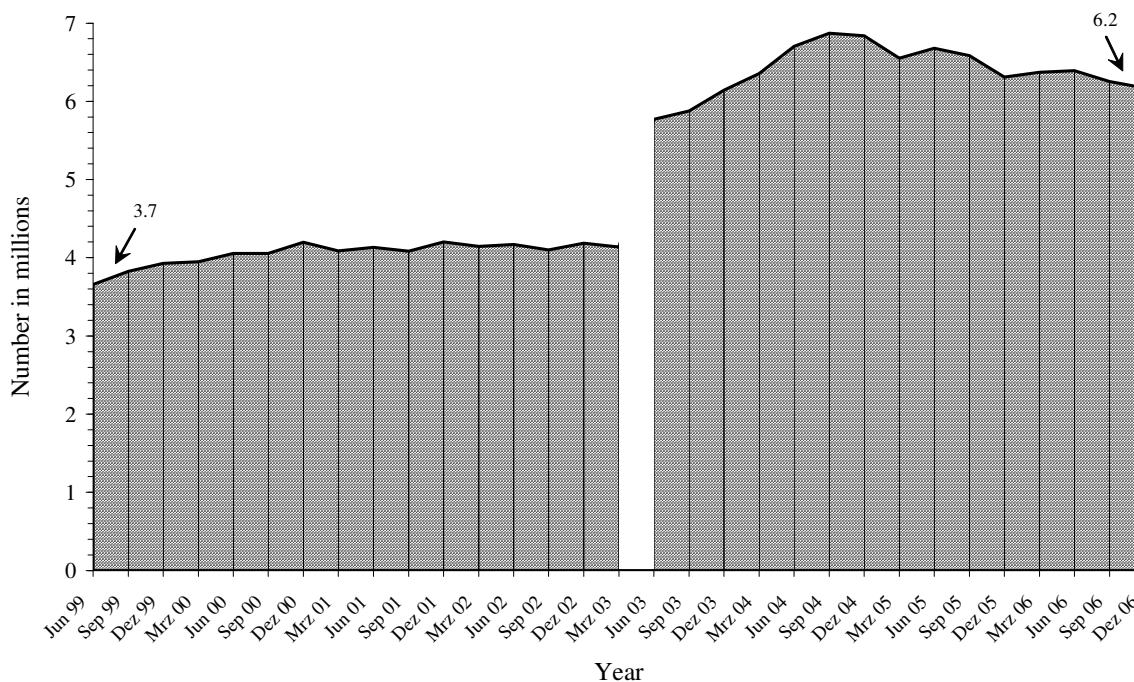


Figure 2. Not Compulsory Insured Employees in Millions

Source: Bundesagentur für Arbeit, Beschäftigungsstatistik.

Not only is the general coverage by the social security system relevant but also the extent of insurance. This holds true because of the equivalence of transfers for income replacement, if a social risk occurs. So low income e.g. because of part-time work determines low transfers from the statutory pension system (GRV) or from the unemployment insurance. To form a picture of the amount of those people the following figure shows the development since the end of the 1990s.



Note: Because of the Zweite Gesetz für moderne Dienstleistungen am Arbeitsmarkt from 23th of December 2002 (BGBl I, S. 4621) the registration system of marginal employed people was changed with effect from 1. April 2003.

Figure 3. Marginal Employed People in Germany in Millions

Source: Various reports of Deutsche Rentenversicherung Knappschaft–Bahn–See/Minijob-Zentrale.

3.2 Self-employed people

Economic policy representatives gave much hope to the idea of self-employed people solving the above mentioned economic problems. To what extent the specific measures have increased self-employment is difficult to judge. However, over the last 15 years an increase of self-employment in both the absolute number and the quota took place.

This development is accompanied by structural changes within the group of self-employed. As can be seen in the following figure, the increase since the middle of 1990s is almost solely marked by the self-employed people without employees whereas the share of self-employed with employees remained roughly the same.



Figure 4. Self-employed People in Germany in Percent of the Labour Force

Source: Own calculations on the basis of the scientific use files of the microcensus of the Federal Statistical Office Germany.

The development was very heterogeneous between and within the economic sectors. Where a reduction took place in the agricultural sector, a noticeable increase occurs especially in the building and the service sector.

Within the scope of the structural changes in employment, new forms of employment took shape regarding the self-employed people in particular. Beside the classical forms of workmen, farmers, journalists, artists, or free professions, meanwhile a great variety of freelancers exists. The majority of freelancers are located within the service sector with an emphasis in the field of consultation, care, I & T, and advertising.

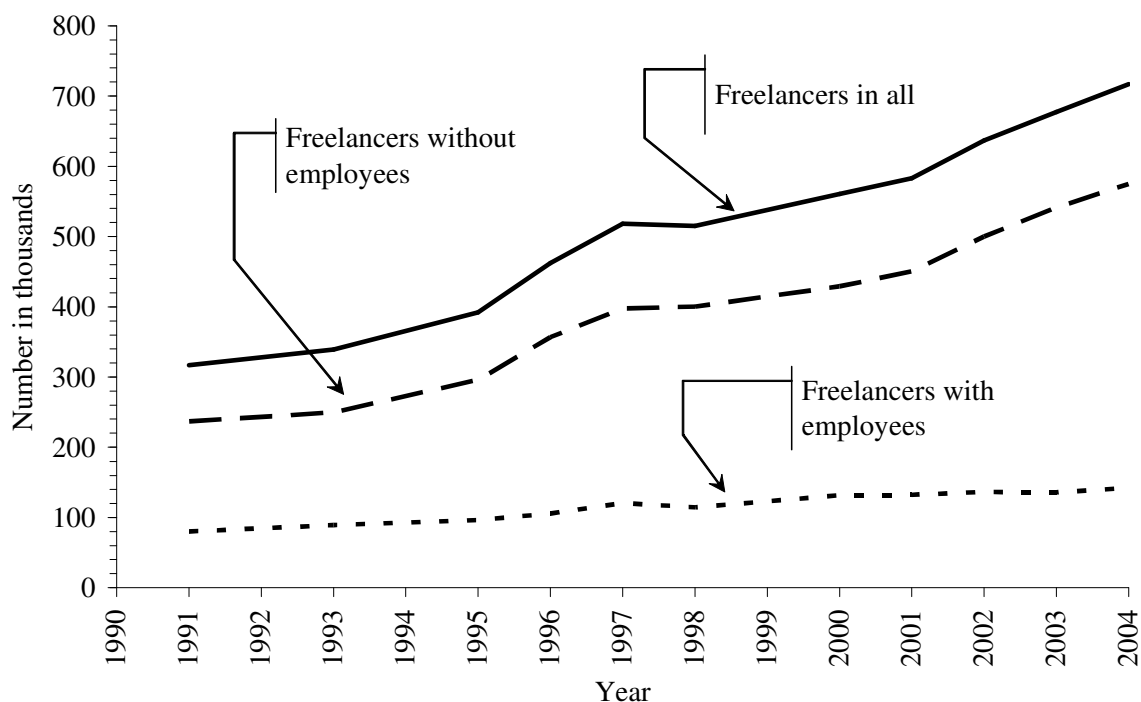


Figure 5. Freelancers in Germany in Thousands

Source: Own calculations on the basis of the scientific use files of the microcensus of the Federal Statistical Office Germany.

At the beginning of the 1990s the number of freelancers without employees was already three times higher than the one of those with employees. However until 2004 the proportion got even worse. In more than 80 percent of the cases a free profession is carried out by self-employed people without further personnel assistance. As the freelancers form about 20 percent of all self-employed people in Germany, this is one reason for the general increase of self-employed people without employees.

Some essential aspects of the structural changes in employment are characterized by these few but striking information. It should be emphasized once more, that this is not a side issue of the economic development but the dynamic changing structure is of quantitatively considerable importance as the following numbers impressively substantiate:

- Between 1992 and 2006 an increase of about 4 million employed people without any insurance in the social security system up to 12.8 million took place.
- 4.5 million people carried out part time work in 2006.
- 6.3 million people were marginal employed in 2006.
- Approximately 4 million self-employed people existed of whom around 2/3 were solo self-employed in 2004.

In principle the structural changes in employment are characterised by

- an increase in people without or with a reduced protection against the material consequences of the occurrence of any social risk (e.g. unemployment, invalidity, illness, or the possibility to save for an adequate pension)
- an increase in people, who have low income on average.

Over the last couple of years employment statuses increased which are potentially problematic from a social and distributional point of view. However it is not clear how far this will actually be true mainly because there is a lack of information on the household situation these people live in. This is important because labour supply decisions are made in the household context. So it might be the case that a household member already is member of the social security system and therefore additional protection is not necessary – especially in systems which provide transfers in kind.

Even the short characterisation above shows, that the massive reshaping and the structural changes of the employment forms mean a great challenge for the social security systems and define a variform field of research.

4 Implications for social security

The effects of the structural changes of employment comprise the whole social and distributional policy. This requires a comprehensive, all systems overlapping approach of analysis. Without such a view, the interdependence of the social security systems – especially its financial intertwining – can not be taken into account. An isolated analysis of single elements of the system – such as GRV or the insurance against the financial risks of unemployment – would come too short.

To analyse the massive effects on the social security system, which the structural changes cause, a categorization in institutions and households or individuals suggests itself as a first step. From an individual point of view, the new forms of employment often lack elements of insurance against the financial consequences of the incidence of social risks. From an institutional point of view, the financial basis of the social insurance system gets weaker step by step.

4.1 Institutional aspects

The structural changes – reduction of the number of employees and the reduction of the basis of assessment as a result e.g. of part time work, mini-, and midi-jobs – cause lower revenues. The problem especially in a pay-as-you-go (contribution or tax) financed system is the reduction of employment, that not necessarily goes hand in hand with the reduction of transfers. This would only be the case if people leave the social security system or lose their entitlements completely. However this is not always the case and differs be-

tween the social security systems. To analyze the effects it is therefore necessary to differentiate between the systems.

Related to the GRV the changes of employment between 1992 and 2006 from 29.3 to 26.4 million mean a reduction of around 11 percent. As a rule of thumb, the change of 100,000 people results in an increase or decrease of revenues of about 500 million Euros. Therefore the reduction of employed people leads to a decrease of about 15 billion Euros in 2006 compared to 1992².

To get an idea of the magnitude of the 15 billion Euros it should be emphasized that this is about 9 percent of the total revenues of the GRV in the year 2004³. A variation in the contribution rate of 1 percentage point results in around 8.8 billion Euros of more or less revenues. Would the number of employees be held constant over time, the contribution rate of the GRV would be *ceteris paribus* around 1.7 percentage points lower.

However it has to be kept in mind that the lower numbers of people with coverage in the GRV lead not only to a loss in revenues but those people also are no longer able to accumulate entitlements. Therefore the total expenditures *ceteris paribus* will be lower in the future.

Compared to the GRV the connection between expenditures and revenues in the unemployment insurance system is more direct. As a voluntary insurance is not possible in the unemployment security system the revenues but also – after a time of transition – the entitlements will decrease.

Such equivalence between benefits and contributions (give and take) as in the GRV or unemployment insurance – which has been undermined with the new legislation since 2000⁴ – does not exist in all social security systems, especially if the systems provide transfers in kind instead of transfers in cash. This issue will be addressed exemplarily on the basis of the statutory health insurance (GKV).

It has to be considered for the GKV that the insurance coverage may continue even after the end of an employment, as it is possible for example to voluntarily maintain the insurance. The contributions are income related as a rule, but the transfers are independent of the contributions. As far as the income in the new job is lower than that during the previous employment, the revenues of the security system therefore will also be lower with-

² It is assumed that the previously compulsory insured people did not choose reinstatement within the GRV.

³ In the year 2004 the revenues were about 169.4 billion Euros; VDR, 2004: 3.

⁴ See e. g. Schmähl (2007b) or Ginn *et al.*, 2007.

out lower transfers in kind. As a result, this leads inevitable to financial problems, which among other things could be solved by reducing the benefit level or by raising the contribution rate.

However not only the reduction of employment or leaving of the social security system yields problems with respect to the financing but also the reduction of the contribution paid by the insured people because of the partly or complete exemption of contribution for special forms of employment – deferred compensation for pension within the scope of occupational pensions is part of that⁵.

Additionally the financial intertwining between the social security systems among each other and to other public budgets is not without its problems⁶. In the past easing the burden of public budget took place at the expense of the social security system⁷. An example is the accompanying budget law of 2006. In this the contributions of recipients of unemployment benefits II were reduced from 75 Euros per month to 40 Euros per month. To compensate the loss in contributions in the GRV the rate of contribution had to be raised for 0.2 percentage points.

Furthermore it has to be considered that if individuals are no longer covered by the social security system the last net of security – the income tested social assistance – is responsible.

Today there exists an institutional intertwining of financing and benefits, which in its actual dimension is unknown. This situation was deliberately caused by the politicians. It enables to use the social security system as “shunting station” and to use them to under-cover easing of the burden of the national budget. Up to now the multiple cohesions of the effects were seldom topics of social and distributional analysis.

4.2 Individual aspects

From a social political view the new forms of employment are a problem, if the people are not at all or only marginal insured against the material consequences of the occurrence of social risks. The taking up of self-employment following an education or the change of employment can lead to the loss of security against social risks.

⁵ See e.g. Schmähl, 2007a.

⁶ See for an in-depth study of the German system Henke and Schmähl, 2001.

⁷ A striking example is the introduction of the long term care insurance in 1995/1996 and since 1989 a large part of the financial burden on the so-called re-unification has to be carried by the social insurance system or rather by the employees who are paying the social security contributions.

This can be exemplified with the statutory pension insurance GRV. If people leave the GRV they are not only longer able to achieve further entitlements for a pension but they also lose entitlements in the case of invalidity or benefits for rehabilitation.

Hereby loopholes in the social protection arise, which can not be filled by a private insurance. Reasons for that are

1. the non-existence of an insurance – like against unemployment or a drop in orders,
2. risk selection by the private insurer
3. with increasing age of entry the contributions are also increased, i. e. the older a person, the higher the contribution.

The financing of private insurance is carried out by so called premiums, which has to be paid by each person⁸ and is independent of the economic situation and of the secured income. That implies that the relative income burden is regressive and that it is the more, the lower the income is. The following figure shows the problem exemplified by the GRV.

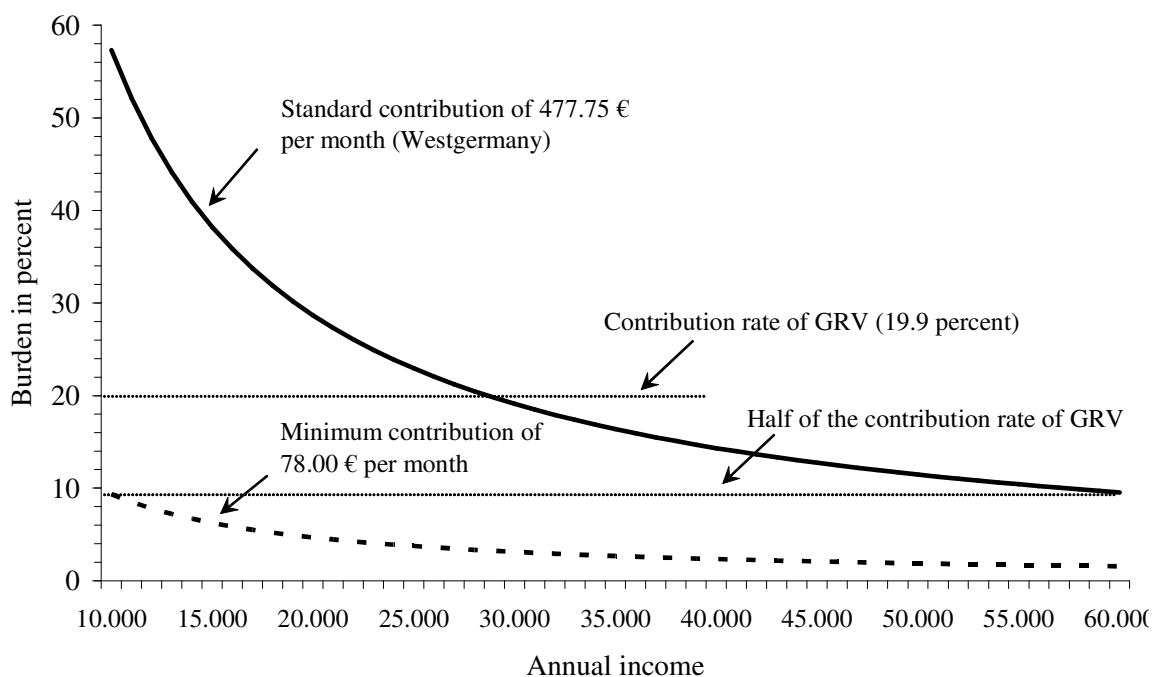


Figure 6. Burden of Different Contributions

Source: Own calculations.

⁸ In private insurance, there exists no free family membership.

The minimum contribution of 78 Euro comes to a monthly pension of 4.27 Euro. After 45 years of payment of contributions the monthly pension is about 192 Euro and therefore much lower than the level of the means-tested social assistance⁹. Even if the person pays contribution of half of the so-called standard contribution (Regelbeitrag) of about 239 Euro per month, the monthly pension will be lower than 600 Euro after 45 years of payment.

This illustrates a further problem: From an individual point of view it does not make sense to pay contributions if the potential entitlements are lower than the level of social assistance. It is to be assumed that with a low level of financial security or with low equivalence between contributions and benefits the resistance against contributions will be relatively high and a protection will be purposefully avoided. This behaviour is boosted by the discussion about social security and the conversion of the welfare state towards a basic system with means tested benefits¹⁰.

Therefore this is not only about people, who are not covered by the measures of the system, but explicitly about people, which are not able to meet the legal obligation. The conversion of the social security system with respect to disguised employment has clearly shown that a legal obligation is by no means sufficient, to identify all employees. Numerous self employed people, which are liable to insurance according to article 2 of the social code VI, did not satisfy laws and regulations – the same is true for artists and journalists¹¹.

Basically problems of social security arise from

- lack of willingness to save and
- lack of ability to save for financial security.

Whereas the low incomes of the new forms of employment affect the ability to save, the willingness to save is spoiled by the way of the discussion about the social security system and by the mass media propagating one nightmare scenario after another with public appeal. Public opinion polls meanwhile indicate a considerable loss of confidence in the social security system.

5 Some concluding remarks

On one hand the structural changes are the result of the tertiarization of the economy and of the developing service oriented society. However on the other hand, the process

⁹ Which is 345 Euro per month; article 20 of the Social Code II.

¹⁰ See e.g. Ginn *et al.*, 2007.

¹¹ See Fachinger *et al.*, 2004.

was caused by extensive economic, fiscal, labour market and social policy measures to promote the general economic development, to reduce the unemployment rate, and to an early adaptation of the demographic change. Furthermore, the measures serve to reduce the public expenditure and to provide firms with low cost employees. This was supported by the argument of the alleged overpriced non-wage labour costs¹² and the demand for maintenance respectively restoration of the international competitiveness.

Among all this, the social-political consequences were more or less disregarded. Once more it is a policy, which neglects the interdependence of the systems – the fiscal and social security system are among those – and where the distributional effects are not taken into account. An isolated consideration normally will lead to unintended effects of the measures at the risk of thwarting the expected results at least partially¹³. Within the scope of reshaping the economy the new forms of employment did not reduce unemployment or support the increase of employment as expected, but instead existing forms of employment were often substituted.

The reduction of the non-wage labour costs and of the public expenditures in principle took place by passing on the financial burden of protection against the occurrence of social risks to private households – and for those it results in an additional increase of the burden. Within the derivation of the positive economic effects it was assumed that private households would not substitute or shift the burden, but – if anything – compensation was supposed¹⁴.

If the structural changes continue any further we will not be confronted with the expected costs of the demographic changes but by a growing number of people with no or a

¹² In the public discussion only the absolute and percentual burden of employers was taken into account and other factors such as the productivity of the employees were totally disregarded.

¹³ Over the last decades this policy was characteristic for the GRV, which was extremely reduced viewed only as a pure individualistic old age security system – neglecting all the other social risks, which are also covered by the GRV, e.g. rehabilitation, invalidity, provision for dependants.

¹⁴ A noteworthy example is the assumption that private households will voluntarily save 4 percent of their gross earnings to compensate for the reduction of the proficiency level of the GRV up to the year 2020. The possibility of substitution or passing on the burden was barely discussed. However it is a mystery why households should react with higher savings to hold their alleged benefit level constant at the beginning of the retirement phase. Only the overall replacement rate – calculated as the relation of the average of the last earnings and the average of the first pension – was taken into account. The adjustment of pensions during the retirement phase was totally neglected. Before the pension reforms since 2000 the pre-calculated contribution rate of 22 percent in 2020 would have been paid by the employers and employees one half each. In contrast now the calculated burden in the year 2020 will be 11 percent for employers and employees and additional 4 percent for the private households. Therefore, an easing of the burden of employers of around 8.3 percent and an increase for private households of 25 percent will take place; see for further considerations Schmähl, 2004.

low coverage against social risks, which was intentionally forced by political measures. These people depend on a basic system to prevent a live underneath the poverty line.

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