The Governance of Supplementary Pensions in Germany: Changing Pension Mix and Coordinated Market Economy

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Abstract:

Recent reforms in Germany cut back state pension benefits and, along with European Directives, fostered the role of the second and third pillar. In order to maintain adequate retirement income occupational and private pension savings are necessary. The impact of changes in the public-private mix depends not merely on the share of private pensions but on the design of supplementary pensions. Decentralisation does not automatically lead to deregulation, rather organized decentralisation (collective regulation) and (state) re-regulation dominates the German supplementary pension landscape. Focusing on the role of the state and social partners in the governance of private and occupational pensions the paper analyses the increasing regulation due to social exclusion tendencies and financial risks. Here it is expected that the more publicly mandated or collectively regulated supplementary pensions are the larger will be their coverage, generosity, redistribution potential and financial regulation.
Additionally, the development and governance of supplementary pensions will be considered from the Varieties of Capitalism perspective, which expects effects on the coordinated market economy.

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Introduction:

Germany has been a paradigm for Bismarckian social insurance system and coordinated market economy, crowding out supplementary pensions without special needs for regulating private welfare provision. A growth to its limits, the rise of unemployment and passive labour market policies, social transfers to East-Germany due to unification and demographic challenges imposed increasing pressures upon the German conservative welfare state. In a first step the paper highlights welfare regime theories, followed by a more intensive focus on the social partners and complementarities according to the Varieties of Capitalism approach.

The second section pays attention to recent pension reforms in Germany which cut back state pension benefits and, along with European Directives, fostered the role of the second and third pillar. In order to maintain adequate retirement income occupational and private pension savings are necessary. The impact of changes in the public-private mix depends not merely on the share of private pensions but on the design of supplementary pensions, which will be described in the next section. The term "supplementary pension" is used for occupational pensions in the private and public sector and the so-called *Riester*-[1] and *Rürup*-[2]pension plans.

Decentralisation does not automatically lead to deregulation, rather organized decentralisation (collective regulation) and (state) re-regulation dominates the German supplementary pension landscape.

Focusing on the role of the state and social partners in the governance of private and occupational pensions the paper analyses the increasing regulation due to social exclusion tendencies and financial risks is analysed. Here it is expected that the more publicly mandated or collectively regulated supplementary pensions are the larger will be their coverage, generosity, redistribution potential and financial regulation.

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[1] Walter Riester (SPD), Federal Minister for Labour and Social Affairs between 1998 and 2002

[2] Bert Rürup, chairman of the *Sozialbeirat*, of the *Sachverständigen Rat zur Begutachtung der gesamtwirtschaftlichen Lage* and of a consulting commission

Additionally, the development and governance of supplementary pensions will be considered from the Varieties of Capitalism perspective, which expects effects on the coordinated market economy.

Theoretical background

In the welfare regime literature Germany is characterized as a Bismarckian social insurance scheme or conservative welfare state that reinforces status differences. The choice between two different goals, poverty alleviation versus status maintenance, led to the post-war development of flat-rate basic pensions (Beveridge-type) or earnings-related insurance benefits (Bismarck-type) that left different developmental space for supplementary private pensions. Private occupational welfare was an important defining criterion of Esping-Andersen's influential welfare state typology (Esping-Andersen 1990). Past research considers Germany as a conservative welfare state and it is assumed that any transformation follows a regime-dependent logic. Changes can only take place within certain paths (Myles and Pierson 2001). The transformation of welfare states is explained by relative inert institutional complexes in which the pension system is only one, but fiscally important, welfare component. The 2001 and 2004 reforms caused significant changes in the German old-age security system for instance the increasing importance of the social partners in this field..

In the past high state pensions crowded-out supplementary pensions. There was no need for additional private pensions (except for high-income earner) (Øverbye 1992). In contrast, lower state pensions today will crowd-in supplementary pensions, compensating for the income gap left by reduced public pensions. The "hidden side" of the welfare state expands, often unnoticed (Howard 1997). The scope for public regulation and control of private pensions increased due to privatization (paradox of privatization) (Leisering 2007). This changing public-private mix will have important repercussions for old-age inequality, particular for lower income groups which are less covered by private pensions (Kangas and Palme 1991; Korpi and Palme 1998).

Taking only into account the state level by analyzing retrenchment of pension benefits and by analyzing the public-private mix past research failed to take a look at the social partners' level. Cooperative labour relations might sustain retrenchment policies by providing welfare through industrial agreements (delegation of state welfare to collective bargaining) and should be considered by welfare retrenchment as a factor on decision-making and as self-regulators (Ebbinghaus 2006; Trampusch 2006).

The main interest of governance-debates is the way in which collective behaviour is coordinated (Lütz 2006). Here, economic transactions are organised not only via the market but also via non-market structures. The welfare-regime and industrial relations approaches expect, in line with the Varieties of Capitalism approach, complementarities and an impact on other production spheres. Economic actions are social actions that take place within social contexts (embedded within institutional contexts) and maybe needs to be coordinated. The economic behaviour in coordinated market economies such as Germany is coordinated and regulated through non-market mechanisms. Several productions spheres like vocational training, corporate governance and industrial relations together build coherent and complementary subsystems which are an expression of a comparative advantage. The Varieties of Capitalism approach assumes that there are mainly two varieties of economy, the Coordinated Market Economy (CME), characterized by non-market coordination and collaborate relationship, and the Liberal Market Economy (LME) regulated by contracts and competitive market arrangements (Hall and Soskice 2001). Institutional choices and constellations in an economy reflect political coalitions and preferences of dominant blocs (unions, employer associations) (Amable 2003). The combination of Varieties of Capitalism and Welfare Regimes assumes affinities between the type of capitalism and welfare regime (Ebbinghaus and Manow 2001; Huber and Stephens 2001).

What happens in the course of reinforcing the expansion of markets? Changing corporate governance to shareholder value and shifts in production systems from internal labour markets to flexible ones will be a crucial variable affecting occupational pension commitments by firms (vice versa).

Actual controversies offer three perspectives: First, convergence of systems towards the liberal economy (Soederberg et al. 2005). A second strand assumes relative stable national institutions against the background of complementarities of production spheres so that one element cannot change without taking into consideration other spheres (divergence). There are path dependencies which hinder institutional changes. This means, that path dependent processes are characterized by self-energizing sequences of events (Pierson 2000). Changes are possible only through exogenous shocks. The third perspective accepts institutional changes, national economies become institutional hybrids (Ebbinghaus 2005; Streeck and Thelen 2005a). Significant changes and transformations can be caused by gradual and incremental processes.

The governance approach is useful to analyse path inertia or change of governance configurations particularly by including actor's behaviour. For the present paper only the state and social partners level matter. The relation between unions, employers, and the state is crucial for the characteristics of capitalism. The welfare state and the public-private mix of pensions are essential institutions of the political economy. It includes and impact on industrial relations, collective bargaining and the financial system (pension savings).

Why is the public-private mix and its governance important for a market economy? Here we should consider the role of financial markets: they channel household savings into investment in the productive sector. Two ways are possible, a) institutions (often banks) mediate aggregate savings and b) direct transfer from savers to investors via securities markets (Jackson and Deeg 2006: 13). The choice between banks or markets is influenced by state regulation. Top-income groups favour market-based systems due to a greater capacity to invest and countries with more income equality have higher levels of savings by middle-income groups (they are more supportive of bank-based systems) (Jackson and Deeg 2006: 14).

Regulation (*Steuerung*) is an action driven approach and governance is an institutionalist approach. Governance is defined as institutional arrangements in which actors act. The structure of regulations and their impact on individual actions is the focal point. The governance approach includes all kinds of collective, state and non-state regulation on different levels, political regulation with involvement of non-state and civil society actors. Here, it is not possible to distinguish between regulation-object and –subject because the concerned actors participate on decision-making and implementation processes (Mayntz 2004). Regulation or governance should not be restricted to market regulation rather the regulation of collective actions should be included.

Reforms in Germany (1990-2008)

Recent reforms changed the public-private mix of the primal statutory public pension system which was characterized by income replacement, representation of male breadwinner family model, parity financing, and self-administration. In the past the social partners shaped public social policy making due to their institutionalization in the self-administration and the principle of autonomous collective bargaining (*Tarifautonomie*) avoids direct state intervention.

The first pillar in Germany is a pay-as-you-go system, paid by pay-roll taxes of employers and employees pursueing the status-maintaining principle. In the following the paper goes not into public pension system details, the main focus lies on the second and third pillar. But reforms of the first pillar are important because reduced public benefits "crowded-in" supplementary pensions.

Employers' associations and financial market actors used the increasing labour costs to demand cut backs in public pension expenditures and to foster supplementary pensions.

In the 1990s parametric and incremental reforms decreased public pension benefits (without fostering private pension provision) at first based on compromises between government, the opposition and social partners (Busemeyer 2006: 413; Ruland 2007:

34; Schulze and Jochem 2007: 17). A worsening economic situation of many companies made an introduction of new and the expansion of existing occupational pensions less likely (Schmähl 1997: 111).

In the second half of the 1990s the consensus could not be maintained. A real welfare retrenchment achieved the 1997 reform by the Conservative-Liberal coalition. Especially the trade unions criticized the reduction via a "demographic factor", reducing the net replacement rate from 70% to 64%. The new red-green government, elected in 1998, abandoned the "demographic factor" and other retrenchment measures but somewhat later realized the gravity of financial and sustainability problems for the public old age security system (Leisering et al. 2002: 87; Schulze and Jochem 2007: 20f).

A first major shift in the public-private mix occurred with the reforms in 2001 and 2004 with an enhancement of supplementary pensions. With different strategies the government was able to overcome reform blockages and veto points. These reforms modified the public pension pillar decreased its benefits (*Nachhaltigkeitsfaktor*) and fostered occupational and private pensions in two ways: a new voluntary private pension (third pillar) the so-called "Riester-pension" with tax deductions and state subsidies was introduced and on the other side tax exemptions and social contributions freedom for occupational pension plans (second pillar) were made possible (see for the detailed policy-process: Busemeyer 2006; Schulze and Jochem 2007). Main goals of these measures were financial sustainability of the public budget (in line with Maastricht criteria) and a stimulation of financial markets, aims which are also part of the Open Method of Coordination (OMC) and some EU-Directives (Castellino and Fornero 2006; Haverland 2003; Haverland 2004; Hering 2006). Whereas the OMC recommendations focus mainly on the balance of public and private pillars, the European Union also takes direct responsibility in the regulation of supplementary pensions through directives regulating the private insurance market. Directive 98/49/EC guarantee the portability of acquired pension rights and the Pension Fund Directive 2003/41/EC established a European market for pension funds (cross-boarder administration, principles of investment). With respect to monitoring occupational pension's providers, the European Commission founded the Committee of European Insurance and Occupational Pension Supervisors (CEIOPS) and the European Insurance and Occupational Pensions Committee (EIOPC) for supervision the pension sector. The CEIOPS informs the EIPOC which advices the European Commission in questions of insurances, occupational pensions and details of Commission's draft proposals.

In order to maintain adequate retirement income in the future public pensions alone are not sufficient, occupational and private pension savings are also necessary (Schmähl 2004)[3]. Decreased public pension benefits "crowd-in" supplementary pensions. This privatization of public pensions does not automatically lead to deregulation, as already mentioned, rather organized decentralisation (collective regulation) and (state) re-regulation dominates the German supplementary pension landscape.

In this context the state and social partners' role shift from direct pension benefit providers to regulators (Leisering et al. 2002: 92). One can speak of a "social politicization of markets" through market regulations and of "socialization of social policy" in the sense that social policy stretch to further sectors (see therefore Leisering).

According to an institutional perspective (Streeck and Thelen 2005b) these reforms combine a strategy of institutional layering (new third pillar) and conversion. Institutional layering is obvious as the 2001 introduced Riester-pension docks at the public pillar. Conversion takes place by changes inside of occupational pension schemes: formally they remain in the old frame but with new aims and actors. Whereas in the past it was a topping-up for high-income earners and employer-only financed, today occupational pensions are necessary in order to maintain an adequate retirement income and they are financed jointly or employee-only with tax concessions.

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[3] See for the discussion whether private pensions substitute or supplement public pensions: (Berner 2006b)

Share of supplementary pensions

Benefits of occupational pensions for retired persons are on the same level since 1990, namely 0,8% of GDP, the same can be observed for benefits of supplementary pensions of public sector employees (0,4% of GDP). At the same time an increase of employees and employers contributions since 2000/2001 is obvious (see Table 1).

But especially since 2005 the rate of Riester-contracts is raising up to today nearly 11 million contracts. The coverage-rate of occupational pensions is also increasing to circa 19 million contracts, an effect not yet measurable in terms of benefits. Despite lower public pensions, retirees can hold their status maintenance, but only in combination with occupational and/ or private pensions.

Table 1 Benefits and financing of occupational pensions (in bn. EUR)

	benefits public pension	benefits occupational pensions (% GDP)	benefits supplementary pensions public sector employees (%GDP)	Occupational pensions			supplementary pensions public sector employees	
				employee contributions	employer contributions		employee contributions	employer contributions
					factual	supposed		
1985	96,2	6,4	4,3	0,4	1,7	11,1	0,0	3,1
1990	115,4	10 (0.8)	5,7 (0.4)	0,4	2,1	12,9	0,0	4,0
1995	203,5	14,6 (0.8)	6,6 (0.4)	0,5	2,3	14,8	-	5,2
2000	231,9	17,5 (0.8)	8,1 (0.4)	0,7	2,5	16,6	0,6	5,7
2003	252,0	18,7 (0.9)	8,7 (0.4)	1,6	5,4	23,5	0,7	7,2
2005	256,6	18,9 (0.8)	9,3 (0.4)	2,8	5,4	22,8	0,5	7,1

Sources: Statistical Yearbook different years (Statistisches Bundesamt), Sozialbudget 2006: Tabellenanhang S.10

A survey of *Deutsche Rentenversicherung Bund* (German Federal Pension Insurance) tried to simulate old-age income of certain cohorts[4] with different scenarios. A model with a more favourable labour market and with a higher retirement age states higher entitlements or less reduced entitlements of the net old-age income of the youngest

[4] Birth cohorts 1942-1961 (2002 at the age of 40 to 60)

cohort (1957-1961) compared to the net old-age income of the oldest cohort (1942-1946) (Deutsche Rentenversicherung Bund 2007: 268f). A second alternative model which includes the 2001 and 2004 reforms (including the changed pension adjustment formula) concludes that it depends on the coverage rate of Riester-contracts and their rates of return if the reduced public pension benefits can be compensated (Deutsche Rentenversicherung Bund 2007: 273). With the most optimistic simulation some cohorts can get higher old-age income with Riester-contracts and reduced public pension benefits (dependent of labour market development, coverage-rate and interest rate) than the oldest cohort (see Table 2). Male employees of the youngest cohort can reach the net old-age income of the oldest cohort only in the positive labour-market scenario with an interest rate of 5% and for West-Germany only with 100% Riester participation.

Even if supplementary pension coverage is relatively large, benefits have thus far been relatively unimportant except for top income groups. To counterbalance the decline in future statutory pension benefits due to recent cuts, coverage of both the new private pensions and occupational pensions will have to increase in the future combined with higher contributions.

Table 2 Simulation of net old-age income of the cohort 1957-1961 in % of net old-age income of the oldest cohort: 1942-1946

	Basis scenario Interest rate 2,75 %				Positive labour-market Interest rate 5 %			
	West-Germany		East-Germany		West-Germany		East-Germany	
	M	F	M	F	M	F	M	F
Standard-perspective	94	106	98	101	96	107	110	108
Participation Riester 50%	91	101	91	93	96	105	106	102
Participation Riester 100%	95	104	93	95	102	110	111	105

Source: (Deutsche Rentenversicherung Bund 2007: 274f)
Notes: M=male F=female

Role of the state and social partners

The social partners take an active part in the development and evolution of both statutory pension insurance and supplementary pensions through different channels and significantly to the formation of the old-age security system. It were not the financial actors alone who imposed their thinking on the supplementary pension, rather the rethinking of employers and unions was crucial. What capacities do trade unions and employers' associations have to influence the governance and design of supplementary pensions, particularly in policy-making and policy-implementation?[5]

On the one hand the development of the public-private mix was intended by state interventions (reforms), on the other hand unintended or absent state actions led to social partner self-regulation. We can distinguish between state regulations and (within this framework) social partners governance. This governance guides occupational pension policy decision-making especially since 2001 in order to pool risks and to give some incentives for private welfare. But we should keep in mind that there are also some EU-Directives which influence the governance of supplementary pensions. The present paper concentrates on supplementary pensions.

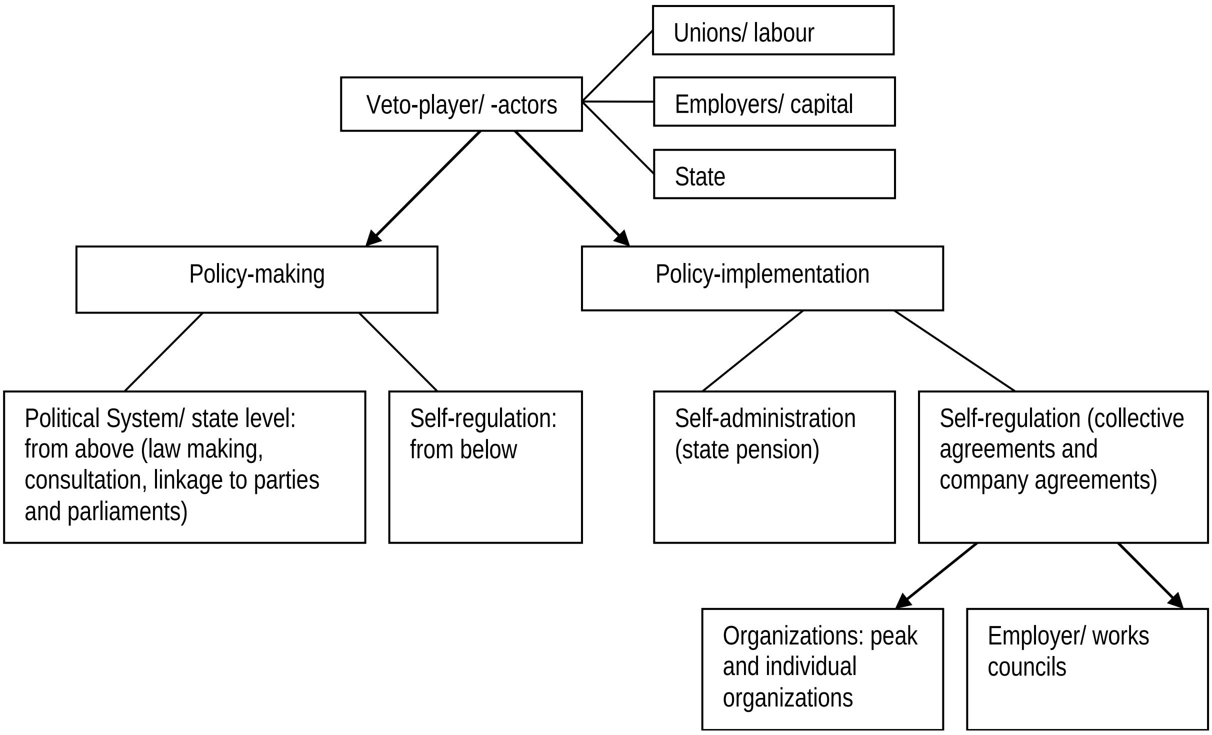
In the policy-making process social partners can take an active part via law-consultations, concertation and via members inside of different parties and parliaments (Trampusch 2004) so that we can speak of ideational or informal veto-player. They are important actors in reform processes in mature welfare states and preferences were shaped in part by the role of public pensions in the political economy (Anderson and Meyer 2003; Hegelich 2006: 556f). Actors' interest (state and non-state) become more important (Ebbinghaus 2006; Hegelich 2006).

Direct policy-making is possible by self regulation e.g. social partners can propose the federal Ministry of Labour and Social Affairs to extend existing collective agreements *erga omnes*.

[5] This papers ignores the weak scope of social partners for the self-administration of the public pension insurance (*GRV*)

On the side of policy-implementation the role of unions and employers' associations was reinforced through *Tarifvorbehalt*, which means that union wage can only be converted into an occupational scheme with the agreement of unions and employers' associations. On company-level, works councils and employers can negotiate for example the mode of occupational pension.

Figure 1 Role of the state and social partners



Until the 1990s occupational pensions were just a subordinated field of collective bargaining. Unions were more interested in wage increases and employer-only sponsored schemes made collective bargaining unnecessary. Furthermore the duration of an occupational scheme tops the usual duration of collective agreements irrespective that employers were not interested in agreed old-age security (Stiefermann 2003: 447f). A new interest for occupational pension schemes against the background of the legal claim to earning conversion had and has different reasons. The employer's interest is to find efficient and advantageous solutions with low administration costs, reducing wage costs and reinforcing the attractivity for potential members. The last point is one of the main reasons why unions agreed to the 2001 reform. But what can be done by collective agreements? They can govern conditions of earnings conversion, the level of entitlements by an early drop out and the adjustments of retirement benefits (Doetsch 2003: 57ff). Works councils have the right of codetermination in case of an absent collective agreement and absent state regulation. They can also specify and improve collective agreed regulations. Company agreements must be negotiated between the works council and the employer (Kemper 2003: 158ff). But generally, the 2001 introduced *Tarifvorbehalt* and the legal claim to earnings conversion shifted the scope for occupational pensions from the company level to the collective bargaining level and to the individual employee (see also Berner 2006a: 16). Especially the unions in the chemical and construction-industry (IG BCE and IG BAU) were forerunners of agreed occupational pensions, which also reflect different interests of different unions within the collective actor "labour".

Design of supplementary pensions: collective and state regulation

Whereas in the past occupational pensions have been voluntary commitments by employers in the private sector, public sector collective agreements concerning occupational pensions are mandatory for public sector employees since 1967 (BMAS 2006: 713-721). In Germany six modes of occupational pensions and two state supported personal pensions exist (see Table 3).

Who is covered and who benefits?

Nearly 70% of all employees (covered by mandatory social security contributions) are covered by occupational pensions. But this relatively large coverage rate comes along with relatively low average benefits. In the past mainly high skilled male employees in the private sector were covered (OPs as a human resource management method), whereas low income earners are also insured in the public sector due to the mandatory collective agreement.

Table 3 Overview supplementary pensions

Supplementary pension form	Coverage (Mio.)	Funding	Sponsor (contributions)	DB/DC	Tax deductions/ state subsidies	Liabilities (bn. EUR)	Limited investment	Insolvency insurance/ supervision
Direct pension commitment (*Direktzusage*)	4,9	internal/ book reserves	employer	DB	yes/ no	231,2	none (book reserves)	PSV/ none
Support fund (*Unterstützungskasse*)		internal	employer	DB	yes/ no	34,3	none	PSV/ none
Direct insurance (*Direktversicherung*)	4,2	external	employer &/ or employee	DC	yes/ possible	45,5	yes	conditional/ BaFin
Superannuation fund (*Pensionskasse*)	4,3	external	employer &/ or employee	DC	yes/ possible	89,4	yes	none/ BaFin
Pension fund (*Pensionsfond*, since 2002)	0,3	external	employer &/ or employee	DC	yes/ possible	1,2	marginal	PSV/ BaFin
Supplementary pension for public sector employees (*Zusatzversorgung Öffentlicher Dienst*)	5,3	PAYGO/ funded	employer and employee	DB, 2002: DC	yes	…	non (PAYGO)	State
Riester-pension	~11	external	individual	DC	yes/ yes	…	-	BaFin
Rürup-pension	0,6	external	individual	DC	yes/ no	…	-	BaFin

Notes: coverage includes multiple entitlements. PSV (*Pensionssicherungs-Verein auf Gegenseitigkeit*), BaFin (*Bundesanstalt für Finanzdienstleistungsaufsicht*)
Sources:(aba 2005; BMGS 2005a; Schwind 2007; TNS Infratest 2005; TNS Infratest 2007)

Since the 2001 reform all employees have the legal claim to convert a part of his/ her pre-tax earnings into a funded occupational scheme.

In the private sector about 1.2 million employees are covered by collective agreements that are mandatory through *erga omnes* extension by the Labour Ministry (e.g. construction and hotel and restaurant industry), together with the public sector nearly 24% of all statutory insured employees are mandatory covered (BMGS 2004).

The 2001 introduced pension fund is Europe-capable and can offer occupational pensions across national boundaries (Bruno-Latocha and Grütz 2001: 413).

Not everybody is entitled to sign a Riester-contract but all statutory insured and civil servants, that are about 35-40 million people. The sign up rates of Riester-contracts increased to nearly 11 million in 2007 (BMAS 2008), some reforms and less strict criterions since 2005 were responsible for this increase.

Approximately 31% of eligible persons have such a contract today, nevertheless the government's initial high expectations that 85% of the beneficiaries will receive state subsidies in 2008 did not materialize (Bundesregierung 2006).

Mainly self-employed, excluded from occupational pensions, are adressed by Rürup-plans. No state subsidies were paid but tax concessions schould animate them to close such contracts. Here again, some conditions have to be fulfilled for tax concessions.

What kind of benefits?

Occupational pensions can vary in the way in which benefits are financed and calculated. In the case of defined benefit (DB) pensions financed by PAYG-systems, the sponsors take on responsibility to guarantee supplementary income based on previous earnings (and contribution periods), while defined contribution (DC) pensions that are funded are determined by the returns on investment portfolio thus leaving the bad investment risk largely to the individual. A shift from DB to DC schemes is obvious (even in the public sector) due to the risk of stock market downturns and cost containment (Stevens et al. 2002:31) which could lead to lower benefits since it is the employee who bears the risk of stock-market downturns and lower rates of return. On the other side this offers the chance to get higher benefits and rates of return in times of prosperity. Most prominently are the changes of the public sector VBL scheme in 2002, it is based on a point system of contributions and years (a notional DC of 4% similar to the Riester-pension) (BMAS 2006: 715f).

The Riester and Rürup-pensions are examples for DC schemes as they are fully funded and benefits depend on contributions (equal for men and women) and the rate of return.

The indexation of benefits depends on the mode of occupational pensions, normally they should be adjusted according to consumer price index or increase at least by 1% per annum, except in cases of economic distress to the firm. However, not every scheme fulfils these obligations as employees are often unaware of their rights. Benefits from the public occupational scheme and from earnings conversion must increase at least by 1% per annum (Betriebsrentengesetz 2007). Like in all private pension plans no adjustments exist in the pay-out period of Riester- and Rürup-plans (Ehrentraut 2007: 587).

Occupational pension are by nature less redistributive then public schemes, nevertheless, there are some aspects in which intra- or intergenerational solidarity plays a role, often enforced by legal regulation. Unlike saving plans, which only focus on the saving process, most German OPs cover at least one of the risks (ex post balancing) of longevity, disability or survivor benefits. Furthermore, many OPs (only DB schemes) include some of the following elements of income redistribution (ex ante): no consideration of sex, state of health, age and marital status for the calculations of defined benefits. In contrast, redistribution plays no role in DC and employee-only financing schemes (BMGS 2004: 14), thus with a shift from DB to DC redistributive elements will disappear. The more generous public schemes include credits in case of incapacity, maternity protection and parental leave (BMAS 2006: 716f).

Portability of pension entitlements is given against the background of more flexible labour markets not only in Germany but also in Europe. Here, employer financed occupational pensions become vested after five years of service and the threshold age 30 (or rather 25 from 2009). Earnings conversion benefits are vested after the first paid contribution. For new contracts since 2005 employees are entitled to take the vested benefits along to the new employer when they change their job. These new rules help less skilled, temporary employees and women who often leave firms for child education. Contrary, benefits of public sector employees are only portable, if they are funded, but just a small part of employees is concerned since in West-Germany this scheme is PAYGO-financed (BMGS 2005a; BMGS 2005b). Particularly in the field of transferability we can find a conflict between employers, for whom higher portability means higher costs and makes occupational pensions less attractive, and social policy actors who wants to protect employees' benefits in times of reduced public pensions (see therefore long discussions about a European Portability Directive). In contrast, one can change the provider of a subsidized personal pension plans at any time and take one's savings along (BMGS 2005a: 51).

Who pays?

The employers finance the traditional modes direct pension commitment and support fund. These commitments (book reserves) are more and more seen as liabilities with an increased importance of shareholder value, so that new occupational pensions are jointly or employee-only financed. Therefore some employers have closed them for new entrants or closed them in case of merger or cessation (Ruppert 1997).

The employer pays four-fifth of the contributions to the occupational pension scheme in the public-sector, but in the private sector a shift from employer-only towards jointly-financed and employee-only financed schemes takes place (BMGS 2004). By earnings conversion in most cases the pensions are employee-only financed (Leiber 2005).

In 2008 occupational pension contributions are tax- and social-contribution free up to a certain ceiling, but taxes must be paid in the pay-out period.

In terms of financial regulation, the direct pension commitment and support fund are forms of reinvestment but have to be reinsured against the insolvency risk, while investment restrictions exist for superannuation funds and direct insurances because a higher percentage of stock market shares imply larger financial risks. International experiences (GB, USA) show that occupational pensions with a large percentage of stocks may lead to underfunding, resulting in higher investments in fixed interest securities (Jackson and Vitols 2001: 184), though an excess demand of fixed interest securities can in turn cause lower returns (Bundesverband deutscher Banken 2007: 18ff). Since foreign assets restrictions are an obstacle to the European Common Market, the European Directive 2003/41/EC allows pension funds more freedom to invest in foreign assets. The German reform of pension funds in 2002 and EU regulations to allow more investment in firms with registered offices in the European Economic Area foster German and European capital markets (BMGS 2002: 11).

Low income earners should profit from state subsidies for Riester-plans, high income earners are favoured by tax deductions. State subsidies include annual allowances per person and child credits. Contributions are tax-free up to 2.100 EUR per annum in 2008. To receive such subsidies certain criterions must be fulfilled (e.g. payments from a minimum age, consumer information and a minimum period of performance) (BMGS 2005b), which reflects the high state regulation of the third pillar. It is the individual who pays into a Rürup-plan, but the contributions can be paid very flexible (this maybe reflects the unsteady income of self-employed).

The subsidy for Riester-plans will not increase after 2008 (defined contribution ceiling of the year 2000), meanwhile the contribution ceiling for occupational pensions is linked to earnings development with the result that more money for old-age can be saved than in personal pensions. The forgone tax income through personal pensions amounts to 11 billion EURO per annum in 2008 (or 2% of tax revenue) (aba 2005: 15), together with the tax benefits for earnings conversion this

amounts to 13 billion EUR (or 0,6% of GDP). Moreover, public pensions will be automatically reduced if more and more people use earnings conversion and Riester-pensions, affecting also those persons who made no such savings.
The private pension regulation mirrors the German social policy tradition, namely the linkage of old-age and family-politics (child credits in Riester-plans).

Who decides and controls?

In Germany the employer decides whether or not to install an occupational pension and especially the form of the scheme. In some cases he is bound to a collective agreement. Generally, all employees have the legal claim to postulate an earnings conversion, but this right is limited because of *Tarifvorbehalt.* The role of social partners was reinforced due to *Tarifvorbehalt*. This means that an extra collective agreement is necessary to convert earnings which are an element of collective labour contractuals.
Direct pension commitments are governed by the management of the company and in case of codetermination with equal representation of employees. The beneficiaries of direct insurances have no influence over asset management. In contrast, the governance of pension funds is more complicated. Theoretically, employees can take part in decision-making in the board of trustees of pension funds via their representatives, but in reality the questions remains if this does matter. In addition, employees have rather different interest than one common interest. Some are more interested in high rates of return, others in social or ecological investments and others have further interests. The pension fund creates a multi-level principal agent problem. On the one side trustees are agents of the beneficiaries, the latter can delegate representatives to the boards and they get information on request (see for information rights BMGS 2004: 33). Information about the expected benefits and investment portfolio from supplementary pensions plays a key role for an adequate retirement income provision. Financial literacy is necessary in order to make well-informed choices between various available options. In the case of personal private

pensions clients have to be informed prior to the conclusion of a contract about e.g. administration costs, guaranteed benefits and portfolio-structure (ethnic, social and environmental issues) (BMGS 2005a). On the other side trustees are principals vis à vis the managers of the pension fund's portfolio.

Furthermore, every mode of occupational pension is supervised either by the Pension Protection Fund (Pensionssicherungsverein) by the Federal Financial Supervisory Authority (Bundesanstalt für Finanzdienstleistungsaufsicht) or both. BaFin is a federal institution formally independent but accountable to the Finance Ministry and financed by a levy on the supervised entities. The Finance Ministry has supervisory control via BaFin's administrative council and in exceptional cases can give ministerial instructions, while BaFin regularly consults the ministry concerning new regulations and guidelines (Pinheiro 2004: 43ff). The German bank supervision, the insurance control and supervisory agencies for securities trading were brought together to BaFin, who is amongst others responsible for the certification of Riester-products and regulation of the products and their marketing. For the non-funded OP schemes, insolvency protection is guaranteed by the Pension Protection Fund (PSV, founded 1974) which is a self-help institution of the German (and Luxembourg) pension schemes insuring 5.8 million employees and paying one million occupational pensions (TNS Infratest 2005: 20f). As a risk reinsurer, PSV continues to pay benefits if a company fails due to bankruptcy (aba 2005: 13), an important social protection function.

Even though regulations exist it is the individual who bears the risks of investments and inflation.

Selected collective agreements and pension funds (organized decentralization)

Self-administered institutions and collective agreements are instruments of the social partners to design and regulate occupational pensions. Given the negotiations between employer(s) and unions or workplace representatives, in particular the more symmetric power and information capacity between these collective actors, these agreements are broader in coverage and risk sharing than unilateral decisions by employers and individual employment contracts.

Especially in the metal, chemistry and hotel and catering industry collective sectoral pension schemes exist which manage broader investment portfolios and reduce administrative costs (Riedmüller and Willert 2007: 147). As already mentioned, in the construction, agriculture & forestry, hotel & restaurant and food industry collective agreements are extended *erga omnes* (BMGS 2004; 4, 21)

In some sectors/ industries legally independent institutions were founded by unions and employers associations where the social partners are members of the advisory board. For example, institutions like *Metallrente*, one of the earliest and largest schemes, are open for non-metal firms, too. Another advantage of such institutions is a broader investment portfolio and reduced administration costs. *Metallrente* is administered by the metal workers' union (IG Metall) and the respective employer organisation (Gesamtmetall). Management functions are outsourced to a consortium of financial service providers, while the social partners are on the advisory board (Karch 2002).

In the construction industry equally represented social security funds (*Sozialkassen*), an institution founded by the social partners, are a special case due to the character of this industry.[6] Since the 1950s all companies are bound to collective agreements and generally binding validity and in 2001 1.5 million employees converted earnings into this scheme. Since 2001 an agreed supplementary occupational pension is possible. In some cases early retirement before the age of 65 is possible (Laux 2001).[7]

Editors of newspapers and magazines pay 7,5% of their earnings into a pension institution (mandatory), whereas two-thirds are employer's contributions. This institution exists since 1926 (WSI 2001: 63). The heaviest regulated and negotiated collective scheme is the occupational pension scheme of public sector employees, based on mandatory collective agreements.

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[6] Risks characteristical for the construction industry like winter-unemployment are limited.

[7] The responsible union IGBAU says, that this is not the main aim of the collective agreement but just a secondary effect.

In contrast to personal pension, occupational pension when administered collectively shift responsibility from employees to collective interest representatives (employer associations and unions or works councils) that usually have more substantial information and financial expertise to make administrative and investment decisions than the ordinary employee or employer in a small firm.

Effects on the coordinated market economy

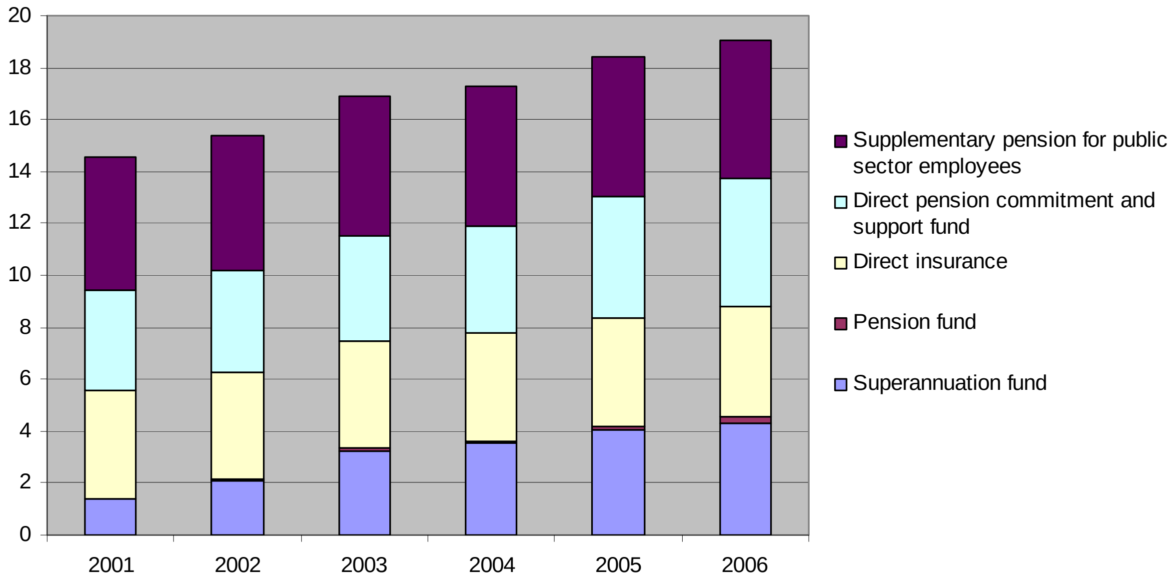
The assumption is that there is a relationship between market economy and pension system. Coordinated market economies (or bank-based) like Germany profit in the past from the bank-based system with less incentives to invest supplementary pension assets in stock markets (Jackson and Vitols 2001; Vitols 2003). With increased importance of shareholder value a reorientation occurred from defined benefit and book reserves towards defined contribution and funded pension (Jackson and Vitols 2001). Is there a transformation to a liberal market economy (securities-based) or does Germany continue as a CME? The Varieties of Capitalism are obvious in the case of supplementary pensions because they reflect the main characteristics of industrial relations, the states' role and the kind of governance.

An additional question could be, if the impact of pension funds on companies is "coordinated" or "liberal"?

Coordinated markets economies like Germany (was) are based on a stakeholder model of corporate governance with long-term bank credits and pension book reserves. Long-term employment relations come along with high skills via dual vocational training and firm-based occupational pensions.

Recent reforms and demographic challenges combined with a trend towards the shareholder model increased pressures on German companies to reorganize their occupational pension schemes. But in 2007 a typical feature of CMEs, pension book reserved pension funding, accounts for 36% of all occupational pensions in the private industry. One can see an increase of superannuation funds but also an increase of pension funds (their relevance is still low) (see Table 4).

Table 4 Development of coverage-rates



Source: (TNS Infratest 2007: 32)

Four factors influence the variations in pension fund assets: The starting point of supplementary pension plans (early, late), the financing mode (PAYGO, funded) the coverage (mandatory, voluntary) and tax deductions or subsidies.

The variations in pension fund assets, financing vehicles and asset allocation reflect the differences in the design and maturity of the public-private mix and pension systems across countries (see Table 5). Here we can see the impact of the pension system on financial markets, a relative low impact for the CMEs (Austria, France, Italy and Germany) and a relative high impact for LMEs (UK and USA). In the UK and the US supplementary pension plans started decades ago. The Netherlands are a special case due the quasi-mandatory funded second pillar (occupational pensions) (Bannink and Vroom 2007).

The CME Germany and Austria have a high percentage of book reserves of all funded pensions whereas the pension fund share is higher in the US and UK. In Italy a high pension fund percentage of all funded pensions come along with relative low percentage of funded pensions compared to the public PAYGO system.

Table 5 Heterogeneity of financing vehicles used in funded pension arrangements, 2006 % of all funds

	Pension funds	Book reserves	Pension insurance contracts	Other
Austria	56	44 (e)	..	..
France	16,2	..	83,2	0,7
Germany	24	64,3 (e)	11,7 (e)	..
Italy	90,3	..	9,8	n.a.
Netherlands	94,2	n.a.	5,8 (e)	n.a.
UK	86,5	n.a.	13,5 (e)	n.a.
USA	61,2	n.a.	14,8	24

Own calculations, Source: OECD, Global Pension Statistics and (OECD 2007b)
(e): OECD preliminary estimate.
n.a. means not applicable. This has been determined thanks to the metadata, describing the countries' pension system.
.. means not available.

The total investment of pension funds in Germany in 2006 was about 4% of GDP, whereas it was 79,1% in UK and 78,4% in the US (see Table 6). There is an increase of absolute financial assets, but Germany is still far away from the liberal economies and close to Austria and Italy. Here again, the high percentage of investments of pension funds in the Netherlands refers to the quasi-mandatory occupational pensions.

Table 6 Pensions

	Total investment of pension funds	Financial assets		Contributions to pension funds	Benefits paid by pension funds
	% of GDP	Millions of USD		% of GDP	% of GDP
	2006	2006	2001	2006	2006
Austria	4,9	15.611,0	7.554,7	0,3	0,2
France	1,2	20.000,0	..	..	..
Germany	4,0	115.754,9	65.147,2	0,2	0,1
Italy	3,0	55.680,9	25.193,8	0,3	0,2
Netherlands	122,5	769.986,0	411.460,0	5,0	3,5
UK	79,1	1.763.762,1	1.040.471,9	3,0	3,0
USA	78,4	9.721.115,0	7.207.878,3	..	..

Source: (OECD 2007a): All types of plans are included (occupational and personal, mandatory and voluntary) covering both public and private sector workers.
.. Not available or not applicable.

The same tendencies can be observed for the contributions to pension funds and benefits paid by pension funds.

A more detailed analysis shows, that investments in pension funds between 2001 and 2005 show only a low increase in Germany and Italy (with low percentage of GDP) and even a decrease especially between 2001 and 2003 in the Netherlands, UK and the US. This collapse can be traced back to the turbulences of financial markets after the attacks against the United States on September 11th (see Table 7). It is obvious, that funded pensions are not just growing but there are also risks and decreases.

Table 7 Development of investment in pension funds 2001-2005 in Euros millions (% GDP):

	2001	2002	2003	2004	2005
Austria	8.436 (3,9)	8.594 (3,9)	9.621 (4,2)	10.704 (4,5)	11.499 (4,7)
France	.. (3,9)	.. (6,6)	20.000 (7,0)	20.000 (6,0)	20.000 (5,8)
Germany	72.745 (3,4)	74.773 (3,5)	78.679 (3,6)	83.835 (3,8)	86.784 (3,9)
Italy	28.132 (n) (2,3)	30.041 (n) (2,3)	32.563 (2,4)	35.696 (2,6)	39.845 (2,8)
Netherlands	459.447 (102,6)	397.767 (85,5)	482.623 (101,3)	531.077 (108,7)	627.481 (n) (124,9)
UK	1.166.260 (72,5)	.. (68,9)	1.037.865 (65,1)	1.178.629 (68,8)	1.241.161 (e) (70,1)
USA	10.873.626 (96,2)	9.214.313 (84,1)	9.202.480 (96,2)	9.339.220 (99,6)	9.974.488 (98,9)

Source: OECD Global Pension Statistics
e means OECD Staff estimates
n means estimated at national level
.. means no data

In the third pillar Riester-contracts are mainly financed via insurance and bank contracts (8,9 million) and not via investment funds (2 million) (BMAS 2008). Savings of bank or insurance products were less invested in stocks than savings of investment funds. The latter allows 100% investment in stocks and the former allows a maximum of 35% of assets to stocks (Vitols 2003: 106).

It is questionable if the new introduced Riester-pension and pension funds strengthen the capital market. Maybe higher coverage-rates of fully funded plans come along with lower coverage-rate of other asset formations (e.g. life insurances) and that we can expect a regroupment. And maybe the new capital flow towards markets is not enough to change the coordinated market economy.

In Germany the starting point was late compared to LMEs like the US and UK, the main financing mode was and still is book reserved (private sector) or PAYGO (public sector) but the mandatory character enlarges and supplementary pensions are subsidized and tax deductible.

From a regulation and governance perspective it can be assumed that Germany is still more coordinated than uncoordinated, not just hierarchical but also organized decentralized, but with a small move towards the liberal direction. Social policy regulations of private and occupational pensions (subsidies, tax deductions) and the legal claim to earnings conversion coordinate the supplementary pensions and a part of financial markets. In the non-state area social partners regulate and coordinate collective agreements on occupational pension. The strong inclusion of social partners in occupational pension schemes and their forced increase elevate the relevance of unions and employers' association for financial markets.

Discussion

The privatization or deregulation of the German old-age security system gives raise to public involvement via state regulation (= reregulation) and organized decentralization via different collective agreements. Especially in the new Riester-pension plans we can state a transfer of social ends to private pensions/ markets. The former microeconomic-oriented occupational pension changed to a more social policy-oriented scheme.

Despite higher regulation and governance of supplementary pensions due to reforms in 2001 and 2004 their coverage rates increased after a decrease between 1976 and 1990 (see for the decrease Bruno-Latocha 2000: 146). Supplementary pensions for public sector employees have advantageous conditions compared to the private sector in respect to financial governance, benefits and redistributive benefits. Certainly, one reason is the mandatory character and high employer contributions.

Tax deductions for the second pillar are more generous than for the third pillar. The fact that you will need occupational or private pensions in addition to the reduced public pension (but not with less contributions) for a an adequate living standard in retirement age means that today we have the often discussed and neglected double-payer-problem situation (Bruno-Latocha and Grütz 2001: 417).

In Germany a stronger linkage and coordination of the three pillars is obvious via the Riester-subsidy for the second and third pillar and the consideration of tax deductions for the second and third pillar (4% of earnings ceiling) in the formula for public pension adjustments (=coordination). Other coordinated elements are information of insurants about their contracts and future benefits (state and supplementary pensions are affected) and a common taxation across pillars. There is a shift to more liberal elements and a reinforced development of supplementary pensions but under a state frame with state regulation (control) and organized decentralization via collective regulated occupational pensions. The interplay of the main actors state and social partners is important for the old-age security system and the public-private mix of today and in the future. This governance of supplementary pensions is not uncoordinated, institutional change occurred, but Germany is still far away from becoming a liberal market economy, it is more an updated coordinated market economy.

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