DEVELOPMENTS

German Labor Law in Transition

*By Marita Körner**

A. Introduction

For decades, German labor law has been among the most advanced in the world, although no labor code was ever enacted like, for e.g., in France with its 'Code du travail' adopted on 15th November 1973. In Germany, after World War II, German labor legislation developed a great variety of specific Acts covering individual and collective labor law. Basics, like protection against dismissal or collective bargaining, as well as employee participation in works councils, reached a high level. Although German law belongs to the Continental legal systems and thus is mainly based on legislation, some of the most important aspects of collective labor law, especially trade union law and the right to strike are not regulated by statutory law. *Bundesarbeitsgericht* (the Federal Labor Court) and *Bundesverfassungsgericht* (the Federal Constitutional Court) filled in the blanks step by step in a variety of decisions. Accordingly, these crucial fields of labor relations are based on mere case law. It turned out to be politically impossible to get trade union law and the law on strike and lock-outs enacted. Despite statements to the contrary, the parties involved seem to be content with this rather flexible handling.[1] On the whole, German labor law became more and more protective over the years, including aspects like equality and prohibition of discrimination in employment, sick-leave payment, and the possibility to claim a part-time job under the 2000 Act on *Teilzeit- und Befristungsgesetz – TzBfG* (Part Time and Temporary Work).

The main structures of today's German labor law were developed in the decades of the so-called *Rhineland capitalism* (named after the location of the former capital Bonn on the Rhine River).[2] This form of capitalism stands for a market economy

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[1] *See e.g*, RALPH BÜNGER, DER VERHANDLUNGSBEGLEITENDE WARNSTREIK (1996), with numerous references.

[2] The term was eminently coined by MICHEL ALBERT, CAPITALISME CONTRE CAPITALISME (1990). On the ongoing debate over the fate and prospects of the German model of Capitalism, welfare policy and corporate governance *see e.g.*, Peer Zumbansen, *Germany Inc. Eroding? - Board Structure, CEO and Rhenish Capitalism*, 3 GERMAN LAW JOURNAL NO. 6 (1 JUNE 2002), available at: http://www.germanlawjournal.com/article.php?id=156; Jürgen Hoffmann, *Co-ordinated Continental*

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which is, although capitalist in principle, characterized by important social protection and a more cooperative than antagonistic attitude between employers and trade unions. This Rhineland capitalism grew after the Second World War in the prosperous decades of the "old" Bonn Federal Republic. Since the collapse of the Soviet Union and the reunification of West and East Germany in 1989, priorities have shifted - slowly but steadily. In the first years of the 1990s, many countries with comparable industrial structures underwent major economic adjustments, including their social systems (e.g. in Scandinavia), whereas Germany profited from East Germany's enormous demand for goods. This gave the West German economy special conditions against the global trend. At the same time, this slowed down the implementation of necessary changes. However, the euphoric years were soon over and the catch up work to adapt to the rest of the world began. As Germany had lost so many years of realistically thinking about reforms before putting them into life, the present Social-Democratic Berlin government is now eager to catch up and laws are being passed in sometimes hasty manners. It is not surprising that in this atmosphere of urgent change, labor law is high on the agenda.

B. Reasons for labor law reform

Why are changes necessary at all? Trade unions have been asking this question during the past years, whereas employers have been demanding fundamental changes, particularly in regard to the existing protective labor law legislation. Globalization - one may like or dislike the term; nevertheless, it is inevitable to recognize that it is real and today's globalization is something different from the outward orientation and global focus of German companies in the past. Today's globalization is different because world-wide open markets, especially for capital and the technical possibilities of exchanging any type of information around the globe within seconds, have practically dissolved national borders and drastically undermined the effect of national legislation, especially if it is not considered to be compatible with international capital market needs by the so-called global players, *i.e.* transnational groups of companies. It is true that the different branches of industry are not all touched by this effect to the same extent, but on the whole, the pressure on companies to reduce costs continues to increase due to the possibility to transfer production to other countries; this has become a daily threat in collective bargaining. One of the latest German examples is the drastic reduction in employment by General Motors at the Opel plants in Germany.[3] The remaining

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Eurpoean Market Economies Under Pressure From Globalisation: Germany's "Rhineland capitalism", 5 GERMAN LAW JOURNAL NO. 8 (1 AUGUST 2004), available at: http://www.germanlawjournal.com/article.php?id=485; Peter Kolla, *The Mannesmann Trial and the Role of the Courts*, 5 GERMAN LAW JOURNAL NO. 7 (1 JULY 2004), available at: http://www.germanlawjournal.com/article.php?id=460.

General Motors at the Opel plants in Germany.[3] The remaining workforce has to make considerable concessions. In the service sector, globalization affects employees even more directly because no expensive transfers of production are necessary. It is easy to establish a new office elsewhere as soon as the legal, political and social frame in a country is no longer considered compatible with company needs. The sinking importance of old industrial structures and the growing importance of the service sector accelerates the process. Meanwhile, it has been hoped that the losses of employment in the production sector could be compensated for by more employment in the service sector. However, this is not the case as it is above all the service sector which profits from the rapid development of information technology so that many services function with few employees.

In listed companies, this tendency to reduce the workforce in order to reduce costs is enforced by giving 'shareholder value' priority over stakeholder oriented approaches.[4] Against the American backdrop, a common explanation is that institutional investors, above all pension and other funds, pressurize boards to make short-term decisions in order to reduce costs. This is supposed to lead to higher prices for shares, which influences the performance of the fund (and the performance of the fund manager). One of the most effective measures of reducing costs in the short term is to dismiss employees. This scenario may become more important in Germany in the near future. So far, pension funds which are the main players in the United States, rarely exist because pensions are paid out of a state pension system and not by private funds. However, as the state system has to deal with the demographic problem that fewer and fewer working people have to subsidize a growing number of pensioners, first steps have been undertaken by the German government to change the system. On the one hand, state pensions have been and will be reduced over the coming years. On the other hand, private pension systems will be subsidized by the state in order to incite people to get involved in them. This will probably lead to a growing number of pension funds which will inevitably exert considerable influence on companies.

On the employees' side, the change in economic structures is reflected in different employment biographies. Until the end of the 1990s, the so-called normal employment meant full-time for an unlimited period. In the meantime, the number of temporary employment, subcontracted work and freelance work, have increased con-

[3] From the worldwide coverage of the events in Detroit and Rüsselsheim, S*ee e.g.*, http://www.dw-world.de/dw/article /0,1564, 1362090,00.html; http://www.dw-world.de/dwelle/cda/popups/dwelle.cda.popups.galeriebild/0,3804,266_G_1427059_1426850 _17,00.html.http://www.detnews.com/2004/autosinsider/0410/19/autos-306467.htm; http://news.bbc.co.uk/2/hi/business/ 4083159.stm.

[4] Pierre Habbard and Roy Jones, *A breakthrough for stakeholders*, MITBESTIMMUNG NO. 8, (2004) 18.

siderably. During the phase of the Rhineland capitalism, life-long employment was the rule.[5] Now employment has become far less steady. For many, phases of employment, often temporary, are followed by unemployment, extended vocational training or freelance work. On the whole, employee income is stagnating or decreasing. These structural employment problems show up particularly in the continuously high unemployment rate. Unemployment already started to rise in Germany in the late 1970s and has not significantly been reduced ever since. In 2003, the unemployment rate was 8.4% for the old *Länder*[6] and 18.5% for the new *Länder*[7], thus a decisive factor in German politics. As a consequence, the reduction of unemployment is one of the principal arguments for changes in labor law. According to well accepted logic, it is the high level of labor protection that prevents employers from employing people (and foreign investors from investing in German corporations). On the other side of this coin, there is the idea that less anti-dismissal law, less anti-discrimination legislation or less collective bargaining rights, could incite more employers to build up their workforce.

C. Labor law on the 65th *Deutscher Juristentag* (German Lawyers' Association Symposium)

Against this backdrop, it is not surprising that the *Deutscher Juristentag* - DJT (German Lawyers' Association 65th Symposium) dealt with this subject during its last session in September 2004. The German Jurists Forum is an association of jurists, including judges, the legal profession and academics, dating back to the 19th century. They deal with current legal issues which are prepared by reports. The DJT recommendations have often had an impact on the legislature. The different legal matters are treated in *Abteilungen* (working groups) whose propositions are put to the vote of the attending lawyers. The underlying reports, the discussions in the working groups, and the votes, are published and constitute no less than an important archive and witness to contemporary legal history in Germany.[8]

In the labor law working group, the central topic was whether or not labor law should be different for small and medium size enterprises (SME), 'different' meaning less protective. SME are considered enterprises with a maximum of 249 em-

[5] MICHEL ALBERT, CAPITALISME CONTRE CAPITALISME (1990).

[6] Statistisches Bundesamt Deutschland: available at: www.destatis.de/basis/d/erwerb/erwerbtab3.php.

[7] Statistisches Bundesamt Deutschland: available at: www.destatis.de/basis/d/erwerb/erwerbtab4.php.

[8] Deliberations of the 65th German Lawyers' Association Symposium 2004 (*Verhandlungen des 65. Deutschen Juristentages, Bonn 2004, Band I: Gutachten; Band II/1: Referate und Beschlüsse; Band II/2: Diskussion und Beschlussfassung*).

ployees. The underlying concept is that German labor law is considered to be more difficult to adopt for smaller companies than for larger ones leading to a situation where the SME do not employ personnel because they fear the (expensive) consequences of the law. The rapporteur of the working group, Professor Abbo Junker of the University of Göttingen, analyzed this question under two aspects: first, he took into consideration the Act on Protection against Dismissal[9]; secondly, the Works Constitution Act[10]idea of deregulating labor law in favor of SME is of great relevance because two thirds of all employees in Germany work in entities of this size and 99% of all enterprises belong to this group. Changing the law for small and medium size enterprises therefore would mean changing labor law as such.

I. Protection against dismissal

1. Propositions

In individual labor law, protection against dismissal is a key subject. In Germany, this field was first covered by general clauses of civil law until 1969 when the *Kündigungsschutzgesetz* (Unfair Dismissal Act) first came into force. On the basis of the current legislation, there is still a high level of protection against dismissal. Although the Act is conceived to guarantee employment for an *unlawfully* dismissed person, in reality, it has developed into a mere severance pay system. This means that in a case of unlawful dismissal, the dismissed employee will not be reemployed but will merely receive compensation. This is due to an exception clause in the Act which allows either party to reject reemployment for loss of confidence (Art. 9 of the Dismissal Protection Act). There are hardly any dismissal cases where employers do not have recourse to this clause. Consequently, practically no employer is bound to continue work with an employee if s/he is not willing to. However, if dismissal is unlawful, it is costly. These costs are the reason for demanding change of the Act in favor of SME. Still, the rapporteur to the 65th DJT did not argue for a structural change of the Act. The proposition was more elegant. Today, the Act is only applicable if ten employees are working in the enterprise. For units below this threshold, the Dismissal Protection Act is not applicable at all. According to Professor Junker, in order to promote SME, the easiest thing to do would be to raise the threshold to 20 employees. In 2004, the threshold was changed under the present government in Art. 23 of the Dismissal Protection Act[11] from five to ten employees by government even though past experience had shown that this would

[9] Abbo Junker, *Arbeitsrecht zwischen Markt und gesellschaftspolitischen Herausforderungen, Gutachten B zum 65*. DEUTSCHEN JURISTENTAG 46 (2004).

[10] *Id..*, 84.

[11] BGBl. I p. 602.

not help raise the employment rate. From 1996 until 1998, the then conservative government had changed the threshold accordingly without a traceable effect on employment. Therefore, in 1998, the new government took back this change but re-enacted it a few years later.[12] So now we stand at a threshold of ten employees for the application of the Unfair Dismissal Act. In this situation, an increase of the threshold would indeed prevent many small enterprises from having to apply the Act. However, it is difficult to understand why 20 employees would be the magic figure to help SME. Why not 15 or 50 or any other figure, especially as they already exist in German labor law which has to deal with some 160 thresholds in numerous Acts.[13] They are apparently an important means to grade the level of employee protection.[14] So the *Betriebsverfassungsgesetz* (Works Constitution Act - *BetrVG*) of 25 September 2001 is applicable only for enterprises with a minimum of 5 employees. The right to work part-time as provided for in the *Teilzeit- und Befristungsgesetz* (Act on Part Time and Temporary Work – *TzBfG*) of 21 December 2000 has only to be granted by employers who employ more than 15 employees (Art. 8 para. 7 of the Act). Art. 622 of the *Bürgerliches Gesetzbuch* (German Civil Code - *BGB*), provides for minimum terms of notice to terminate a contract of employment. Art. 622 para. 5 No. 2 concedes an exception in cases where an employer does not have more than 20 employees. The main argument for these thresholds is to reduce the "burden of labor law" for small enterprises[15], but this does not disprove that the figures are arbitrary. Even Prof. Junker admits that there is no logic in these figures[16]. Consequently, it is very likely that the number of 20 employees is only a further step in the race to the bottom of unfair dismissal law.

This pessimistic view is even more realistic with regard to the second threshold in the Unfair Dismissal Act: even if the enterprise is large enough, the Act is only applicable for employees who have been with the same employer for at least six months. Professor Junker pointed out that it would help SME to extend this period without explicitly saying what other period he was thinking of. However, in labor law discussion, the most recent proposition was that only those employees who

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[12] As to the recent amendments to the Dismissal Protection Act cf. Thomas Ubber, *Agenda 2010: Reform of German Labor Law: Impact on Hiring and Firing Staff*, 5 GERMAN LAW JOURNAL NO. 2 (1 FEBRUARY 2004), available at: http://www.germanlawjournal.com /article.php?id=380.

[13] Abbo Junker & Ute Dietrich, *Schwellenwerte in arbeitsrechtlichen Gesetzen*, NEUE ZEITSCHRIFT FÜR ARBEITSRECHT (NZA) 2003, 1057.

[14] Esther Endress, *Schwellenwertregelungen im Arbeitsrecht - Verfassungsrechtliche und rechtspolitische Fragen*, 2002.

[15] *See, supra*, note 9 at S. 39.

[16] *See, supra*, note 13 at 1059.

have worked with the same employer for a minimum of three years should have recourse to the Unfair Dismissal Act. Essentially, this means that employees would be on probation for a three year period.

2. No evidence

The main argument for these propositions is that a lighter Unfair Dismissal Act could increase the employment rate. This, however, needs evidence. Generally, the economic and social effect of a law are not very well researched before put into force. There is also very little empirical proof of the effects on society once enacted. Normally, law is put into force on the basis of mere assumptions, without any empirical evidence. In labor law, however, there are several up-to-date empirical studies on the practice of the Unfair Dismissal Act, especially in SME[17]. There is a tendency among employers to perceive labor law negatively which may explain a certain psychological bias against protective labor legislation.[18] The main results of the surveys are, however, that the threshold has no effect on employment. In reality, other problems may prevent SME from employing more personnel. Many of them have financial problems because credit terms are very rigid. Outstanding accounts can sometimes even threaten their existence. This was also the conclusion of Professor Heide Pfarr, chairperson of the Hans Böckler Foundation, in her report which she presented at the 65th DJT[19] in annotation to Professor Junker's presentation. Professor Dieter Sadowski, an economist from the University of Trier, came to a similar result in his report.[20] He admitted that the Unfair Dismissal Act may prevent employment but pointed out that it would also be likely to prevent dismissal. Economically, this would lead to a zero-sum game. In the end, there would be no

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[17] Thomas K. Bauer, Stefan Bender, & Holger Bonin, *Dismissal Protection and Worker Flows in Small Establishments*, IZA DISCUSSION PAPER NO. 1105, APRIL 2004; Sher Verick, *Threshold Effects of Dismissal Protection Legislation in Germany*, IZA DISCUSSION PAPER NO. 991, JANUARY 2004; Werner Friedrich & Helmut Hägele, *Ökonomische Konsequenzen von Schwellenwerten im Arbeits- und Sozialrecht sowie die Auswirkung dieser Regelungen - Kurzfassung des Endberichts*, 1997; JOACHIM WAGNER, CLAUS SCHNABEL & ARND KÖLLING, IN: DETLEV EHRIG & PETER KALMBACH (EDS.): WENIGER ARBEITSLOSE - ABER WIE?, (2001) 177; Harald Bielinski, Josef Hartmann, Heide Pfarr, & Hartmut Seifert, *Die Beendigung von Arbeitsverhältnissen: Wahrnehmnung und Wirklichkeit*, ARBEIT UND RECHT (2003), 81.

[18] Peter Janßen, *Arbeitsrecht und unternehmerische Einstellungsbereitschaft*, 31 IW-TRENDS NO. 2 (2004), 16.

[19] Heide Pfarr, *Arbeitsrecht zwischen Markt und gesellschaftspolitischen Herausforderungen - Differenzierung nach Unternehmensgröße?*, paper presented at the 65th German Lawyers' Association Symposium 2004 (*not yet published*).

[20] Dieter Sadowski, *Arbeitsrecht zwischen Markt und gesellschaftspolitischen Herausforderungen: Differenzierung nach der Unternehmensgröße*?, economic paper presented at the 65th German Lawyers' Association Symposium 2004 (*not yet published*).

more or less employment with or without unfair dismissal protection.[21] However, as Professor Sadowski pointed out, the structure of the employees has influenced more women, young people, and long-term unemployed to stay without employment under an unfair dismissal protection regime.

II. Works councils

Even modest enlargement of the works council's rights in 2001[22] have been criticized; although, at the same time, there were propositions to transfer rights from the collective bargaining units - trade unions and employers' organizations (which were industry-wide in Germany) - to the works council level. At the 65th Jurists' Forum it was not explicitly this 2001 reform which was on the agenda but the fact that the most important works council's rights were said to be too far-reaching for SME. In Germany, a works council may be elected by all employees in companies with a minimum of five employees. For special rights, the underlying Act, the Works Constitution Act, provides for thresholds. So for example, an Economic Committee which has specific information rights can only be constituted in companies with a minimum of 100 employees. However, on the whole, the main codetermination rights of the works council are not linked to the size of the company. Therefore the proposition on the 65th Jurists' Forum was to grade the rights of the works council according to the size of the company so that in SME, a works council would have fewer rights than in larger companies.

According to the opposing position however, on the one hand, the establishment of a works council is not compulsory anyway. It must only be elected if employees want it to be elected. In practice, less than one third of companies with up to 100 employees have a works council. In entities with up to 20 employees, the rate is only 4 percent.[23] If the vast majority of SME have no works council, there is no need to provide for special SME-rights. On the other hand, experience with graded rights of works councils, *e.g.* in France, has not been positive. There the *Comité d'entreprise* with relatively far-reaching rights may only be elected in companies with 50 or more employees. For smaller ones, there are other employee representatives, *les délégués du personnel,* with fewer rights. The system is very complex and often con-

[21] Stephen Nickell & Richard Layard, *Labor Market Institutions and Economic Performance*, 3 HANDBOOK OF LABOR ECONOMICS C. 3080 (1999); Ronald Schettkat, *Mehr Arbeit durch weniger Recht?*, WIRTSCHAFTSDIENST NO. 83 (2003), 225.

[22] *See* further Manfred Weiss, *Modernizing the German Works Council System: A Recent Amendment*, 18 INTERNATIONAL JOURNAL OF COMPARATIVE LABOUR LAW AND INDUSTRIAL RELATIONS (IJCLLIR) NO. 3 (2002), 251.

[23] BT-Dr (Official Gazette - *Bundestagsdrucksache*) 14/5741, p. 2.

fusing, even for the representatives themselves. In short, it is not very effective but very bureaucratic[24] and thus not a model for other countries to follow.

III. Elsewhere, too: Labor law under pressure

To complete the picture of the present state of German labor law, two more fields shall be mentioned where deregulation is also at stake. They were not officially on the agenda at the 65th Jurists' Forum but they were tightly connected to what was discussed there.

1. Right to work part-time

Only four years ago a right to work part-time was guaranteed to employees who wished to reduce their working hours in companies with a minimum of 15 employees.[25] If an employee so required, the employer had to grant part-time work unless s/he was able to prove urgent economic grounds not to do so. This new right has been much criticized for restricting the flexibility of employers which is why it is also threatened.

2. Collective bargaining

The legal rules for collective bargaining were only on the agenda indirectly. This is, however, a crucial topic. Collective bargaining in Germany takes place on branch and regional levels between trade unions and employers' organizations. Works councils, which are formally independent from trade unions, also have bargaining powers which are strictly separated from the trade union level. Works councils may only deal with certain matters in so-called *Betriebsvereinbarungen* (company agreements).[26] Company agreements must not treat matters which are normally dealt with in collective bargaining agreements (between trade union and employer), above all salary and working time. Exceptions are possible if the collective bargaining agreements contain opening clauses for company agreements or if company agreements are more favorable for employees. In case of conflict, collective bargaining agreements between trade unions and employers' organizations prevail. In practice, however, many company agreements directly contravene the law. The most popular setting is the following: works councils negotiate agreements with the

[24] MARITA KÖRNER, FORMEN DER ARBEITNEHMERMITWIRKUNG: DAS FRANZÖSISCHE COMITÉ D'ENTREPRISE (1999).

[25] Marlene Schmidt, *The Right to Part-time Work under German law: Progress in or boomerang for equal employment opportunities?* 30 INDUSTRIAL LAW JOURNAL (2001) 335.

[26] Art. 77 Works Constitution Act of 21st September 2001.

employer which provide for longer working hours and/or less pay than granted in the relevant collective bargaining agreement. As compensation, employers promise to refrain from dismissals for a certain period, arguing that this package is more favorable for employees than the collective bargaining agreement. This type of agreement is daily practice in Germany.[27] In the leading *Burda*-case, however, the Federal Labor Court confirmed its preceding decision that only the same types of working conditions may be compared.[28] Thus, the working time of the collective bargaining agreement could be reduced by a works council company agreement. A link between working time or salary and job guarantee is, however, not permissible. The trade union, of course, could negotiate such an agreement. Only the works council is not in a position to do so. Consequently, more far-reaching opening clauses in collective bargaining agreements or even a general opening clause in the relevant Acts are on the agenda in order to better adapt the law to the needs of the shop floor.[29] Then agreements between trade unions and employer would only provide a frame for further negotiation. The crucial details would then be negotiated on the shop floor level by the works councils and the employers. At first glance this would lead to a stronger position of the works council. Here we are back to the 65th Jurists' Forum, where works councils rights were considered to be too extended.

D. Conclusion

This discussion shows clearly what the debate is all about: although there is need for adaptations, the creation of more employment does not always seem to be the major concern. Of course, this is not openly put forward but many may think that the present situation, with weakened unions and employees under pressure, may be a good chance to deregulate labor law on a wider scale.

However, there is no need for a SME labor law. Thresholds in Labor Law Acts are arbitrary: why 20, why not 15, 50 or 100? There is no plausible argument for any of these figures. Also, the economic argument is not convincing. Economic theory seems to support the view that protection of labor is an obstacle for the economy. However, even economists are divided on this. As mentioned above, studies prove

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[27] Cf. Achim Seifert, *Employment Protection and Employment Promotion as Goals of Collective Bargaining in the Federal Republic of Germany*, 15 INTERNATIONAL JOURNAL OF COMPARATIVE LABOUR LAW AND INDUSTRIAL RELATIONS (IJCLLIR)_ NO. 4 (1999), 343.

[28] BAG AP Nr. 89 zu Art. 9 GG (20 April 1999).

[29] Herbert Buchner, *Öffnung der Tarifverträge im Spannungsfeld verfassungsrechtlicher Vorgaben und arbeitsmarktpolitischer Erfordernisse*, in: GEDÄCHTNISSCHRIFT FÜR MEINHARD HEINZE 105 (ALFRED SÖLLNER ET AL. EDS. 2005).

that especially dismissal law has no influence on the employment rate. Instead of dividing labor law into units for SME and other companies, it would be more forward-looking to further develop the concept of *flexicurity* - more flexibility for the economy with enough security for employees. And finally, hardly anybody seriously asks what the loss of social protection will cost the economy.