
Notes and Brief Reports

Social Security Abroad

German Provisions for Deferred Retirement*

The social security system of the Federal Republic of Germany adopted a flexible retirement age in the early 1970's. The general trend then—in Germany and in other countries—was toward providing for earlier retirement. When the reform was instituted in 1973, it included, almost incidentally, a special advantage for workers continuing on the job beyond age 65 that would enable them to increase their pensions substantially.

Since that time, two factors have added considerable importance to the deferral provisions: (1) The world recession that has caused financial problems for most social security systems in industrial countries and (2) increasing awareness of the aging of the population—a growing problem in Europe. Consequently, working contributors per social security beneficiary have become fewer and fewer. Both recession and demographic trends have put pressure on social security resources and programs to encourage workers to stay in the labor force and contribute longer and to put off the decision to draw their social security benefits.

Flexible Retirement Under 1973 Reform

The Federal Republic of Germany adopted the deferred retirement age as part of a larger legislative package intended mainly to provide early flexible retirement to Germans above age 62. The announced purpose of creating this flexibility was to make retirement more “humane” for those with a “full working life”—that is, with 35 years of covered employment. Lawmakers recognized that physical and mental exhaustion resulting from long years of employment would make the possibility of early retirement popular among the working population. The thrust of flexibility was to permit not only greater latitude

in making retirement decisions, but, specifically, to permit earlier retirement.

Before 1973 the normal retirement age had been 65. The 1973 reform made available a range of retirement ages. Now a normal retirement benefit can be received beginning at age 63 or 64, if the individual has completed 35 years of covered service. This requirement can usually be met without any problems since most workers enter the labor force in their teens and because the German social security system gives credits for periods of unemployment, wartime, etc. The pensioner who retires early is permitted to work, if certain income and time limitations are not exceeded. To keep his pensions, he can earn no more than 30 percent of average earnings (a maximum of approximately \$430 per month in 1977), or, alternatively, work no more than 50 days per year.

When the 1973 reform was initiated, the German social security system had not yet experienced significant financial problems. The reform continued the existing provision for retirement at age 65, without a retirement test. At that age a beneficiary is still entitled to his full pension with no limit on earnings.

Deferral Provisions

Deferral provisions were an almost coincidental byproduct of the 1973 reform. Persons who continue to work through ages 65 and 66 receive a special increment of 0.6 percent for each month worked after age 65, plus the regular increment of 1.5 percent for each year of service due any retiring employee. (This formula calls for 1.5 percent of average earnings for each year worked—45 percent for 30 years, for example, and 60 percent for 40 years.) In practical terms, a working person who defers retirement until age 67 receives a pension about 18 percent higher than the amount to which he would have been entitled at age 65.

In 1973, the deferral provisions were assumed to be especially suited for persons who want to stay on the job and are physically able to do so. Deferred retirement was also geared to men who want to increase their pensions in order to benefit their spouses, especially those considerably younger and most likely to survive their husbands by many years.

A potential beneficiary therefore has three options at age 65: (1) He may quit working altogether and live off his

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earned social security pension; (2) he may "retire"—that is, collect his benefit—and continue to work without any loss of income from either source; or (3) he may continue working up to age 67 without receiving retirement benefits and then receive the basic 1.5-percent increase per year, as accumulated from his entire working career, plus the 14.4-percent deferral increments.

Impact of New Provisions

Most of these potential beneficiaries choose the first or second option. The majority of them choose not to work at all. The employee who does decide to continue working must find out which is more advantageous financially—getting regular earnings and a full benefit or receiving earnings while building a larger, deferred benefit. Cash in hand seems to win out.

The possibility of receiving income from two sources from age 65 on has been preferred. In the eyes of the retiree, getting two incomes right away outweighs the long-range possibility of living long enough to do better financially with a higher benefit. In addition, the low rate of inflation has tended to discourage workers from delaying their benefits.

According to official reports, the response to the favorable deferral provisions has been minimal—less than 1 percent. In 1977, about 1,400 applications were made for annuities at ages 66 and 67. In October 1978, 12,000 pensioners were receiving benefits with over-age-65 increments. About one-third of all retiring workers decide to draw a benefit at the traditional age of 65. More than one-third retire at age 63. The rest retire at various ages from 60 to age 70 or older.

Trends Since Reform

The German flexible retirement legislation occurred at a time when its social security funds were prospering because the ratio of contributors to beneficiaries was at a favorable level and the contribution rate was high (17 percent in 1970, 18 percent since 1973). Since 1973, however, the number of working contributors has been declining as the number of social security beneficiaries continues to rise. Early retirement, a greater life expectancy for women, and the general decline in the labor force because of unemployment have rapidly absorbed the surpluses of the social security funds.

In 1973, 20.3 million working persons contributed to maintaining the pensions of 9.6 million social security beneficiaries. By 1976, contributors numbered only 19.8 million and the number of pensioners had risen to 11.0 million. The ratio of contributors to beneficiaries has thus dropped from 2.1 in 1973 to 1.8 in 1976. This negative demographic development resulted in a deficit of 6 billion deutsche marks in 1976¹ and has led to projections for continuing deficits beyond 1980. Recent social security legis-

lation provides for reduction of expenses and additional income to the funds. It is aimed at overcoming the financial impact of the growth in the number of beneficiaries by 1981.²

The scarcity of deferred retirements has not been studied. So far, the Government seems preoccupied with the problems of high unemployment and is trying to solve the financial crisis of the social security funds by other measures than inducing workers to defer retirement.

²See Lois S. Copeland, "Effect of Recession on Financing of German Pension Program," *Social Security Bulletin*, February 1977.

Book Review

Welfare

By Martin Anderson
251 pp., Stanford University, California, Hoover Institution Press.

The book provides an insightful account of the author's experiences while working on welfare reform efforts. Mr. Anderson was Special Assistant and Special Consultant to the President from 1969 to 1971. He was on the staff of Arthur F. Burns, Counselor to the President in 1969. Their efforts were aligned against the forces supporting Daniel P. Moynahan's idea of a guaranteed income, developed for President Nixon's Family Assistance Plan (FAP). The author provides reasons why FAP was doomed to failure, along with other major welfare reform efforts that continue to surface.

The critical acclaim provided statistics and statisticians offers an interesting balance throughout the book. Mr. Anderson cites his experiences with FAP as "a classic example of the power of research in the making of national policy." Some government series are criticized for their "gross" inadequacies. Yet the book provides a fact-oriented presentation of the recent history of welfare reform efforts, relying to a large extent upon various statistical series and major research efforts.

Each chapter presents thesis and discussion of such subjects as: The "war on poverty" has been won; a "poverty" wall (high effective marginal tax rates) destroys the financial incentive to work; the work effort of low-income workers would be substantially reduced by a guaranteed income; and radical welfare reform is politically impossible.

Mr. Anderson has drawn his evidence from the guaranteed income experiments and other research and government statistics as well as from personal experience. Poverty has been abolished, he says, through "the strong, sustained economic growth of the private sector . . . and the vast and growing array of government welfare and income transfer programs."

¹In March 1976, the deutsche mark equaled 40 cents (U.S.).