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The German Employment Protection Act – How does it work in company practice?

Karen Ullmann/ Dr. Silke Bothfeld

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Karen Ullmann
Former Academic assistant at the
Institute of Economic and Social Research (WSI)
Hans-Böckler-Foundation
e-mail: karenullmann@gmx.net

Dr. Silke Bothfeld
Institute of Economic and Social Research (WSI)
Hans-Böckler-Foundation
Hans-Böckler-Str. 39
40476 Düsseldorf
Germany
e-mail: silke-bothfeld@boeckler.de

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Abstract:

The article describes the manner in which in companies make decisions about dismissals. It begins with the presentation of a number of theories, which attempt to depict the complexity of the employment relationship. This is followed by the presentation of the legal framework and the various options for action at the respective levels. The third section draws together empirical data that illuminates the relevance of the various steps involved in the termination of the employment relationship. It shows that the prevalent assumptions that companies hold regarding the effects of the KSchG are unfounded.

Key words: Employment Protection Legislation, Dismissal, Severance Payment.

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1. Introduction

The focus of discussions on labour market politics moves again and again to dismissal protection, which, as an element of labour market regulation, is attributed partial responsibility for stagnating labour market development. Carried further, a relationship is assumed between the rigidity of dismissal protection and the employment trend, which is largely based on implicit assumptions about company behaviour. Above all, it is assumed that German dismissal protection makes dismissal more expensive and consequently deters companies from necessary new appointments. These theses have found their way into German labour market research without the assumed interrelationship being thematised in any way. Rather, the company is usually perceived as a black box, so that the internal company decision-making processes and motivation involved in personnel planning remains unconsidered (cf. on this subject, e.g. the articles by Jahn/Schnabel 2003; Jahn/Walwei 2003; Jerger 2003; Jahn 2004). In fact, aside from partial investigations conducted by human resources management, there has been no representative empirical research into how companies implement labour legislation since the Max-Planck Institute study of 1981[1], and consequently there are few substantiated findings about current company employment and dismissal practices.

This paper follows twin goals. On the one hand, it intends to show the spectrum of possible company behaviour while considering the theoretical principles of human resources management and in doing so identify complimentary or conflicting factors in the explanation of hiring and dismissal decisions. On the other hand, an empirical analysis of dismissal processes will illustrate the effect of labour law in company practice and so question the purely benefit-oriented “cause and effect” schema. This makes it clear that company practice is determined by a multitude of sometimes complexly interwoven factors among which labour law plays only a marginal role.

The structure corresponds to these two research goals. The first section discusses existing empirical findings and theoretical perspectives, identifies alternative options for action and relates these to the termination process. In the second section,

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[1] This research was commissioned by the Federal Ministry of Employment and Social Affairs and had the goal of researching dismissal protection and practice. Five sub-surveys were conducted: a representative, written survey of companies per post (612 companies were questioned about the general process of termination and a further 804 companies were asked about their last case of termination), a representative, written survey of works councils per post (740 cases), a representative, verbal survey (879 persons), plus an analysis of labour court files, including questioning Judges and legal representatives and an analysis of collective labour agreements. The questioning of judges and DGB legal protection secretaries was conducted as a complete, written survey by post (The rate of return lay at around 50 % in each case), a random sample was selected for the questioning of owners and lawyers (Falke et al. 1981).

company practice provides the basis for demonstrating the extent to which employer-initiated termination competes with other instruments during personnel adjustments, and how dismissal is carried out in business. The article is limited to an explorative approach and concentrates primarily on a descriptive presentation of findings. This approach permits a comprehensive presentation of findings from the only current representative survey on this subject: the WSI Survey on the Termination of Employment Relationships (2001) and the WSI Survey on Company Personnel Policies (2003). Where it makes sense or appears to be necessary, the findings are supplemented by analyses from the IAB Betriebspanel (Institute of Employment Research) and the Socio-Economic Panel (SOEP). Data is also drawn from the KÜPRAX Project. This project analysed dismissal disputes that were brought before the Labour Courts in 2003 (Höland et al. 2007). This means that all currently available data sources on this subject are used.

2. Engagements and dismissals in the shadow of the legislative regulation of employment – theoretical considerations

2.1 The limits of macro-economic analyses

As an element of the institutional labour market conditions, dismissal protection has occupied a central position in employment policy discussions since the OECD Job Study of 1994 (OECD 1994). The question of the effect of dismissal protection on the level, duration and structure of unemployment has given rise to a multitude of macroeconomic studies. However, it has not been possible to prove an identifiable and unequivocally positive relationship between the rigidity of dismissal protection and the rate of unemployment, though an effect on the dynamic of labour market processes – and therefore on the duration of long-term unemployment suggests: “All time spent in anxiously complaining about the rigidity of labour market regulation, employment protection and minimum wages is probably wasted“ (Nickell/Layard 1999: 3080; cf. the discussion on this subject in Truger/Hein 2003 and the overview in OECD 2004: 82). There is also doubt that employment protection has a clear effect on the development of productivity. In fact, regulation of the product market rather than of the employment market has been made responsible for slowing down productivity (Nicoletti and Scarpetta 2003), and the lack of long-term investment in the future, for example in training, for ongoing high unemployment (Aiginger 2004). In contrast, one suspects a positive relationship between employment protection and long-term unemployment (Elmeskov, Martin, and Scarpetta 1998), and a negative relationship between employment protection and production growth in those

countries where the wage parties negotiate their wages in neither a coordinated nor a completely decentralised manner (Scarpetta und Tressel 2004). The latter does not apply to Germany however, since wage negotiations are largely coordinated.

International comparative macroeconomic studies are afflicted by two methodological problems. Firstly, the development of indicators demands objectifying and reducing the complexity of labour law. The conventional EPL indicators (*Employment Protection Legislation indicators*, cf. Nicoletti, Scarpetta and Boylaud 1999: 40 ff.) mostly only consider the legal situation related to the regulation of employment relationships. The “cost of dismissals” or the “rigidity“ of employment protection is therefore not measured on the basis of empirical findings on the actual application of the legal conditions, but solely on the basis of selected formal legal regulations. Provisions that regulate application, which are highly relevant for the practice, such as, e.g. the duration of the term in which legal action can be filed and the openness of many regulations to change by collective labour agreement, are largely excluded from the analyses or cannot be compared due to the depth of their practice-related differences. For example, Denmark is often cited as a country without legislative dismissal protection. What is not taken into consideration is that here, dismissal protection is frequently regulated by collective labour agreements, which demonstrate a very high level of coverage. Since the individual steps in establishing the factors are not provided, it also remains unclear how, e.g. the cost of compensation for dismissal is evaluated, which German legislation anticipates only under exceptional circumstances but which is nevertheless often a result of negotiations between employers and employees. Consequently, the complexity of the various dismissal protection regulations and their application is usually only made clear in comparative legal studies (cf. on the subject, Zachert, 2004). In addition, the correct and immediate application of the formal regulations is assumed.

Secondly, comparative studies are revealed to be methodologically problematic to the extent that the real costs of the regulations have been far from completely documented. Namely, the data increasingly includes the regulation of functional equivalents (fixed term and personnel leasing). Sometimes the interconnection between labour law and social security systems is also included (OECD 2004: 91). Possible long-term costs for the company resulting from the specialist workers’ lack of commitment to the company and from the loss of these workers also remain unconsidered, particularly as they are difficult to measure and quantify. Generally considered, these country comparisons underestimate the complexity of the social and economic systems in which the regulations for dismissal protection are embedded (for a revised perspective cf. OECD 2004: 64). Analytical perspectives

whose theoretical and empirical focus is on the actions of the actors within companies appear to be more promising in their capacity to explain the effect of labour law regulations on company behaviour.

2.2 Company behaviour from the micro-analytical perspective

Labour market institutions as limitation and support to entrepreneurial action.

In macroeconomics, especially transaction cost theory (Williamson 1985) offers an approach to explaining company decisions. In contrast to the simple neoclassical contract model, in which contracts are negotiated through the free interaction of (market) forces, transaction cost theory assumes that the organisation and realisation of company actions (transactions) gives rise to costs, the scope of which are largely determined by the conditions of the institutional framework and which are not compensated for earnings: Hiring suitable employees entails information and search costs and possibly qualification costs; the employees' performance must be monitored and, where necessary, motivated through incentives or disciplinary action, and employee dismissal must also be planned and realised. Consequently, the costs incurred through dismissal, in the form of severance payments, legal action against unfair dismissal or backwages, are considered typical "ex-post" transaction costs. In this respect employment protection legislation can increase costs and therefore, it is not surprising that employers perceive labour market regulation as a *constraint* and limitation of their entrepreneurial action. However, institutional regulations can also improve the transactions in that they set transparent and binding rules and minimise variance in behaviour through routines and practices and consequently reduce the associated costs.

Because the conditions for employer-initiated dismissal are specified in the Employment Protection Act, it offers a binding legal basis that reduces the insecurity of both contractual partners in respect to their respective performance and obligations, and as such reduces the potential for conflict. For the German employment system, a typical "side effect" of the relative security of employment associated with the legislative regulation of labour is the willingness of employees to acquire company-specific qualifications and to remain in the company long term. Thus, labour law does not only act as a *constraint*, but also in ways as a support for companies.

The nature of the employment relationship and economic pressures as the most important determinants of personnel decisions.

The way in which is dismissal protection is practiced in companies and the extent to which it is actually a cost factor depends not only on the individual appraisal of labour legislation and the anticipation of possible sanctions. In fact, two additional factors play an important role: The relationship between the employer and employee within the firm and the existence of pressure to comply, i.e. the company's perception of this pressure.

The relationship between employer and employees can be marked by a purely functional and rather short-term calculation or through a long-term and tendentially cooperative and social personnel policy and culture. From the perspective of transaction cost theory, the employment relationship is considered a "relational" contract, which is characterised by the fundamental openness and long-term nature of the contractual relationship. Work performance cannot be agreed to in fine detail or for an extended duration in the employment contract so that the employment contract is a social relationship embedded in a complex social context (Ebers/Gotsch 2002: 231). The actual fulfilment of the contract (the assurance of employment and payment wages in exchange for the employee's performance of tasks) cannot be automatically taken from the formal legal framework. Rather it is determined by a series of complex factors such as motivation, mutual trust, company promotion and the company culture (for elaboration, cf. Sadowski 1986). The same phenomenon is discussed in the legal literature under the heading "incomplete contract". Further, the institutional economics perspective, to which transaction cost theory belongs, recognises that the parties to the contract (can) act rationally only to a limited extent because the amount of available and processed information is inevitably limited and therefore decisions are always made under a greater or lesser degree of uncertainty.

For example, companies can only estimate their personnel requirements when hiring or dismissing staff; they cannot determine their prospective requirements exactly. Because personnel requirements can change, the Employment Protection Act (KSchG) makes provision for dismissal on urgent operational grounds. Of course, companies must not necessarily be informed about the legal conditions in order to engage in hiring or dismissals.

As long as no conflict results, the lack of information about labour law is hardly noticed so that the companies evaluate their level of information as satisfactory in spite of their lack of knowledge. In this case, labour law has no relevance to company

actions, whereby both generous paternalistic and also short-term profit-maximising behaviour are by all means compatible with transaction cost theory assumptions. A further behavioural assumption of transaction cost theory is interesting in terms of explaining the behaviour of the various parties in the company. According to this, the contract partners are opportunistic or even sly and may act contrary to their knowledge of the law (Ebers/Gotsch 2002: 226). So it is theoretically plausible that the company provides its employees with false information, threatens them or attempts to prevent them from forming a works council. Conversely, the parties may choose a cooperative strategy and participation by employee representatives if they expect that this will result in a reduced amount of (expensive) conflict, better information or the conclusion of linked agreements. In any case, the respect and the departure from formal regulations can be consciously calculated: An unsystematic approach and the acceptance of legal disputes can be just as economically worthwhile as the long-term design and planning of the Personnel Department. On the employee side, the reaction to termination is also unforeseeable since the employees possess quite different levels of knowledge and expectations in terms of asserting their rights. Above all, they have an interest – although of varying intensity – in the maintenance of the employment relationship, which is dependent on their social security, their individual reemployment chances and their life situation. The assumption that an unjust dismissal is automatically followed by legal action is therefore unrealistic. In all cases, the behaviour on both sides is also influenced by other institutions, such as the form of unemployment insurance or the existence of early retirement regulations, which reduce the conflict potential of dismissals. The behavioural science organisation theory, which is more closely concerned with behavioural assumptions and conceptualises companies as the expression of a multitude of operational behaviours, drives the unforeseeability of business decisions to the extreme with the assistance of the “garbage can“ model (cf. the collected essays of March 1990). According to this perspective, the solution to problems, e.g. personnel decisions, can occur ad hoc and by chance, whereby the parties involved tend to oriente themselves on interpretation patterns (organisation culture) that are socially and culturally influenced, and widely accepted (Berger/Bernhard-Mehlich 2002: 159). Thus, a broad spectrum of company behaviours can be explained by transaction cost theory and behavioural science.

A second complex of factors, in our estimation, is the extent to which the reduction of personnel is viewed as a necessary and unavoidable solution. From the perspective of the business economics situational approach, the perception of problems is considered to be partly determined by other areas of action (e.g. goods and product markets) in the environment. Central to this approach is the assumption that formal

organisational structures have a strong influence on the efficiency of organisations, but that, on the other hand, there are no universally efficient organisational structures. In order to act efficiently, organisations must adjust their structures to the respective situations (Kieser 2002: 169). Consequently, labour law provisions are in no way uniformly implemented. Rather, the implementation is influenced by each company's respective reality, which in practice is confronted with the law. Of particular influence here is the company's size and branch, and the associated respective specific structural characteristics on the one hand, and its culture and traditions on the other.

The interpretation of the situation under labour law is correspondingly diverse. Because companies are not obligated to conduct personnel planning, internal decision-making takes place within the framework of more or less developed structures. Consequently, in this perspective the adoption and diffusion of labour law are also considered processes of organisational learning (on the problem of organisational learning, cf. the contributions in March 1990).

Here, changes to labour legislation are picked up and implemented with varying rapidity depending on the parties involved, their individual situations and the number of cases arising. This makes it possible to classify companies into various types according to their labour law culture. The spectrum ranges from an approach that is strictly guided by the regulations to an economic perspective in which the cost of complying with a regulation is weighed against contravention, through to the extreme case where labour law regulations are simply – consciously or unconsciously – ignored (Schramm/Zachert 2005).

Application of the des Employment Protection Act in practice

The structure of the formal legal framework leaves no room for the development of a political personnel strategy that would apply to all companies. Rather, it can be expected that a company's economic personnel culture and the micro-economic demands a company experiences, i.e. their interpretation, influence personnel decisions. As such, labour law is a necessary but insufficient variable for the explanation of personnel-political actions.

In summary, the theoretical considerations provide the basis for at least three hypotheses on the application of labour law and the generation of costs through the legislative regulation of labour:

1. The interpretation of the Employment Protection Act (KSchG) is relativised by competing problems in the company's environment. Problems connected to the product or goods markets prove to be much costlier and therefore more important. The strategy of cost reduction through personnel reduction and the signalling effect of saving (personnel) costs appears to be gaining significance with the increasing importance of stock exchange results so that – independent of understandable changes – an increasing amount of pressure for adjustment is experienced.

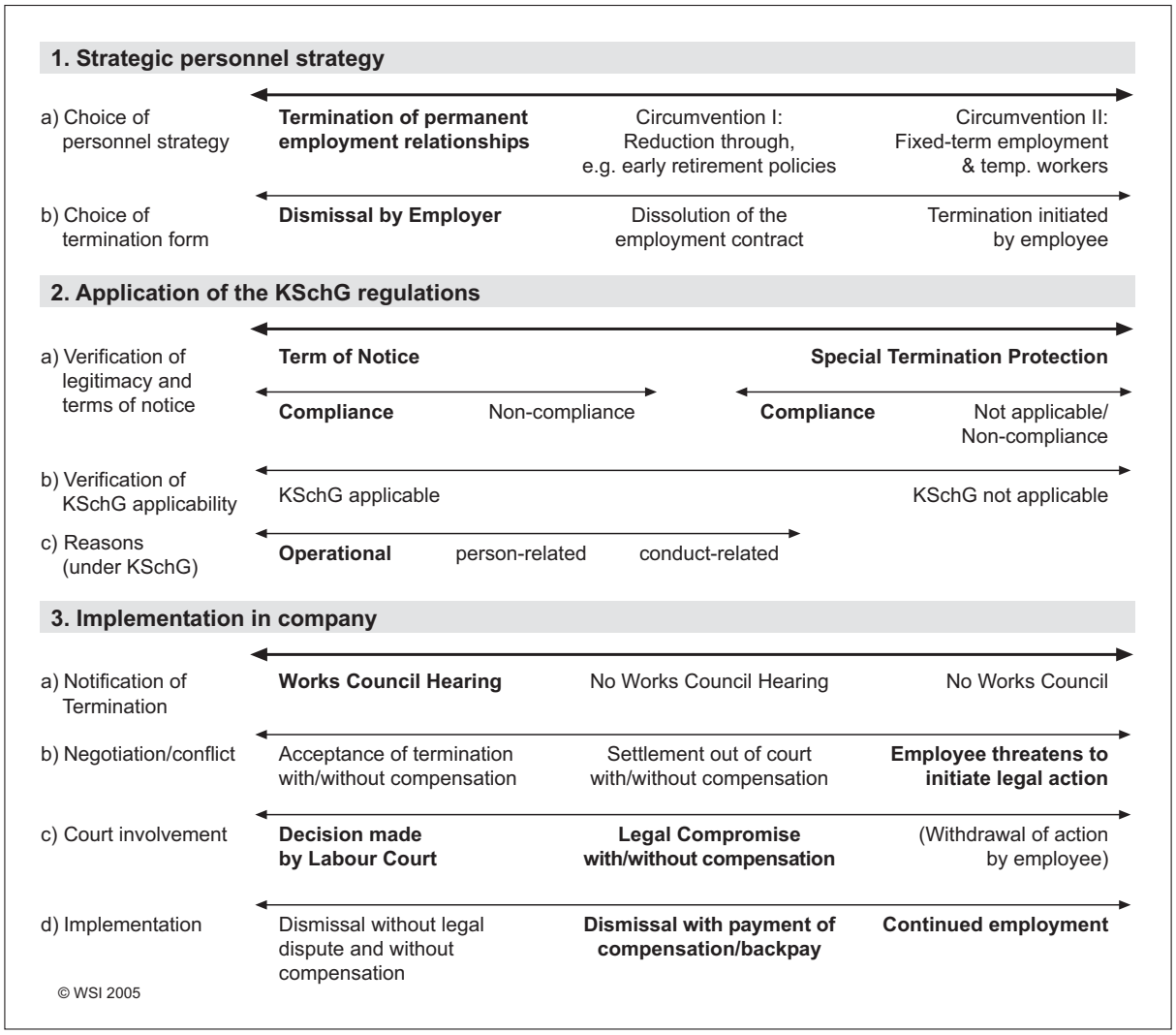
2. Transaction cost theory stresses the significance of information, i.e. of insecurity for operational action. In this respect, the Employment Protection Act (KSchG) must be considered not only a limitation but also a support that tends to standardise termination processes and make them transparent. In addition, because it protects the employees from arbitrary dismissal, it also increases motivation and consequently productivity, and provides an incentive for investment in company-specific training.

3. The "rational" of cost-calculated action by the interest groups in a company presents only one type of possible reaction. At the same time (personnel) decisions are also made under the influence of cultural and social factors and routine procedures. From this perspective, it is also possible that the company completely ignores the provisions of labour law and orients itself on its peer group, i.e. on other companies. The provisions of labour law are then only of relevance when it came to problems and the company is confronted with the valid legal situation (possibly in court) in order to solve these problems.

2.3 Analytical Framework: Stages of action in the adjustment of company personnel levels

Three typically characteristic stages can be distinguished when analysing the role of labour law in reducing of employee numbers: The choice of strategic personnel policy, the application, i.e. how the provisions of dismissal protection are handled and the company implementation of termination (Figure 1).

Fig. 1: Stages of Action in Company Personnel Adjustment



In choosing the approach of the personnel policy, a decision is first made about the nature of dismissal of the affected employees (Stage 1). Here, the provisions for fixed-term and temporary workers are effectively “functional equivalents”, which – with appropriate planning – make it possible to avoid dismissal processes (cf. also Zachert 2004). A reduction in personnel can also be achieved by not reoccupying positions that become vacant or by making use of the provisions of social positions such as semi-retirement or the reduction of working hours to reduce the volume of work. In this way, conflicts associated with employer-initiated dismissal can be minimised in advance (1a). Either a dissolution agreement can be concluded with the affected person or the employer can directly or indirectly call upon the person to give notice (1b). For employees to terminate the employment contract themselves is – unless a seamless transition into new employment is found – unattractive for the employee, because the self-initiated termination of the employment relationship can

result in their eligibility for unemployment benefits being blocked for of up to 12 weeks, which can consequently reduce their entitlements. According to a judgement of the Federal Social Court, a period of ineligibility can result not only from the conclusion of a dissolution agreement, but also from the conclusion of a so-called “Winding-up Agreement” in which the dismissed person enters into an agreement with the employer to accept the dismissal within the term in which legal action can be initiated through the Labour Court. Only when there are important grounds for concluding such a contract, does it fail to result in a period of ineligibility. If the dismissal is objectively justified on grounds that are not conduct related, this constitutes an important ground.[2] However, should this compromise be concluded before the Labour Court, no period of ineligibility is imposed on principle (on this problem, cf. Kramer 2004). Consequently, this precedence reduces the employee’s willingness to sign such contracts and possibly increases the occurrence of legal action. Following the introduction of Section 1a of the Employment Protection Act (KSchG), according to which the employer can offer the employee compensation in the written notification of termination, to which the dismissed person may only lay claim if they refrain from pursuing legal action, the Federal Social Court deliberates to waive investigation of the legal validity of the dismissal if the amount paid as compensation does not exceed the level anticipated by Section 1a of the Employment Protection Act (KSchG), i.e. half of the monthly wage per year of employment.[3] On the other hand, employees may prefer to terminate the employment contract themselves in order to avoid any possible disadvantages associated with dismissal during future job applications.

Should a company decide to dismiss an employee, the legitimacy of the dismissal and of any possible special dismissal protection must be checked and the terms of notice must be observed (Stage 2). If the Employment Protection Act applies to the company, the management must provide grounds for the dismissal, which may relate to the employee’s person or conduct, or to urgent operational business requirements, in keeping with the act. Should dismissal be due to operational requirements, all employees who perform comparable tasks must be identified in order to carry out a so-called social selection. According to the most recent legislative amendments,[4] increased consideration can be given to operational requirements, especially

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[2] Federal Social Court, Judgement of 12.07.2006, B 11a AL 47/05, published in: Neue Zeitschrift für Arbeitsrecht, Issue 23/2006, p.1359

[3] Federal Social Court, Judgement of 12.07.2006, B 11a AL 47/05, published in: Neue Zeitschrift für Arbeitsrecht, Issue 23/2006, p.1359

[4] Federal Law Gazette No. 67 of 30.12.2003, BGB. Part I 2003, No. 67, 30.12.2003, p. 3002.

differences in performance between employees. A further relaxation for the company is that in the event of a compensation agreement ("Interessenausgleich") the employer can compile a list of names together with the works council, i.e. jointly select the employees to be dismissed. In this case the burden of proof is reversed: Normally the employer must provide evidence that the dismissal is due to operative requirements; however, in this case the dismissed employee must provide evidence that there was no urgent operational necessity for the termination. In addition, the selection of those to be dismissed can only be legally challenged if it is grossly erroneous. If an employee has been selected for dismissal, the dismissal must be issued in written form (Stage 3). In the case of dismissal, the works council only has a right to information, i.e. it has the right to be heard prior to the dismissal, to be informed about the person and the grounds for dismissal (3 a).[5] Disregard for this obligation makes the dismissal ineffective. Should the works council disagree with the dismissal, and the employee decide to take legal action, he/she must continue to be employed by the company during the proceedings.[6] The dismissed person can accept the dismissal independent of an objection by the works council, he/she can attempt to negotiate a dissolution agreement and/or a severance payment or threaten to take legal action (3b). The situation described above applies here; the negotiating position of the dismissed person is restricted in that the participation in one's own dismissal leads to a partial loss of unemployment insurance benefits. The right to severance pay exists in only two cases. When other persons are simultaneously dismissed, this can result in the obligation to compile a social plan, which is usually accompanied by redundancy pay.[7] The social plan must be negotiated by the management and the works council. If there is no works council, there is no obligation to produce a social plan. If proceedings are already pending before the Labour Court, the employee has a right to redundancy pay in the event that he/she is successful before the court but cannot be reasonably expected to

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[5] In contrast, new engagements and the classification, reclassification and relocation of personnel requires consent, whereby this right is limited by the fact that the works council can only withhold consent for few, clearly defined reasons (Section 102 of the Works Council Constitution Act (BetrVG)). These grounds include, e.g. failure to duly advertise a position in the company, contravention of the law or company agreements and the violation of company regulations.

[6] Under certain circumstances, the claim of continued employment can also be successfully asserted without an appeal through the works council, e.g. if the dismissal is obviously illegal (cf. Federal Labour Court, Greater Senate ("großer Senat") decision of 27.02.1985, Az.: GS 1/84, BAGE 48, 122-129).

[7] Social plans can only be concluded in companies with a works council and in which a specific percent of the employees are to be dismissed due to changes in the company (Section 112, 112a of the Works Council Constitution Act (BetrVG)). Social plan termination payments are therefore almost exclusively paid by large companies. Termination payments are negotiated for the complete social plan and not for those affected individually, cf. on this subject Fn. 28

continue the employment relationship.[8] The newly introduced Section 1a of the Employment Protection Act (KSchG) recognises an “entitlement“ to compensation only when the employer indicates in the notice of dismissal that the dismissal is due to operational grounds and offers compensation on expiry of the term in which legal action can be filed. Sometimes reference is made to Section 1a of the Employment Protection Act (KSchG) as having introduced a “right to compensation” (Marczynski 2004; Spieß 2004). However, a right as such is not provided by the regulation. It is an improvement to the extent that if this compensation is accepted, a period of ineligibility for unemployment benefits is not imposed.

Where appropriate, the dismissed person can file a complaint with the Labour Court within a term of three weeks. In contrast to conditions in other European countries, this comparatively short deadline for lodging a complaint[9] increases the company’s legal security. The court usually suggests a compromise with – or also without – compensation or ends the conflict with a decision (3c). Costs are incurred for legal representation in all cases before the Labour Court, given that legal representation is used.[10] If the employer loses the case, the employment relationship is not ended by the dismissal so that the obligation to pay wages continues, even if the employee has been released from duty (backpay).[11] If the dismissal was legally justified, then it is implemented as planned under observation of the term of notice. (3d). Ultimately, the conduct of both parties and the company culture decide the enforceability of employer-initiated dismissal.

3. The three levels of action in company reality

The events involved in terminations within the German employment system can be partly investigated through research by the Company Panel of the Institute for Employment Research (IAB Betriebspanel), which conducts an annual survey of 15,000 companies of all size and from all branches. The survey is representative and

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8 Although the labour courts have a very narrow interpretation of the prerequisites for this provision (Section 9, Para. 1, Sentence 1 of the Employment Protection Act (KSchG)).

9 Even in Great Britain, the term within which an appeal can be lodged against dismissal is three months. Only in Austria, where a regulation for severance pay applies, is this term shorter and amounts to only one week (Zachert 2004).

10 Before the Labour Court – in contrast to ordinary courts – each party must carry the costs of their own lawyer, regardless of whether they win or lose (Section 12 a Labour Court Act (ArbGG)).

11 By dismissal on urgent operational grounds, it is in the employer’s interests to release the dismissed worker from duty because the fact of their continued engagement makes it more difficult to prove that the position has become redundant. The company’s financial risk increases with the duration of the labour court proceedings. Companies that are well informed about labour law usually dismiss the employee again under other grounds during the proceedings in order to minimise the risk of having to pay backpay.

therefore reflects the structure of the 2.1 million companies in Germany. Analyses of the IAB Panels are used here, above all to test the reliability of our special surveys.[12] However, his data set contains very little information about specific termination procedures.

The Institute for Economic and Social Research (WSI) at the Hans Böckler Foundation therefore conducted a survey of persons and a survey of companies in cooperation with Infratest, Munich, to investigate events associated with termination. The "WSI Survey on the Termination of Employment Relationships" provides, above all, person-related information about how the employment relationship was ended. This involved questioning 2,407 persons in 2001, whose employment relationship had ended within the questioning period.[13]

With the "WSI Survey on Company Personnel Policies" in 2003, information was gathered about the application of the Employment Protection Act. It was based on a representative survey of persons with personnel responsibility in 2,000 private companies.[14] The table below differentiates according to company size where possible. For this purpose, we divided the companies into size classes and in keeping with the definition of the European Union used the following designations: "Small and medium-sized enterprises" (SME) for all operational units/companies[15] with up to 249 employees; broken down into: "smallest companies" for companies with up to 10 employees, "small companies" for companies with 11 to 49 employees and "medium companies" for those with 50 to 249 employees. "Large companies" in contrast are those with more than 250 employees.[16]

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[12] The IAB-Betriebspanel data used here excludes public sector data because personnel policy in this area is atypical. As such, all Betriebspanel data refers only to the private economy.

[13] The survey period lay between September 1999 und November 2000. A prerequisite was the respondent had terminated an employment contract during this period, either through dismissal or because they had quit, through dissolution of the employment contract or through expiry of a fixed term contract. The results of this survey were published in (Bielenski et al. 2002; Bielenski et al. 2003; Bothfeld/Ullmann 2004, Schneider/Ullmann 2006).

[14] The survey instrument used was the computer-supported telephone interview. This instrument guarantees high quality data, partly because fewer questions are left unanswered. The questions especially addressed the company's behaviour in relation to hiring and dismissals over a 5-year period (Summer 1998 to the summer of 2003). The results of this study were published in Pfarr et al. (2005).

[15] These two terms have different meanings in legal discussion and their use here is not equivalent to their use in legal dogma, since the empirical basis of the data typically relates to operational units and not to companies.

[16] Since no turnover data was available, we abstained from classifying the companies, according to EU definition, using this criteria. However, research by the Institute for Small and Medium Size Enterprises, Bonn (IFM) shows that the additional criteria of turnover does not significantly alter classification according to size (Institut für Mittelstandsforschung 2006).

3.1 The relevance of termination of the employment relationship in the German employment system

The exact number of employment relationship that are terminated annually is not documented in official statistics and can therefore only be approximately reconstructed using supporting indicators. For example, the Federal Employment Agency (Bundesagentur für Arbeit) counts around 7 million entries to and departures from unemployment per annum,[17] whereby less than half of these (2006: 43 %) were previously in active employment[18]. From the WSI Survey on the Termination of Employment Relationships (2001), it can be taken that of all persons whose employment relationships ended within the survey period approximately half registered as unemployed (Pfarr et al 2005: 45). If only half of the terminations were recorded through registration as unemployed and approximately half of the new unemployment registrations come from paid employment, then the total number of terminated employment relationships is probably in the order of 7 million per annum.

Choice of Termination Form

Employer-initiated termination competes with other personnel policy instruments and accounts for approximately a third of regular employment contract terminations. Calculations from various data sources estimate the employer share of terminations at 32% (Bielenski et al. 2003). The SOEP 2003 attributes a share of only 26% to employer dismissals, or 36% with the inclusion of terminations associated with the cessation of business (on the problems of the individual data sources, cf. Bielenski and Ullmann 2005). This demonstrates relative stability when compared to the results of a representative survey of around 2400 companies in the private economy in 1987, in which the share of employer-initiated terminations lay at 27% (Büchtemann 1990: 402). Nevertheless the share of employer terminations and own termination correlates with the economic situation, as shown in Tables 1a to 1d. While the German economy was doing well from 2000 to 2002, recession began in 2003 and continued until 2005. The share of employer-initiated terminations rose from 23% in 2000 to 33% in 2003, before sinking once again (Table 1a). In contrast, the share of employee-initiated terminations dropped from 42% in the year 2000 to 26% in 2005 (Table 1b).

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[17] Bundesagentur für Arbeit (Federal Employment Office) (2006) The Labour Market in Figures, Status: December 2006, http://www.pub.arbeitsamt.de/hst/services/statistik/200612/iiia4/akt_dat_jzd.pdf.

[18] cf. Bundesagentur für Arbeit (2004).

During the same period, the number of unemployed increased by around a million persons. Apparently the inclination of employees to give up their jobs is lower in times of high unemployment than during times when labour is in higher demand. Worker's reduced mobility during difficult economic times increases the significance of termination by the employer since the decline of departures of employees reduces the company's flexibility.

Tables 1a to 1 d: Share of personnel departures between 2000 and 2005 according to the nature of termination (as % of all terminations)[19]

Table 1a: Employer Termination

Employer Termination	1 to 5	6 to 10	11 to 19	20 to 49	50 to 99	100 to 249	>= 250	Total
2000	30%	26%	29%	21%	23%	20%	15%	23%
2001	36%	36%	32%	30%	24%	24%	13%	26%
2002	40%	37%	31%	31%	32%	28%	14%	29%
2003	47%	34%	37%	38%	34%	31%	18%	33%
2004	46%	38%	39%	33%	31%	31%	15%	31%
2005	48%	37%	34%	32%	28%	27%	18%	31%

Source: IAB-Betriebspanel, excluding public services, weighted results.

Table 1b: Own Termination

Own Termination	1 to 5	6 to 10	11 to 19	20 to 49	50 to 99	100 to 249	>= 250	Total
2000	40%	44%	43%	49%	49%	44%	34%	42%
2001	30%	35%	45%	41%	49%	40%	35%	38%
2002	27%	33%	40%	38%	34%	33%	29%	33%
2003	25%	41%	36%	29%	30%	24%	24%	29%
2004	25%	32%	31%	31%	30%	22%	22%	27%
2005	22%	33%	30%	29%	27%	25%	22%	26%

Source: IAB-Betriebspanel, excluding public services, weighted results.

[19] Terminations due to the completion of training, retirement and "other causes" (i.e. termination due to occupational disability and relocation to other companies) are not shown here.

Table 1c: End of Fixed Term Contracts

Fixed Term	1 to 5	6 to 10	11 to 19	20 to 49	50 to 99	100 to 249	>= 250	Total
2000	5%	4%	3%	7%	9%	13%	19%	10%
2001	5%	6%	4%	6%	9%	16%	22%	11%
2002	5%	3%	4%	9%	12%	16%	26%	13%
2003	5%	5%	3%	11%	17%	17%	21%	12%
2004	4%	5%	7%	14%	11%	22%	26%	15%
2005	3%	5%	9%	14%	18%	23%	21%	14%

Source: IAB-Betriebspanel, excluding public services, weighted results.

Table 1d: Dissolution

Dissolution	1 to 5	6 to 10	11 to 19	20 to 49	50 to 99	100 to 249	>= 250	total
2000	4%	5%	4%	4%	4%	6%	9%	6%
2001	6%	3%	5%	4%	5%	5%	8%	6%
2002	6%	6%	4%	4%	6%	7%	9%	6%
2003	4%	4%	6%	5%	6%	9%	10%	7%
2004	4%	6%	4%	4%	5%	6%	10%	6%
2005	4%	5%	2%	5%	8%	6%	11%	7%

Source: IAB-Betriebspanel, excluding public services, weighted results.

These results require differentiated interpretation on another count. Considering the nature of termination according to company size class shows that employee-initiated terminations are of much greater significance in small companies than in large companies with more than 250 employees. In contrast, large companies use the option of fixed-term employment to a much greater extent than the small company classes with up to 50 employees. These size related differences are contingent on at least two factors. Firstly, the staff turnover in the smallest companies is markedly higher than in large companies (Bielenski et al. 2003; Erlinghagen/Knuth 2003), so that the need for employer-initiated termination is much more probable in large companies simply as side-effect of size. At the same time, the smallest companies have access to fewer alternative instruments for reducing personnel, whether because they lack the knowledge and practice in relation to labour and social legislation, or because their internal flexibility is limited. For example, in 2003 only 2.1% of all companies engaged temporary workers to the key date 30.6. compared to 36% of companies with more than 250 employees.[20] The use of fixed-term

[20] Source: IAB-Betriebspanel 2003, excluding public services; own calculations, weighted results.

employment, also increases with company size (Düll/Ellguth 1999: 173; see also Hagen/Bookmann 2002). At the same time, large companies use dissolution contracts more often than smaller companies. We don't know the content of these contracts. There is no data available, but it can be assumed that large companies often agree to severance payments in dissolution contracts. Nevertheless, the data shows that companies don't use dissolution contracts more frequently in economically difficult times. Apparently they manage to dismiss the employees they no longer require.

Termination Initiative

Die relative significance of employer-initiated termination doesn't support any conclusion about the concrete events involved in the termination. In fact, it could be part of company strategy to call on employees to quit themselves when necessary or to offer a dissolution agreement. In that case, not the formal execution of termination but rather the *initiative* to end the employment relationship would be crucial. The results of the WSI Survey on the Termination of Employment Relationships (2001) show that more terminations were initiated by employers (44%), than by employees (32%; Table 2). If one considers the form of termination by initiative, it becomes apparent that the employers who want to separate from employees rely on employer-initiated termination in only 58% of cases and let fixed-term contracts expire in 32% of cases. At 8.5%, dissolution agreements are relatively infrequent in employer-initiated terminations[21], and the situation where employees quit in response to the employer's initiative was also found to be rare, with a share of only 2%.

Among employees, the share of self-initiated terminations (49%) is also greater than the share of own terminations (39%). In most cases (75%) employees who wanted to end their employment relationships decided to quit however, some managed to conclude a dissolution agreement (11%), with their employer and only a few (6%) had their employer dismiss them.

[21] In this analysis no distinction was made between whether the agreement was made out of court or on the basis of a compromise suggested by the Labour Court.

Table 2: Initiative and form of termination during the period 9/1999-11/2000 (in % of respondents)

	Total	Proportion: by formal type of termination (Row percentages)				
			Termination by Employer	Termination by Employee	Dissolution	Fixed Term
Formal nature of termination	100 (2394)		32 (758)	39 (930)	10 (242)	20 (464)
Employer Initiative	44.0 (1178)	100	57.5 (605)	1.8 (19)	8.5 (90)	32.2 (339)
Employee Initiative	49.2 (1053)	100	6.2 (73)	75.1 (885)	10.8 (127)	7.9 (93)
Mutual Initiative	6.8 (163)	100	49 (80)	16 (26)	15.3 (25)	19.6 (32)

Source: WS Survey on Employment Relationships 2001; own calculation. Weighted share in percent, unweighted no. of cases in brackets; Details of mean deviation are available on request.

Around 7% of all terminations resulted from the joint initiative of the employee and employer. In half of all cases the employer issued the termination; dissolution agreements were only seldom negotiated (15.3%).

During the survey period, employees quitting on their own initiative represented the most frequent case (37% of all terminations); the terminations initiated and issued by employers followed in second place with 25%. The third largest group was formed by fixed term contracts concluded on the employer's initiative (14%). As such, employer-initiated termination stands in competition to the instrument of fixed-term contracts when it comes to the adjustment of personnel resources, but also to finding a common solution with the employee. In view of the high share of terminations by employees, it should be considered that the positive labour market development during the survey period (Autumn 1999 to Autumn 2000) had a positive influence on the number of employee-initiated terminations. In contrast, an increase in employer-

initiated terminations is to be expected during times of increasing unemployment (cf. Table 1a).

3.2 The application of employment protection legislation in company practice

Section 2.3 presented the spectrum of theoretical options for action that companies have at their disposal to reduce their personnel. In the previous section, it was shown that employer-initiated terminations represent only a small part of the total terminations. In this section, we will illuminate the individual stages of action in an employer-initiated termination and attempt to illustrate their relevance in practice using available empirical material.

Inquiry into legitimacy and the term of notice

Minimum employment protection[22] and the terms of notice of termination are regulated in the German Civil Code (BGB), which applies to all companies. The statutory term of notice of termination for employers depends on the employee's tenure and is first set at over 6 months for tenure of more than 15 years. Aside from this, a probationary period of up to six months can be agreed to, within which the employment relationship can be terminated with two weeks notice (Section 622 III BGB). However, the statutory terms of notice are fully subject to collective wage agreements so that they can be lengthened or shortened by collective regulations.

A "special dismissal protection" that precludes the statutory notice of termination can be agreed to in collective wage agreements. This is usually coupled with the achievement of a specific age and duration of tenure in the company (WSI 2003).[23]

Special legislation prohibits issuing notice of termination to pregnant women, mothers for 4 month after giving birth and employees on parental leave, and to members of the works council, youth trainee representatives and disabled persons.[24] However,

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[22] According to the jurisprudence of the Federal Constitutional Court (BVerfG), the general clauses of civil law (Section 242 of the German Civil Code (BGB) – In good faith, and § 138 – Immoral Transactions) provide the basis for minimum protection from arbitrary dismissal (Federal Constitutional Court judgement of 27.01.1998, Neue Zeitschrift für Arbeitsrecht, Issue 9, 1998, p.470).

[23] According to the jurisprudence of the Federal Constitutional Court, should continued engagement be absolutely impossible, e.g. because the entire company closes, employees under special dismissal protection can also be dismissed, though with long terms of notice, cf. Federal Labour Court (BAG) judgement of 06.10.2005, 2 AZR 362/04, published under: www.bundesarbeitsgericht.de.

[24] The provisions for special dismissal protection, among other things, regulated by Section 15 of the Employment Protection Act (KSchG), for pregnant women and mothers for the first four months following birth by Section 9 of the Maternity Protection Act (MuSchG), for employees on parental leave and 8 prior to giving

this employment protection is not absolute since the German Civil Code (BGB) provides employers with the right to dismiss any employee without notice "on important grounds" (Section 626 BGB). Government authorisation must be obtained for the dismissal of persons whose employment is covered by special legislation prohibiting termination (for persons with disability: Sections 85 ff. of the German Social Code (SGB IX)). This authorisation can also be granted for the regular dismissal of a pregnant woman or young mother during the four-month period following giving birth if the dismissal has nothing to do with her condition or situation (Section 9, Subsection 3 of the Maternity Protection Act (MuSchG)).

Little is known about the application of these special regulations, the suspension of the special regulations prohibiting dismissal or the number of dismissals issued without notice. The survey results show that the terms of notice are observed in the overwhelming majority of cases: in 83% of cases of employee-initiated termination and in 85% of cases of employer-initiated termination.[25] Whether the non-observance of the terms of notice is due to failure to comply with the statutory regulations or justified termination without notice is unknown. But surely dismissal without notice represents only a small share of all terminations. There is an additional regulation for collective redundancies that requires notification of the Federal Employment Agency (*Agentur für Arbeit*).[26] The *Agentur für Arbeit* can withhold agreement to the planned date of the dismissals and in doing so delay them by one, or in individual cases by two months.

In specific cases of multiple dismissals by companies with more than 20 employees, a social plan must be compiled in cooperation with the works council, given that the company has one.[27] The survey results show however, that dismissals seldom occur within the framework of a social plan: Although 44% of those made redundant

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birth, by Section 18 of the Child Support Payment and the Parental Leave Act (BerzGG), i.e. since 01.01.2007 by section 18 of the Federal Parental Benefit and Parental. Leave Act (BEEG).

[25] Source: WSI Survey on the Termination of Employment Relationships (2001); own calculation, weighted results.

[26] Section 17 of the Employment Protection Act (KSchG) demands notification of dismissals before the employees are issued with notice of dismissal if, within a period of 30 days, a company with between 20 und 60 employees intends to dismiss 5 of them, a company with between 60 and 500 employees intends to dismiss 10 percent or more than 25 employees, or when companies with at least 500 employees intends to dismiss at least 30 of them on urgent operational grounds.

[27] One case where this is required is changes to a company that involve only the dismissal of staff. Section 112a of the Works Constitution Act (BetrVG) also sets thresholds beyond which the formulation of a social plan is obligatory. These are more generous than the thresholds defined for the obligatory notification of dismissals acc. to Section 17 of the KSchG. Here, companies with 55 employees, of whom 6 are to be dismissed, must notify the Federal Employment Agency, but they are first required to formulate a social plan when 11 employees are to be dismissed. The obligation to create a social plan does not apply to companies that have been established for less than four years.

through employer-initiated termination stated that other employees were also dismissed, only 8% indicated that there had been a social plan (cf. also Bielenski et al. 2003: 88).[28]

Justification of termination on operational grounds according to the Employment Protection Act (KSchG)

According to the KSchG, the company must provide the employee with grounds for their dismissal. Especially termination on operative grounds is the subject of discussion about the anti-employment nature of dismissal protection. Conditional to carrying out dismissal on operative grounds is that “urgent operational requirements”, which may result from internal or external circumstances, lead to the loss of one or more positions. The court can only investigate whether the underlying entrepreneurial decision was arbitrary. Once it has been determined which positions have been lost, a social selection must be made between all employees in equivalent positions. It is permitted for preference to be shown to those on whose performance the company relies.

The WSI Survey on the Termination of Employment Relationships (2001) showed that around two thirds (67%) of terminations were justified using operational grounds, only 15% were conduct or person-related and 18% could not be clearly classified[29].

The relationship had reversed since previous research: According to a survey by the Max Planck Institute in 1980, the share of terminations on operational grounds accounted for a good third, while two thirds were attributed to conduct and person related grounds. (Falke et al. 1981). This could be due to the more favourable economic situation at that time. However, it is also possible that operational grounds are being pushed to the forefront today because conduct and person related dismissals can be more difficult to ground (on this subject, cf. also Jahn/Walwei 2005). Data from the KÜPRAX research project shows that terminations on operational grounds stand up in court more often than conduct related terminations. Employers lose cases based on conduct related grounds significantly more often

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[28] However this provides no indication of how many dismissals are carried out each year within the context of a social plan. Firstly, the employees are not always well informed – around 14% of respondents stated that they didn’t know whether a social plan had been concluded - and above all, the information relates to a survey period of 15 months (September 1999 to November 2000) so that an annual value for the year 2000 cannot be calculated.

[29] Of dismissals against which an appealed was lodged before the Labour Court in 2003, 56% were due to urgent operational grounds (LAG: 44%), 32 % were conduct related (LAG: 44%) and 7 % were person related (LAG: 12%), cf. {{Höland et al., 2007: 282, 286}}

than those based on operational grounds: In judgements related to dismissals on operational grounds, the dismissal was found to be invalid in the first instance in 55 % of the cases (State Labour Court (LAG): 46%), and in conduct related dismissals, in 68 % of cases (LAG: 55%) (Höland et al. 2007: 144 f.)

The WSI Survey of Personnel Policies showed that a third (33%) of all respondent companies had gained experience with dismissal on operational grounds during the previous five-year period (1998 – 2003)[30].

Questioned about the greatest problem that the company had faced with dismissals on operational grounds, almost a quarter (24%) of the companies stated that they had experienced no problems – although "no problems" was not one of the optional answers provided. A quarter (27%) of the companies had difficulty in presenting the operational grounds, a further quarter (24%) mentioned the loss of key performers and 9% cited conducting the social selection as a problem. Overall, no differences could be identified between the company size classes – with one exception: Companies with up to 19 employees stated more frequently that they had experienced no problems with dismissals on operational grounds (cf. Pfarr et al 2005: 56). In court proceedings, social selection also appeared to lack the importance ascribed to it in the literature: Only 8% of all dismissals on operative grounds were deemed invalid by the Labour Court or Regional Labour Court due to deficient social selections (Höland et al. 2007: 123).

Works Council involvement in terminations

If a works council exists, it must be heard before the notice of dismissal is issued; this means that it must be informed about the person to be dismissed and the grounds for dismissal. If the works council has reservations, it can object to the dismissal within a week and in doing so must provide grounds for the objection. However, the objection is only legally relevant if legal action is initiated since then the employee has the right to continued employment until the proceedings have been concluded.

According to calculations of the IAB-Betriebspanel, companies with a works council are in the minority: In 2004, only 13.5% of all companies with more than five employees had a works council[31]. Nevertheless, around half of all employees (in West Germany 53,5%, in East Germany 47%) work in companies with works

[30] WSI Survey on the Termination of Employment Relationships 2001; own calculation.

[31] Source: IAB-Betriebspanel 2004, weighted results.

councils. Qualitative research has revealed that there are various patterns of internal company cooperation between employers and the employee representatives and that some of the works councils function effectively as “co-managers” (Bradtke et al. 2004) and the cooperation between the personnel managers and the works council is often judged to be good to very good (cf. de Santana 2005: 375).

In the WSI Survey on the Termination of Employment Relationships (2001), most (60%) dismissed employees from companies with an active works council stated that it had been informed of the dismissal. This represents a quarter of all employer-initiated terminations (25.7%).[32] Of those works councils that were informed, only one in ten objected to the dismissal. It came to legal action in half of the cases where the works council had placed an objection.[33] The results of the KÜPRAX project showed that in the cases in which a works council was present, they expressed misgivings about the dismissals, i.e. objected to them in 35% of cases before labour courts and in 38% of cases before regional labour courts respectively (Höland et al. 2007: 103). There are indications that as control mechanisms, works councils also have a positive effect on the correct application of labour law: The presence of a works council significantly increases the probability that companies state that they have an overview of labour legislation (Pfarr et. al. 2005: 19). This appears not to be implausible since the works council is available as an additional source of information about labour law and can advise of legal options and limits where appropriate. At the same time, its existence alone is cause for compliance with applicable legislation, which results in the minimisation of conflict.

Knowledge of the law within companies

While the German Civil Code (BGB) and special dismissal protection apply to all companies and guarantee a minimum of protection, the scope of application of the Employment Protection Act is limited and applied only to companies with more than 5 employees until 31.12.2003.[34] Since the 1.1.2004, the Act applies to all new

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[32] In 56.4% of all dismissals, there was no works council; in 12.7% of cases, the respondent didn’t know whether the works council had been informed and in only 4,3% of cases, the respondent reported that the works council had not been informed (WSI Survey on the Termination of Employment Relationships (2001), own calculation; weighted results).

[33] Due to the small number of cases, this data could only be evaluated as an indication and not as evidence. The number of cases that appealed amounted to N=19.

[34] According to Section 23 Subsection 1 of the Employment Protection Act (KSchG), the following employment limits apply: Part-time employees working up to 20 hours count as only a half, and part-time employees with up to 30 hours count only as ¾.

engagements in companies with more than 10 employees.[35] In addition, the Employment Protection Act is only applicable to employment relationships that have existed for longer than six months.

In the WSI Survey on Company Personnel Policies (2003) companies were asked about their problems with labour law. Only about a third of companies (31%) answered affirmatively to the question of whether there were problems in maintaining an overview of labour law (Pfarr et al 2005: 13). That two thirds of the companies reported that they have no problems with labour law does not mean however, that they know and apply the law; it is equally possible that they don't know it and don't apply it and therefore have never had a problem[36]. An indication of this situation is provided by the finding that particularly many of the smallest companies have no exact knowledge of the law since just under two thirds (64%) of the respondents from companies with five or less employees didn't know that the Employment Protection Act (KSchG) did not apply to them (for detailed information, cf. Pfarr et al. 2005: 27 ff.). A multi-variant analysis found that alongside the existence of a Personnel Department, a works council and long-term personnel planning, the economic situation has a highly significant influence on whether companies stated that they were unable to understand labour law (Pfarr et al 2005: 20 f.). It follows that a systematic examination of the law, whether for reasons of long-term planning or internal expert knowledge (Works council or Personnel Department), increases the chance that an employer does not find labour law too complex. On the contrary, the fact that the economic situation has a highly significant influence indicates that the respondents interpreted the problem of understanding of labour law as a problem with the labour law. Finally, only qualitative research can deliver information about the way those responsible for personnel deal with labour law. The realm of personal motivation for action cannot be adequately described through quantitative data, which is why these results can only be considered first indices.

Another interesting question is that of how companies procure their information.

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[35] Cf.. Federal Gazette, Part I 2003, No. 67, 30.12.2003, p. 3002.

[36] A Bertelsmann Foundation project (Öwar) discovered that a large proportion of the population estimates its competence in labour law as good, but that the real knowledge of labour law is poor. The project report can be found here:
http://www.arbvg.de/downloads/Empirische%20Studie%20zur%20Oeffentlichen%20Wahrnehmung%20des%20Arbeitsrechts.pdf

Table 3: Knowledge and assessment of labour rights (in %)

	Total	By Company Size Categories					
		1-5	6-9	10-19	20-99	100-499	500 +
Does the company have the support of a Personnel	17,9 (889)	9,2	20,4	33,3	58,3	93,1	100,0
Which external services are used for consultation on labour law?							
Lawyer	47.7 (1143)	39.8	60.4	62.0	77.5	80.0	50.0
Accountant	75.3 (1281)	76.8	78.7	71.1	69.5	41.4	25.0
Chamber	43.5 (821)	42.3	52.8	44.3	42.4	31.0	25.0
Employers Association	21.8 (799)	16.0	23.9	35.0	45.0	69.0	75.0
Federal Employment Office	26.4 (670)	22.4	32.5	34.4	39.7	48.3	50.0
Other services	12.7 (400)	10.1	14.5	21.7	18.5	31.0	50.0
Did the company refrain from dismissal?	8.9 (435) /21.2* (408)	3.7	12.8	18.9	32.7	37.9	50.0

Source: WSI Survey on Company Personnel Policies (2003), own calculations; weighted shares in percent; Unweighted no. of cases in brackets;

* Excluding small companies that are exempted from the Labour Protection Act.

If two thirds of the smallest companies do not know that the Employment Protection Act does not apply to them, this is presumably also partly due to the available sources of information. Indeed, Personnel Departments are seldom found in the smallest companies. An average of 18% of all companies have access to a Personnel Department either within in their own company or in a parent company; over half the companies with over 20 employees and almost all companies with more than 100 employees have this infrastructure (cf. also the findings of (Alewell 2002). The question of whether and as the case may be, which positions in the company take advantage of an external consultation on labour law resulted in a very different

pattern of information procurement for the various company size classes. Smaller companies frequently received their advice on labour law from the accountant, in larger companies this advice was more likely to come from a lawyer. Small companies tend to consult the Chamber of Commerce while large companies are more likely to consult employer associations.

The Federal Employment Agency provided advice to approximately a quarter of all the companies (26%), whereby the share of large companies is distinctly higher here. This is possibly due to the regulations for mass dismissal or the implementation of labour market policy instruments.

Alternatively, knowledge of labour law also comes from experience with personnel policy instruments. Interestingly however, this experience does not lead to labour law being considered clearer. Rather, awareness of the existence and complexity of labour law first emerges with its application. It therefore appears plausible that companies that have experience with terminations on operational grounds and fixed-term or temporary personnel more often reported that it was difficult to gain an overview of employment legislation (Pfarr et al. 2005: 18 f.). A systematic examination of the law, independent of an instance of conflict would presumably lead to a positive approach to the law: this is supported by the finding that those companies that responded having access to internal expert knowledge or maintaining a long-term personnel plan less frequently found the law too complex (ibid.: 19).

Refrainment from Dismissal

Ultimately the question is posed of whether the feeling of legal uncertainty – arising from concrete experience – leads to reluctance in dismissals. In the WSI Survey on Company Personnel Policies (2003), those responsible for personnel were therefore asked retrospectively about their actual behaviour, namely the refrainment from dismissal and asked about the continuation of those affected in their positions.[37] Around 9% of all companies reported to have considered dismissal at least once but then having refrained from doing so. In the smallest companies (with up to five employees), in which dismissals occur most frequently, this occurred in only 4% of cases. If the smallest companies are excluded from the population, the average lies at 21%. Although in all, only few employees were affected[38] and not every

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[37] The wording of the question was: “Have there been cases, since the beginning of 1998, in which dismissal was considered but not carried out due to fear that the dismissal could not be enforced?“

[38] On average, there were three cases where dismissal was abstained from during the five-year period from 1998 to 2003 in companies with 20-99 employees, five cases in companies with 100-499 employees and 14 in

refrainment from dismissal led to permanent continued employment: Nevertheless 78% of respondents (all company sizes) reported that it resulted in continued employment in least in some cases[39], 21% reported that the employees (among others) had quit themselves, and 12% reported that they had sometimes concluded dissolution agreements.

In respect to company size, it is conspicuous that the occurrence of employee-initiated termination in such cases was, with 35%, clearly of above-average frequency in small companies with between six and nine employees and the share of companies that concluded dissolution agreements clearly increased with company size.[40]

3.3 Cost of Terminations

According to the principles of the German Employment protection Act, companies incur no costs through lawful dismissals – aside from the requirement that they observe the term of notice. However literature and the press advance the idea that employers must regularly "buy themselves free" of employees because the dissolution of the employment relationship is otherwise hardly possible due to the complexity of the law and legal practice.

Termination Payments

The WSI Survey on the Termination of Employment Relationships (2001) found that termination payments were seldom paid, on average in only 10% of all terminations (Table 4). In the case of dissolution agreements, through which every tenth employment relationship was terminated, a severance payment was made in one third of the cases (n=62). Severance pay was provided in only 15% (n=133) of employer-initiated terminations. Overall, terminations in small and medium sized companies are much less often accompanied by severance payments than those in large companies. Only 5% of employees from companies with less than ten

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companies with 500 employees (WSI – Survey on Company Personnel Policy 2003, own calculation; weighted results). The reasons for not carrying out these dismissals could not be determined for methodological reasons.

[39] Since it was only asked "what happened to the employees concerned", multiple answers were possible where several dismissals had been avoided so that an exact assignment of outcomes to the individual cases was not possible.

[40] Greater differentiation was not possible due to the small number of cases (For further findings, see Pfarr et al. 2005, p. 82 ff.).

employees received severance pay following dismissal, while in large companies severance pay was received by 38% of dismissed employees.

Table 4: Frequency of severance payments by company size (in %)

	Total	1-9	10-49	50-199	200-499	500 +
All terminations	9,8 (223)	3,1	9,4	7,3	15,2	25,4
Employer dismissals only	14,8 (133)	5,2	15,4	19,2	29,9	38,0

Source: WSI Survey on the Termination of Employment Relationships, own calculations, weighted share values in percent; unweighted no. of cases in brackets.

The conclusion of a social plan or legal action against the dismissal increases the probability that a termination payment will be made but there is no guarantee: a termination payment was received in 75% of cases where dismissal occurred within the context of a social plan. Of those persons who took legal action against their dismissal, 47% received severance pay (cf. Pfarr et al. 2005: 72; for termination payments by labour court action proceedings, see also Höland et al. 2007: 154 ff).

In addition, broader analyses show that tenure is the most important condition for determining whether a termination payment is made at all: Termination pay is almost never paid in cases of dismissal following a tenure of less than two years and only after tenure of 20 years does every second dismissed employee receive a termination payment (Bothfeld/Ullmann 2004). Surprisingly, age plays no role: although more older employees receive termination payments, the decisive criteria is the length of tenure and not the age itself (Schneider/Ullmann 2006: 16, 20). In determining the sum of the termination payment in cases where the parties amicably agree to terminate the employment relationship in exchange for severance pay, the courts sometimes apply the so-called “rule of thumb“ according to which half a month’s salary is paid for each year of tenure.[41] However, in addition to the main criteria, company tenure, the courts also take the action’s prospects of success and the company’s economic situation into consideration in formulating their suggestion (Höland et al. 2007: 158). The nature of termination also plays a role: Compensation

[41] The so-called rule of thumb has been adopted in Section 1a of the new Employment Protection Act (KSchG). However, this section does not forbid compensation solutions in which higher or lower termination payments can be made.

for termination is most often paid in dismissals that are person related or due to operational requirements (Höland et al. 2007: 164).

In a third (30%) of settlements fixed by the Labour Court and in half (55%) of those fixed by the Higher Labour Court, a “certificate of mutual release” was also accorded, which means that the parties agreed that the compromise satisfied all claims arising from the employment relationship, including any possible backpay. (Höland et al. 2007: 154). Astonishingly, whether or not an action had been filed had no influence on the amount of the termination payment although, in the event of successful legal action, the employer runs the risk of having to pay backpay. On average, termination payments – whether they are settled in or out of court – are oriented on the previously mentioned Labour Court rule of thumb of a half month’s wages for each year of tenure (Pfarr et al. 2005: 74), and on average, higher termination payments are only achieved before the Higher Labour Court, (Höland et al. 2007: 160).

Frequency of legal action

The results of the two WSI surveys are the only sources based on current representative surveys and that allow a reliable calculation of the frequency of legal action. The last study in the context of which the frequency of legal action by dismissed employees was reliably calculated comes from 1978/1981 and found a frequency of 8% – in an, at that time, good economic situation (Falke et al. 1981). Other frequencies of legal action have been calculated recently but they are based on an unreliable data source (Jahn/Walwei 2003; Jahn/Schnabel 2003b; Bonin 2004; Jahn 2004). The – in contrast relatively reliable – results of the WSI Survey on Company Personnel Policies (2003)[42] show that the overall rate of legal action lies at about 15% and increases with company size (Table 5). While in companies with over 500 employees, according to those with personnel responsibility, legal action is taken against a good quarter of dismissals[43], the rate was only 7% in companies with up to 5 employees.

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[42] The WSI Survey on the Termination of Employment Relationships (2001) found an appeal rate of 11%.

[43] Here, it must be taken into consideration that the number of lawsuits in large companies over five years was often estimated and it can be expected that court proceedings, as a markedly negative event, is overestimated over a long period.

Table 5: Frequency of legal action by company size during the period 1998 to 2003 (in percent)

	Total	1 - 5	6 - 9	10 - 19	20 - 99	100-499	500+
Rate of legal action* (weighted)	15 (8490)	7 (66)	13 (78)	13 (195)	23 (687)	24 (1522)	28 (5942)

Source: WSI Survey on Company Personnel Policies (2003). Weighted share values in percent; unweighted no. of cases in brackets. * defined as the share of complaints against employer-initiated dismissal.

The low rate of legal action in the smallest companies possibly arises from the situation where the closer relationship between employer and employees holds the employee back from initiating action, and perhaps also because they hope to be reinstated should the economic situation improve. The reasons for dismissal on urgent operational grounds are possibly also more transparent for employees in small companies or the knowledge of a precarious financial situation in the smallest companies restrains the employees from legal action out of loyalty.

If legal action is filed, the court investigates whether the legal requirements are satisfied. If neither the Employment Protection Act (KSchG) nor provisions for special dismissal protection are applicable, the court only decides whether the dismissal represents a breach of general clauses under civil law. The law court statistics make it clear that the possible costs incurred as a result of the duration of the proceedings (obligation to pay backpay) are small since two thirds of all proceedings are finalised, at the latest, within three months (25% after one month, a further 41% after 1-3 months). Only 2% of cases take more than a year. In the great majority of cases, the proceedings are then also finalised: An appeal is lodged against only around 4% of cases.[44] The data from the KÜPRAX project shows that the proceedings are shorter when the parties are not represented (Höland et al. 2007: 192). In addition, should the employer refuse to pay backpay, this must also be legally enforced. Specific expiry deadlines, which are defined in the employment contract or collective

[44] The Federal Ministry of Economic Affairs and Employment calculates statistics on the work of the labour courts each year and makes these available to the State Labour Courts via the responsible State Ministries. Publication of the results, including those of the individual states, takes place later in the Bundesarbeitsblatt. (cf. Statistics of labour court jurisdiction, summarised averages for the years 1999 to 2003. The rate of appeal relates to the year 2001; http://www.arbeitsgerichtsverband.de/Statistik%20ArbGe.htm, Accessed on 15.11.2004.).

agreement, apply here. Winning the employment protection case alone does not create an entitlement to backpay (cf. on this subject Schier 2006).

Results of the Proceedings

The majority of Employment Protection cases before the Labour Court (65%) ended in a compromise (Höland et al. 2007: 139): In 1978, this share already lay at 60% (Falke et al 1981, p. 481). Only around 11% of the dismissal cases before the labour courts and approx. 30% of dismissal cases before the higher labour courts ended in a disputed judgement (Höland et al. 2007: 139). Not every court compromise is accompanied by termination payments. Only in approx. ¾ of all court compromises was, among other things, a severance payment agreed upon (Höland et al. 2007: 160). The dismissed employee's claim that the dismissal breached the law was upheld in only 6% of cases (Höland et al. 2007:). In these cases, the employment relationship continued. It is unknown whether these employment relationships continued enduringly or whether they were terminated at the next possible opportunity. On the other hand, it is also possible to secure continuation of the employment relationship through a consent decree or a compromise. The KÜPRAX project researchers came to the conclusion that the employment relationship continued (at least in the first instance) in approximately 15% of all dismissal disputes, excluding those involving public servants, in 2003 (Höland et al. 2007: 204).

4. Conclusion

The action taken by companies is determined by a multitude of factors. Labour law is only one of them. Macroeconomic studies cannot show the complexity of company decisions or the interaction between the various factors of influence. There is no single "best personnel strategy" for all companies: a short-term personnel strategy that accepts conflict can be just as worthwhile as a long-term, amicable strategy. Therefore, the law does not prescribe a single, obligatory action. On the one hand, legislation allows various options for action; on the other, there are various ways of dealing with the law.

Quantitative surveys show that termination by the employer accounts for only a third of all terminations – depending on the overall economic situation. These are usually implemented without conflict. Severance payments are rare. Most cases before the labour courts result in a compromise and the duration of labour court proceedings is exceptionally short. Continued employment following notice of termination occurs in only very few cases. Companies seldom shy away from issuing terminations.

Consequently, the overall picture indicates that companies incur few costs as a result of the Employment Protection Act. It is therefore unlikely that altering the Employment Protection Act would lead to the creation of new positions. On the other hand, the data makes it clear that companies have limited knowledge of the law. Above all, small companies rely on an accountant rather than a lawyer when it comes to problems with labour law regulations. In contrast, many of those who are responsible for personnel report having no problems with labour law. However, this is due to the fact that they don't (have to) use it rather than that they have profound knowledge of the law.

In all, it is clear that companies cannot implement German Labour Law 1:1, as assumed by neoclassical theory, because many of them lack the knowledge of labour law. In addition, labour law may not even be required to solve many problems. It follows then, that all economic models that present the law as an influential factor suffer the following flaw: They cannot model the company decision-making process and therefore don't know what influence law has in the companies. As such, they portray only a picture of the written law and not how labour law is lived.

In addition, the economic and regulatory perspectives focus on the negative effects of the Labour Protection Act. The positive effects associated with employment security, for example the employees' willingness to acquire company-specific qualifications, the willingness to remain in a company long term and minimisation of the cost of proceedings through the establishment of binding regulations usually remain unconsidered in macroeconomic models.

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