

## 5 Shock-Absorbers Under Stress: Parapublic Institutions and the Double Challenges of German Unification and European Integration

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### **Introduction**

The weakness of the (West) German ‘semisovereign state’ that Peter Katzenstein diagnosed in his book in 1987 was, according to his argument, not as insurmountable a disadvantage as one might have assumed. Quite the contrary: the profile of policy outcomes seemed to suggest that not having an almighty state could actually be an advantage. But the reason for these positive outcomes was not the state’s weakness alone; it was the peculiar combination of a ‘decentralised state’ with a ‘centralised society’ that proved advantageous. It also helped to explain the central puzzle that West Germany presented when compared with similar cases of highly industrialised liberal democracies, namely the tendency towards only incremental policy change and the high degree of policy stability even after changes of government (Katzenstein 1987, pp. 4, 35).

Katzenstein argues that the ‘decentralised state’ and the ‘centralised society’ interact primarily through three ‘nodes’ in the policy network, namely political parties, co-operative federalism and parapublic institutions. In this chapter, the focus will be on the latter – and the question whether (and if so, how) their function in the German political system has changed. For the period since Katzenstein developed his hypotheses about (West) German politics in the mid-1980s has seen momentous changes in the history of the country. Above all German unification, but also further steps in European integration, certainly make it worthwhile to ask how far these developments have affected the ‘parapublic institutions’ that Katzenstein has portrayed as a vital ingredient of German politics.

How have these institutions developed during that period? Did their role change as a result of the challenges mentioned above? Have any structural changes occurred as a result of unification? Did different institutional patterns develop in western and eastern Germany? And

how have any structural changes affected the patterns of interaction of the various actors? These are questions that will guide the analysis of this chapter. The empirical evidence for the analysis will be provided by case studies of three parapublic institutions and the role they have played since 1987. Their selection is guided by the criterion of the 'twin challenge' the German political system faced in the 1990s: that of German unification and European integration. While limiting the analysis in this way has the disadvantage of not allowing any statements about the development of parapublic institutions in general to be made, at least well-founded ones about the institutions covered here will be possible. Given the widely varying nature of these institutions and the contexts in which they operate, it seems unlikely that any generalisations would be possible anyway. Chapters 8 and 9 in this volume consider some other institutions from this class.

The next section will look in more detail into the parapublic institutions and their role in the German political system. The main section of the chapter will offer case studies on the *Treuhandanstalt*, the *Bundesbank* and the *Bundesanstalt für Arbeit*. The final section then offers reflections on the role of these German parapublic institutions 'under stress' in the changing circumstances of the 1990s and the present decade, arguing that their role diminished as their potential to absorb shocks decreased.

### **Parapublic Institutions: Shock-Absorbers in the Political System**

Katzenstein's enumeration of parapublic institutions includes single institutions (such as the *Bundesbank*, the Council of Economic Advisers, the Federal Employment Office and the Science Council), classes of institutions (like the Labour Courts, churches, social-security funds and private welfare associations) and even rather abstract principles (such as co-determination, or *Mitbestimmung*). The term thus summarises a 'heterogeneous set' of institutions, as the author himself admits (Katzenstein 1987, p. 58), that does not map easily onto the categories that German constitutional and administrative law provide.<sup>1</sup> But in spite of the absence of a clear and encompassing definition, they share a

<sup>1</sup> The greatest organisational commonality between these institutions seems to be that many of them are organised under public law, mostly as *Anstalten des öffentlichen Rechts*. Therefore (and particularly in an Anglo-Saxon context) they are often mistaken as 'state institutions'; however, as this chapter will demonstrate, the state's influence on their operation is often quite limited and they operate with considerable independence.

common trait: namely that they bridge the gap between the public and private sectors, and that they carry out important policy functions.<sup>2</sup>

In organisational terms, parapublic institutions are often characterised by participation of the country's highly centralised economic and social interest groups in the affairs of a highly decentralised state. Granting access to policy-making to privileged groups is thus one hallmark of parapublic institutions. But besides this, two further elements characterise parapublic institutions:

- 1 a high degree of autonomy in policy-making (that takes place under the general supervision of the government, but that rules out interfering in details), and
- 2 a high level of expertise (which often surpasses that of the supervising government departments).

While the extent of each of these three elements varies across the parapublic institutions, it is by their *combination* that they manage to achieve positive effects for the political system. These can be described as reinforcing peace between the political left and the political right, thus inducing stability and limiting controversies in policy implementation. Functionally, parapublic institutions thus benefit the political system both in terms of politics and in terms of policy:

- 1 In terms of politics, they shelter governments from shocks by keeping many policy decisions 'at arm's length', thus removing direct accountability (which may have electoral advantages). By fostering compromise between all parties involved, they guard against adversarial politics.
- 2 In terms of policy, parapublic institutions provide continuity, because they are one or several steps removed from government, and are thus unlikely to change policies radically, for instance after a change in government. Smoother adjustment paths and less interruption are likely to result in superior policy outcomes.

To sum up, the delegation of important policies to institutions characterised by a (varying) mix of participation (for privileged groups), autonomy and expertise – parapublic institutions – can create advantages both for the political process and for the policies. By acting like

<sup>2</sup> The delegation of important policy functions to institutions over which the state has no direct control has a long tradition in Germany and dates back to the late nineteenth century (see, most recently, Manow 2002). Prominent examples include social-insurance institutions or placement services, in which tripartite co-operation has long been established between employers, trade unions and government in quasi-corporatist networks.

buffers, these institutions create positive externalities for both political actors and substantive policy decisions.

### The Case Studies

Parapublic institutions fulfilled an important task in the West German political system up to the late 1980s. But how have they fared since? Based upon three case studies, the following section will look into the changes that have occurred in the years since Katzenstein's analysis.

In 1990, German unification was thrust upon a political system unsuspecting and largely unprepared for it. To cope with this challenge, what had seemed to be firmly established standard operating procedures of the political system were changed with amazing ease. New institutions sprang up, and none of them was more symbolic than the agency charged with privatising the, in former times, almost exclusively state-run economy of East Germany, the *Treuhandanstalt*. Not only was this an unprecedented institution in German history, but it also dealt with the problem of privatisation in a way that was unique among the central and east European countries.

The second case study chosen here was perhaps the most famous 'parapublic institution' in Katzenstein's list, and certainly the one that commanded most attention and respect not only in Germany, but also internationally, namely the *Bundesbank*, the country's central bank. It not only played an important role in the process of German unification, but was also totally transformed as a result of European integration. To any observer at the time of Katzenstein's writing in the mid-1980s, it would certainly have appeared completely beyond imagining that fifteen years hence the *Bundesbank's* role in German politics would be completely changed.

Lastly, this section will deal with the Federal Employment Office as an example of a 'normal' case – at least compared with the seismic shifts that created or affected the other two institutions. But this, too, was an institution that faced new challenges as mass unemployment became a fixture of 1990s Germany – another case of a parapublic institution 'under stress'.

#### *The Treuhandanstalt*

If parapublic institutions are associated with tradition in the German political system and with an aversion to policy change, as has been argued above, then the *Treuhandanstalt* (literally the trustee agency), the institution charged with privatising the East German economy, is,

in a way, not a typical case: a temporary institution, alien to many of the core principles of German political and economic governance, it played a central role during a decisive period, namely the four years following unification. But, upon closer inspection, it becomes clear that both organisationally and functionally, this was a typical parapublic institution, albeit a short-lived one built for a very special purpose.

The genesis of the *Treuhandanstalt* (THA) is as unique as the whole institution, for it was conceived of in principle and founded by the last Communist government of the GDR, and charged with the task of safeguarding the 'property of the people' (*Volkseigentum*) in March 1990 (Kemmler 1994, p. 94).<sup>3</sup> After the free elections later that month, the new, democratic government under Lothar de Maizière swiftly concluded a Treaty on Currency, Economic and Social Union with the Federal Republic, to come into effect on 1 July 1990. As part of the agreements, the mandate of the THA was altered in the *Treuhand Act* (which came into effect on the same day); it now required the agency to privatise East German enterprises. The 270 combines (*Kombinate*) were unbundled into some 12,000 joint stock or limited liability corporations of which the *Treuhandanstalt* held all the equity. Together, these firms employed some four million people – or 50 per cent of the total GDR working population of eight million. The sheer size of its holdings gave the THA and whatever it decided to do an immense political weight. It is, therefore, not surprising that it has frequently been likened to a 'shadow government in the east' (*Nebenregierung Ost*) (Czada 1993a, p. 153; see also H. Schmidt 1993, p. 110).

With respect to the three characteristics of 'parapublic institutions' identified above, the *Treuhandanstalt* can certainly be counted as such: it clearly possessed considerable *autonomy* in its actions, provided room for *participation* of organised societal interests (more on which below), and undoubtedly had a high degree of *expertise*.

Organisationally, the *Treuhandanstalt* was of a 'singular character' (Schmidt-Preuß 1997, p. 862): it was from a legal point of view not an enterprise, and it did not act like a state agency (*Behörde*). Located between the public and the private sectors, it was part of both in some respects. Although a corporation of public law (*Anstalt des öffentlichen Rechts*), it was legally empowered to discharge itself of its privatisation tasks according to 'entrepreneurial principles', thus enhancing its autonomy (sections 2 and 7 of the *Treuhand Act*). This autonomy has been compared by observers to that of the *Bundesbank*:

<sup>3</sup> This legacy remained visible throughout the life of the *Treuhandanstalt* because its fifteen regional offices coincided with the administrative structure of the *Bezirke* of the GDR.

The form, variety and scope of its activities give the impression that the *Treuhandanstalt* – like the *Bundesbank* – forms a third level in the federal structures of the State; this third level undertakes, for a limited time period and with technocratic autonomy, tasks – such as monetary policy – that neither the federal government nor the *Länder* are entrusted with. (Czada 1993a, p. 156)

At the top of the organisational structure of the THA was the executive, consisting of the president, the vice-president and six other members who were responsible for the conduct of business. They were appointed and supervised by the administrative council (*Verwaltungsrat*) which consisted of twenty members who had a role similar to the supervisory board of a German joint stock corporation. The members of the council were all appointed by the federal government. It is here that the contacts and networks vital for the fulfilment of the THA's task were represented, namely in members from both the federal and the *Länder* political levels as well as organised societal interests. The federal government appointed two permanent secretaries (*Staatssekretäre*) from the Federal Finance and Economics Ministries as well as one representative from each of the five new *Länder* and the state of Berlin.<sup>4</sup> The remaining representatives primarily came from industry and the trade unions. Here it is interesting to note that the CDU/CSU-FDP federal government appointed no fewer than four high-ranking trade union representatives to the council in order to compensate for the fact that the THA as a corporation of public law was exempt from the regulations concerning co-determination.<sup>5</sup> The council thus represented all the major interests the *Treuhandanstalt* needed to collaborate with in order to fulfil its task; it also allowed the THA to co-opt many important actors (Czada 1993a). In addition, there were advisory councils at each of the fifteen regional offices, comprising representatives of regional societal interests, and the *Bundestag* in October 1990 set up a subcommittee of the Budget Committee to monitor the conduct of the *Treuhandanstalt*.

From a resource and manpower point of view, the *Treuhandanstalt* was a remarkably small operation, with only 4,800 persons being employed at the headquarters and the fifteen regional offices at the peak of its operations in 1993. The latter were primarily charged with the privatisation of small and medium-sized enterprises in their region, while the 'big fish' were dealt with by the headquarters in Berlin. Altogether, the

<sup>4</sup> The seats of Brandenburg, Saxony, Saxony-Anhalt and Mecklenburg-Western Pomerania were filled by the respective minister-presidents themselves, indicating the high priority they ascribed to that task.

<sup>5</sup> The trade union representatives were Heinz Werner Meyer (head of DGB), Hermann Rappe (head of IG Chemie), Roland Issen (head of DAG) and Horst Klaus of IG Metall (Kemmler 1994, p. 199).

THA's task was certainly unparalleled, both in German history, and also in comparison with the other 'transition economies', namely to privatise practically a whole economy. As the title of one of the first academic books on the subject put it, the agency was 'daring to do the impossible' (Fischer et al. 1993). It was also an unenviable task, for its assets were an odd mixture, containing (in addition to the 12,000 firms mentioned above) some 20,000 small retail and catering outlets, 1,900 pharmacies, all East German cinemas, 390 hotels and no less than 62,000 square kilometres of land that amounted to 57 per cent of the whole area of the GDR (Kemmler 1994, p. 175). To arrive at well-founded valuations for these assets was, indeed, to perform an impossible task, especially since the *Treuhandanstalt* (at least initially) was short of qualified staff, and no reliable data on its assets were available. The situation was even further complicated, first, by the collapse of all East German exports to the traditionally strong markets in eastern Europe and Russia (a consequence of currency union with the Deutschmark), and, second, by the recession of 1992 and 1993 (a consequence of the high interest-rate policy of the *Bundesbank*). The gap between reality and the expectations that the Kohl government had raised with its talk of a 'second economic miracle' could hardly have been greater.

Nevertheless, when the *Treuhandanstalt* was dissolved in 1994, after four and a half years in existence,<sup>6</sup> it had managed to sell all but sixty-five firms from its portfolio. A total of 8,444 firms had been sold, and 3,718 liquidated; however, in terms of employment, the results of its activities were about three million redundancies (Kaser 1996, p. 61). Similarly bleak were the results in financial terms: initially, it had been estimated that the privatisation process would yield profits in the range of DM 500–600 billion (€ 256–308 billion). However, in reality, not only was there no profit, but there was a deficit of some DM 275 billion (€ 141 billion), according to figures provided by Federal Finance Minister Theo Waigel in 1994 (Deutscher Bundestag Plenarprotokoll 12/214; see also Kaser 1996, p. 62), a deficit which had to be covered by the taxpayer. So it was no wonder that criticism about the THA abounded: with a view to the job losses, the agency was accused of insufficiently committing itself to active restructuring, and of not pursuing an industrial policy. In fact, all the results had taken place in spite of previously unimaginable injections of public funds: in the Buna-Leuna-Bitterfeld chemicals triangle, only 2,700 jobs remained, although DM 30 billion (€ 15.4 billion) had

<sup>6</sup> Several successor organisations were created, the largest of which is the *Bundesanstalt für vereinigungsbedingte Sonderaufgaben*. Their tasks include the control of the more than 30,000 contracts between investors and the THA, privatisations of public lands and other similar tasks (Turek 1996, p. 666).

been spent since 1990; and a 50 per cent share of Carl Zeiss Jena was sold to its (West) German sister, Carl Zeiss Oberkochen, for the symbolic sum of only DM 1 (€ 0.51) after the THA and the Thuringia *Land* authorities had invested DM 1 billion (€ 510 million) (Flockton 1996, p. 227).

More disinterested observers, such as business consultant Roland Berger, consequently also stated that the THA had done ‘an excellent job’ (Kemmler 1994, p. 20), especially given that it had been, in the assessment of its President Birgit Breuel, ‘absolutely overburdened’ (H. Schmidt 1993, p. 108). Economically speaking, it is difficult to imagine how the *Treuhandanstalt* could have acted in a substantially different manner in principle – although one can always think of better solutions in the case of each individual decision. But the THA was acting under severe constraints – not the least of which were the consequences of the GDR adopting the Deutschmark at an early stage, which resulted in a de facto revaluation of 400 per cent, a markedly different situation from the other transition economies, all of which allowed their currencies to *devalue* (Kaser 1996, p. 64). While East Germans profited from this decision in the short run in terms of the value of their savings and their purchasing power, it became very costly in terms of job losses – particularly for the elderly and the comparatively less well-trained.

From the point of view of the political system, the *Treuhandanstalt* has certainly fulfilled its task very well. On the one hand, given the absurdly complex situation and the level of uncertainty it acted under, it is difficult to imagine any other strategy than one of pragmatic ‘muddling through’ to be appropriate – which is what the THA largely did (Czada 1993a, p. 171). In that sense, the THA, far from being ‘alien’ to the constitutional and institutional system of the Federal Republic (Wollmann 2001, p. 40), was actually rather typical of it. In addition, its special mix of extensive autonomy in each individual privatisation case, access to substantial financial resources and an embeddedness into the multilayered decision structures of the German political system proved up to the task at hand (Czada 2000, p. 470). Above all, it insulated the political system, and, in particular, the Federal Finance and Economics Ministries, from the negative fallout of many aspects of privatisation, since most of the criticisms were deflected to the *Treuhandanstalt*. As such, it played the role of a ‘scapegoat’ or ‘lightning conductor’ in a most excellent manner – a fact that did not go unnoticed by the SPD opposition, which was, however, unsuccessful in its complaints about it. This was also recognised by the government, as the following quotation from the then Federal Economics Minister Helmut Haussmann shows:

It is and remains historically correct that an intermediary institution such as the *Treuhandanstalt* was established. Even if the Federal Ministry of Economics had been directly involved in the privatisations and even if it had played a leading role, it would have been impossible for a ministry to carry out such a high number of privatisations. As a result, the *Treuhandanstalt* would have had to have been re-invented. One or two things about it would have been different, but the basic idea [*Grundansatz*] was correct. (quoted in Kemmler 1994, p. 20)

The parapublic institution *Treuhandanstalt* was a specific solution to most unusual circumstances in the first half of the 1990s. It classically fulfilled the tasks ascribed to parapublic institutions by Katzenstein – namely that of a political shock absorber and pacifier. However, the case also shows that while the German system may tend to shift certain tasks to parapublic institutions, these tasks need not always be associated with a low degree of policy change; this was certainly not so in the case of the *Treuhandanstalt*.

### *The Bundesbank*

Contrary to the fleeting phenomenon of the *Treuhandanstalt*, the *Bundesbank* had been a fixture of (West) German politics for most of the Federal Republic's existence. It became almost the embodiment of many of the positive aspects of the country's macro-economic strategy and record. Certainly, the (West) German central bank was one of the best-known German institutions, both domestically and internationally. Largely credited with the enviable low inflation record of the Federal Republic, which ranks as the OECD champion of price stability in the post-war era (Busch 1993, 1995), it had claimed, and found, an important role in West German economic policy-making. Yet the 1990s were to transform its role completely.

As a parapublic institution, the *Bundesbank* is characterised by only two of the three features mentioned above: autonomy and expertise, the projection of both of which has always been central to the *Bundesbank's* corporate identity. On the one hand, these have been achieved through a careful distancing from the government and on the other, through the highly professional management of its public relations with both economic experts and the public at large. The third feature, participation of societal interests, is, however, notably absent from the *Bundesbank*, which knows no quota system for allocating posts to representatives of societal interests such as business associations or trade unions.<sup>7</sup>

<sup>7</sup> It should, however, be mentioned that on the regional level (that of the *Landeszentralbanken*) there exist advisory councils manned by the banking industry, trade unions and

However, the federal mode of appointing the members of the *Bundesbank* council has always led to a wide range of societal interests and views being represented here at any point in time.

Organisationally, the *Bundesbank* has the status of a 'directly federal corporation of public law' (*bundesunmittelbare Anstalt des öffentlichen Rechts*) according to section 7 of the *Bundesbank Act*.<sup>8</sup> It is, therefore, free from ministerial and parliamentary control. The Act further stipulates that the *Bundesbank* conducts monetary policy with the aim of safeguarding 'the stability of the currency', and that, in doing so, it is free from directives of the government (sections 3 and 12). The constitutional and legal position of the *Bundesbank* is discussed in detail in Stern (1998).

The *Bundesbank's* high standing is a result of its use, over the decades, of the powers rested in it. It has not been afraid to confront governments of various party-political compositions if it thought their economic policies were detrimental to its own task of keeping inflation down; nor, indeed, has it desisted in its criticisms if it was itself criticised by governments. The respective track record of skirmishes ranges from Adenauer in the late 1950s (on raising interest rates) to the grand coalition in the late 1960s, to the debate over revaluation of the Deutschmark, and to disputes with Chancellor Schmidt in the early 1980s, again over the level of interest rates (Sturm 1990, p. 265). In the 1990s, conflicts between the government and the *Bundesbank* centred around issues of budgetary consolidation and the planned revaluation of the central bank's gold reserves (Zohlnhöfer 2001a; Duckenfield 1999). On the international level, the *Bundesbank's* importance grew as the Deutschmark developed into the de facto anchor currency of the European Monetary System and German interest-rate decisions affected many other countries (Busch 1994).

As a result, the *Bundesbank's* power and independence became the subject of some mythology. It was dubbed the 'power upon Main' and 'the bank that rules Europe' (Marsh 1992). To many observers, it seemed a powerful shadow government (*Nebenregierung*) to the one in Bonn (Wildenmann 1969).<sup>9</sup> The 1990s, however, saw two conflicts in

business associations. But the *Bundesbank* emphasises that these councils are not official organs of the *Bundesbank* itself (Deutsche Bundesbank 1995, p. 22).

<sup>8</sup> I will not here discuss in any more detail the organisational structure of the *Bundesbank*. It is well described, for example, in Katzenstein (1987, pp. 61–2) and Kennedy (1991). Any changes in the structure since the early 1990s will be described below.

<sup>9</sup> The mythology surrounding the *Bundesbank's* independence has even led some observers such as Hall (1986, p. 235) and Katzenstein (1987, p. 85) to state erroneously that the bank's independence was enshrined in the constitution. This is not the case – or, to be more precise, it was not at the time it was stated, when independence was only

which the *Bundesbank* had to surrender, and on issues it considered to be of central importance: once on the question of German monetary union in 1990, and then, two years later, on the question of the EU's programme for Economic and Monetary Union (EMU). The context of these defeats and the consequences thereof will be discussed in the remainder of this section.

After the opening of the Berlin Wall, political pressure mounted quickly as East Germans flooded into West Germany, creating huge problems for the administrations of both German states (Busch 1991; Kennedy 1991; Hartwich 1992; Marsh 1992). To alleviate the situation, the Kohl government decided in February 1990 to offer a German currency union to the GDR government, i.e. to introduce the Deutschmark into the GDR and make it the common currency of both states. This was an unexpected move: only days before, Finance Minister Waigel had rejected such a proposal from the SPD. The offer was made against the explicit recommendations of the *Bundesbank*, and the then *Bundesbank* president Karl-Otto Pöhl even briefly considered his resignation when he learned of the government's proposal about which – in a deliberate snub – he had not been informed in advance.

The *Bundesbank* feared that (what it considered to be a premature) currency union between the Federal Republic and the GDR might create inflationary pressure in the west, as East Germany required low interest rates to stimulate economic development. Once the principal decision had been taken by the government, however, the *Bundesbank* explicitly accepted it while emphasising that the responsibility lay entirely with the government.

The next decision to be taken was the rate of conversion between the Deutschmark and the East German mark. For free commercial transactions, the rate was about 1:4.5 at the beginning of 1990. Political considerations, however, dictated a rate that was closer to 1:1 – to indicate primarily that East Germans were not inferior to West Germans. The dilemma was clear: it was political logic against economic logic – and political logic prevailed as the government again chose the conversion rate against the clear wishes of the *Bundesbank*.

On the European level, discussions about a European Currency Union had been conducted in the second half of the 1980s. The *Bundesbank*, which had already been suspicious of the commitments emanating

granted by the *Bundesbank* Act and could easily have been withdrawn. It was only after the amendment of the Basic Law in 1992 (which incorporated the decisions of the Maastricht Treaty) that independence of the central bank and the primary goal of price stability were mentioned in the text of the constitution and thus gained constitutional quality (Stern 1998, pp. 180–3).

from the European Monetary System, was less than enthusiastic about it, though it had not openly opposed the idea. While one theory saw monetary union as a means to achieve tighter integration in other areas and therefore preferred a speedy implementation, the *Bundesbank* clearly favoured a competing theory according to which monetary union should only be the 'crowning' achievement after the successful completion of a series of prior steps and be achieved in conjunction with political union.

Again, the *Bundesbank* lost out. In 1992, moved forward more quickly by the very process of German unification that had led to the bank's first big defeat, the Maastricht Treaty was signed which led to the establishment of a European Central Bank and the Euro before the decade was out. Although the *Bundesbank's* requirements were not met, it had no way of stopping these developments. Its independence was of no practical use, for technically (as in the case of German Monetary Union), these were decisions about the currency area that were not in the *Bundesbank's* remit, but in the government's.

On the other hand, the government's victory (at least in the first case) was not a complete one, for the *Bundesbank* raised interest rates to record levels in the early 1990s to combat inflation and the debt financing of German unification, thus forcing the government to change its policy stance (Zohlnhöfer 2001a). And in the European case, the *Bundesbank* had managed to leave its imprint on large parts of the plans for the future European Central Bank which was largely modelled on its own organisational principles: with strong independence from political interference, a primary stated goal of maintaining price stability, and eventually even located in Frankfurt.

The organisational structure of the *Bundesbank* itself was also not left untouched by the developments in the 1990s. In two stages, it underwent major changes. Both were not uncontested, and mainly concerned the question of the federal dimension of the *Bundesbank's* organisation. They consequently pitted the federal government against the *Länder*, and the members of the *Bundesbank's* directorate against the presidents of the *Landeszentralbanken* (or the *Land* central banks).

Even before German unification had been completed, *Bundesbank* president Pöhl launched a proposal to centralise and streamline the *Bundesbank's* organisational structure. To prevent the number of *Landeszentralbanken* (LZB) increasing from eleven to sixteen (one for each *Land*), he suggested creating eight combined LZBs. This was immediately met with strong resistance from a majority of the LZB presidents who feared the *Länder* would lose influence in that area. Eventually, however, a somewhat more modest reform was agreed, and the number

of LZBs was limited to nine. Federal misgivings were overcome by cutting the maximum number of members of the *Bundesbank* directorate from ten to eight, thus preserving the relative power distribution between the two groups of members that make up the *Bundesbank* council.

After responsibility for the conduct of monetary policy had been taken over by the ECB in 1999, a more substantial reform was called for. Again, it pitted two principal solutions against each other: one with a more centralised character; the other with a more federal one (cf. *Zentralbankrat der Deutschen Bundesbank* 1999). The former opted for an eight-member executive (four of whom would be appointed by the federal government and four by the *Bundesrat*) in which the individual members would have regional responsibilities, but the LZBs would be abolished and replaced by administrative units under the leadership of regional directors who would not be members of the executive; the latter retained the previous structure (a directorate that together with the LZB presidents forms the *Bundesbank* council), but would cut both the numbers of the directorate (from eight to six) and LZBs (from nine to seven).

The *Bundesbank* directorate and the Finance Ministry preferred the first, the *Länder* and the LZBs the second solution. It took more than three years of debates and the report of a committee of experts (under the former *Bundesbank* president, Pöhl) finally to arrive at a solution. Ultimately, the more centralised model with an eight-member executive was adopted, changing the character of the *Bundesbank* substantially.<sup>10</sup>

Looking back over the past fifteen years of the *Bundesbank*, one could be tempted to argue that they cover both the *Bundesbank*'s zenith and its demise. The EU's Economic and Monetary Union (EMU) has robbed the *Bundesbank* of its main task, the conduct of monetary policy, and its attempts to expand into the field of banking regulation have been thwarted.<sup>11</sup> The *Bundesbank*, admired and at times vilified in German (and European) politics, will certainly play a less important role in the future. The combined effects of German unification and European integration have altered the environment for the formerly so powerful

<sup>10</sup> The eventual solution was only achieved because the CDU-governed *Länder* that had opposed the law passed by the *Bundestag* on 1 March 2002, boycotted the *Bundesrat* on the day in question (22 March 2002) because of the controversy over the new immigration law. Otherwise, there would have been a majority for a new round of negotiations as SPD-governed North Rhine-Westphalia had announced it would vote against the law.

<sup>11</sup> The *Bundesbank* had tried to take over responsibility for the Federal Banking Supervisory Office: however, on the same day the *Bundesbank* reform was passed (22 March 2002), a new integrated institution was, instead, created to combine the supervision of banking, insurance and securities.

institution completely. Some observers had already in the early 1990s thought of the *Bundesbank* as 'politically overrated' (Hartwich 1992, p. 272). On the other hand, one might argue that this German and quintessential 'parapublic institution' has now been exported successfully to the European level (see chapter 6 in this volume, p. 127).

### *The Bundesanstalt für Arbeit*

The last of the parapublic institutions to be portrayed in this chapter is the Federal Employment Office, or *Bundesanstalt für Arbeit* (BA). There are two reasons for including it here: on the one hand, the BA was – unlike the *Bundesbank* and the THA – much less directly affected by the seminal challenges of European integration and German unification, and is, perhaps therefore, more 'normal' and representative for the development of this set of institutions as a whole; on the other hand, the substantial reforms of the BA initiated in 2002 may give an indication about the direction in which parapublic institutions may change in the future. This section starts by briefly describing the institutional structure of the BA prior to the recent reforms, before describing and discussing those.

The BA is, like the *Bundesbank*, organised as a public-law organisation that is directly responsible to the federation (*bundesunmittelbare Körperschaft des öffentlichen Rechts*), and as such is part of the indirect administrative structure of the state, or *mittelbare Staatsverwaltung*. The BA's organisation, tasks and instruments are governed by chapter 11 in the third volume of the Social Security Code (*Sozialgesetzbuch III*).<sup>12</sup> Organised into a three-level structure (the headquarters in Nuremberg, ten regional centres of *Landesarbeitsämter* and 181 local employment offices), the core principle of its organisation is tripartite representation in each of its organs – a tradition that goes back to the Weimar Republic. Consequently, the BA is a typical example of the German tradition of sectoral self-governance, in which considerable autonomy is devolved towards non-state institutions. Representatives of labour, employers and the state thus jointly administer the sectoral tasks of unemployment insurance, placement and employment counselling, and keep it at arm's length from direct influence of the federal government.

The most important organs of the BA prior to the reform were the *administrative council* (a 51-person-strong tripartite institution with seventeen representatives from each group), practically the 'legislative

<sup>12</sup> Prior to the introduction of the Social Security Code in 1998, the BA was governed by the Labour Promotion Act (*Arbeitsförderungsgesetz* or AFG).

organ' which sets the rules in the areas the BA governs autonomously; the *executive* with three representatives from each of the three groups; and the *president*, in charge of most of the day-to-day decision-making within the BA. While the former two organs would already appear to be lavishly manned, given their rather restricted tasks, tripartite representation is nevertheless faithfully replicated also on the two lower organisational levels, where on the *Land* level each regional employment office has its own administrative council with at least five representatives of each of the groups, similar to the local employment offices, where the number of representatives is at least three each.<sup>13</sup>

Over time, tripartite consensus led to the BA being used as an instrument for tasks that go well beyond the core area of labour-market policy (Trampusch 2002; see also chapter 8 in this volume). Examples include the administration and payment of child benefit and, more recently, the *Erziehungsgeld*. More generally, the BA was used by consensus of the parties involved to remedy economic structural problems (for instance, by generously extending early retirement) and repeatedly to plug holes in the federal budget and the pension system (for instance, by introducing pension contributions for recipients of unemployment benefits, in effect a cross-subsidy of the pension system by the BA). The BA thus classically fulfilled its task as a 'shock absorber' in the political system. But using this shock absorber had other consequences as well, for these were tasks of the whole state that should have been financed out of general taxation, but which were instead almost exclusively paid for by wage and salary earners contributing to the BA.<sup>14</sup>

The tradition of using the BA as a 'buffer' was continued – and even extended – after German unification. The BA poured enormous sums into the eastern German *Länder*: between 1990 and 2002, no less than € 242 billion were spent, of which € 91 billion (or 37 per cent) were unemployment benefits, and € 138 billion (or 57 per cent) expenses for active labour-market policy (Bundesanstalt für Arbeit 2003, p. 11). The BA thus spent about 40 per cent of its outlays in an area where only about 20 per cent of the population lived – a massive net transfer to the

<sup>13</sup> This replication of representation on the lower levels is, however, to a certain degree justified as the regional levels enjoy a considerable degree of independence in implementing measures of labour-market policy. While it is true to the spirit of *Selbstverwaltung* and may make reactions to specific local circumstances and challenges easier, it makes centrally co-ordinated strategies at the same time more difficult. But that is a well-known problem in a country where the federal government has to rely on implementation by the *Länder* for most administrative tasks.

<sup>14</sup> This means that approximately 15 per cent of the working population who are civil servants or self-employed did not contribute to these outlays.

east that drove up non-wage labour costs in all of Germany.<sup>15</sup> But even resources on so massive a scale could not engender the lasting economic upturn in the east many had hoped for.

In early 2002, a scandal about misrepresentation of placement statistics prompted a significant reform of the BA's organisational structure.<sup>16</sup> Characteristically, this took the form of a two-stage process, consisting of a package of immediate measures, combined with the setting up of a committee charged with the task of making further recommendations. The immediate reforms – which were rushed through the *Bundestag* and *Bundesrat* in only one month – amount to the most substantial reorganisation of the BA in its entire fifty-year history. The key provisions were an organisational shake-up of the BA structure, a strengthening of the role of private placement services and the pledge to reform the whole system root and branch by the year 2004.

Organisationally, the office of the president was abolished, and replaced by a three-member executive, which does not consist of civil servants, but which is being appointed for a five-year term. This new executive was now organised in accordance with private-sector practices (with clear lines and areas of responsibility) and also took over the (few) tasks of the former executive. The administrative council was charged with the task of controlling the executive, and substantially reduced from fifty-one to twenty-one members, but with continued tripartite representation. The BA was also renamed to *Bundesagentur für Arbeit*.

In addition to organisational changes, the role of private placement services in the labour market was enhanced to increase competition. The licensing of such firms was abolished, and vouchers for use in the private placement sector were introduced for long-term unemployed persons the BA could not place. A stronger 'customer orientation' was set as a goal for the provision of the BA's services, and transparency measures and 'benchmarking' between regional employment offices as well as performance-related pay were introduced (Hartwich 2003). Further recommendations were put forward in the report of the commission<sup>17</sup> on 'Modern Labour-Market Services' under the chairmanship

<sup>15</sup> BA contributions have consequently risen from 4.4 per cent of wages in 1990 to 6.5 per cent in 2000 (Trampusch 2002, p. 51). If it were not for the net transfers to eastern Germany, the rate could be lowered for West Germany to 5.0 per cent (Bundesanstalt für Arbeit 2003, p. 12).

<sup>16</sup> The fact that this occurred about six months before the general election of September 2002 and in a phase when labour-market results took a marked turn for the worse, thus threatening the chances of the incumbent government, added considerably to the controversy in the politics of the reform.

<sup>17</sup> Interestingly, the new chairman of the BA, Florian Gerster, was not appointed a member of the Hartz Commission, thus weakening his stance immediately after his installation.

of Volkswagen board member Peter Hartz (Hartz et al. 2002). Its thirteen main suggestions included measures for increasing placement efficiency and enhancing flexibility especially of the low-wage sector; part-time employment was to be particularly encouraged and partially subsidised by the BA; and the latter was in the future to be run by setting targets rather than by detailed prescriptions.

Most of these proposals – a detailed summary and critique of which can be found in the annual report of the Council of Economic Advisers (Sachverständigenrat zur Begutachtung der gesamtwirtschaftlichen Entwicklung 2002) – were put into law, albeit after some changes, with the support of the opposition parties (Hartwich 2003, pp. 132–5). Assessing whether they will have the desired positive effects on the German labour-market slump is beyond the scope of this chapter. At the time of writing (spring 2004), the results do not look promising so far. With regard to the consequences of the organisational changes within the BA, it is clear that the state's hand has been strengthened over that of the employers and trade unions, and partially against their expressed wishes. But what result that will bring is difficult to predict: while some scholars emphasise the 'quite revolutionary structural change' that lies in imposing a private-sector governance structure on the BA (Hartwich 2003, pp. 126, 139), others are markedly more reserved and point to the incremental decentralisation of labour-market policy that has been going on since the 1980s. Changing the rules at the top of the organisation will, in this assessment, have little impact on the way sectoral self-government works at the local level (Trampusch 2002). Initial signs (such as the sacking of the first chairman of the new board of the BA, Florian Gerster, over disputes concerning contracts with external consultants in January 2004) point to an increased politicisation of this parapublic institution. Gerster (a Social Democrat) was replaced by his deputy Weise (a Christian Democrat), even though the latter bore formal responsibility for said consultancy contracts. A coalition of disaffected trade unionists and business representatives was thus able to claim the political scalp of one of the Schröder government's most visible reformers – a symbolic victory. If such politicisation were to continue, it would severely endanger the BA's buffer function, which in turn might limit its usefulness for the political system.

### **Conclusions: Parapublic Institutions in a Changed Environment**

Looking back on the case studies presented above, we can conclude that parapublic institutions do continue to play an important role in the

political system of unified Germany. Indeed, as especially the case of the *Treuhandanstalt* after unification demonstrates, they very much belong to the standard policy repertoire of the Federal Republic: when faced with a new and hitherto unknown challenge, the response was the construction of a new parapublic institution, in which the various levels of the state worked with privileged societal interests to try to tackle the problem co-operatively. Similarly, the *Bundesanstalt für Arbeit* continues to display the characteristics of a parapublic institution throughout the period under investigation here – and maintains them even after the fundamental organisational reform of 2002, albeit on a somewhat reduced scale, as state influence over the BA has been strengthened. The most notable change has taken place in the case of the *Bundesbank*, which has been transformed as a result of the introduction of EMU. As was mentioned above, this can be interpreted either as the *Bundesbank's* demise (particularly if one focuses on the disputes the central bank had lost against the federal government), or as its successful export to the European level, since the European Central Bank (ECB) is institutionally very much modelled on the *Bundesbank*. So, significant changes have taken place in some respects, and this section will focus on assessing these changes and looking for explanations.<sup>18</sup>

Parapublic institutions are, at the beginning of the twenty-first century, operating under circumstances that differ considerably from the ones emphasised in Katzenstein's 1987 study. It may be partly due to these changed circumstances that the policy outcomes associated with their role are now decidedly mixed (when parapublic institutions were once held to be major causes for policy success): they are ambiguous in the cases of both the *Bundesbank* and the *Treuhandanstalt*, but clearly not much cause for pride with respect to unemployment and the *Bundesanstalt für Arbeit*.

One particular change that has altered the foundations on which parapublic institutions operate is the relationship between state and society. In Katzenstein's original analysis, the weakness of the decentralised state was compensated for by its interaction with a centralised society. That centralised society, however, has been severely weakened in the Federal Republic in the past two decades. Hardly anywhere is this more evident than in the area that lies at the core of German corporatist networks, namely industrial relations (cf. chapter 7 in this volume). As

<sup>18</sup> Obviously, the conclusions offered in this chapter cannot claim to be generalised for all parapublic institutions – they have to restrict themselves to the cases studied here. The main reason for this is that recent and detailed studies for many of them are missing in the academic literature. Particular *desiderata* are studies on the role of the churches.

most parapublic institutions are characterised by privileged access for the 'social partners', namely employers and trade unions, they are directly affected by this change. Trade unions have lost four million members during the 1990s, and overall union density has dropped by one-third between 1980 and 1999 to just 18.6 per cent (Ebbinghaus 2002a). Moreover, although trade unions are still relatively strong in the declining 'blue-collar' industries, they are particularly weak in the 'white-collar' section of the economy that continues to grow: here union density is a meagre 12.6 per cent. Conversely, employers' organisations are also plagued by a decline in membership, which is particularly acute in the case of the small and medium-sized enterprises. One result of this is that big firms begin to dominate the associations more and more, and, thus, influence policy in their particular interest.

Both sides of the divide thus suffer from declining organisational capacity, which means that the gap grows between what is in their particular interest and what is in the interest of society as a whole. To halt their respective decline, these organisations are thus less inclined to compromise constructively. Instead, they try to provide their members with specific incentives for membership – and this can mean increased militancy. In the case of the trade unions, these tendencies have been exacerbated by mergers of unions (particularly in the service sector), which further weakened organisational capacities and put the need for finding a common identity above that of constructive co-operation in industrial relations.

The area of industrial relations is, however, only the most visible part of the decline of the 'centralised society'. It is not only unions that have seen declines in mass membership and organisational capacity: the same is true for political parties and churches, to name just two other prominent examples. These developments not only weaken these actors organisationally, they also result in declining financial resources, and above all in a reduction of the legitimacy which is so crucial for the effective operation of parapublic institutions. Put simply, the core institutions of Germany's 'centralised society' have lost much of their *Bindungskraft*, their power to organise and amalgamate interests at a high level. The underlying factors behind these developments, such as economic structural change (resulting from a shift from an industrial economy to one dominated by the service sector), increased societal heterogeneity and more individualisation, have thus affected the German political system in a special way. What is more, as chapters 3 and 4 in this volume have shown, the changes that have befallen parapublic institutions also affect the other two 'nodes' Katzenstein identified as linking state and society, namely political parties and co-operative federalism.

As this chapter has demonstrated, parapublic institutions continue to play a central role in the political system of unified Germany. But since 1990, they have had to cope with enormous new burdens and challenges from both German unification and European integration, while at the same time the societal foundations on which they rest have weakened. Parapublic institutions have thus come under considerable stress in the past fifteen years.

With their foundations and their operating environment changing, it becomes obvious that – with a view to policy outcomes – they have not operated as successfully as in previous decades. Obviously, their method of operation worked less well in the ‘zero-sum’ game situation during a time of low growth than it had in previous decades when higher growth rates made gains for all parties involved possible, with the dispute only being about relative gains.

Seen from the perspective of the political system, however, parapublic institutions have continued to fulfil their shock absorber function to a large degree. When German unification made massive fiscal transfers to eastern Germany necessary, it was parapublic institutions that enabled the political system to work like a ‘problem atomizer’ (Czada 1995), transferring money from their various funds and thus initially preventing the need for politically unpopular tax hikes. The degree to which this happened is, indeed, astonishing: no less than 75 per cent of the transfers to eastern Germany came from the coffers of the various social-security funds (Bundesanstalt für Arbeit 2003, p. 9).

But ‘buffering’ and postponing did not obviate the eventual need to face the truth. When the hoped-for self-sustaining economic upturn in the east did not materialise, costs mounted in the second half of the 1990s, and visibly so. At the same time, external constraints like the European Stability and Growth Pact put shackles on state deficits and an uncomfortable squeeze on state budgets both at the *Länder* and federal level.<sup>19</sup> Discontent with policy outcomes, not least in the labour market, has led to collective soul searching and calls for root and branch reform of the political system. However, even if these calls were less sweeping and unspecific than they generally are, it is unlikely that they would succeed because the German political system is not prone to radical changes – the original puzzle that, after all, prompted Katzenstein’s original study of the ‘semisovereign state’.

<sup>19</sup> It is no small measure of irony that it was a German government that insisted on the introduction of rigorous deficit limits as a precondition for EMU. Thus, the wounds can be seen as largely self-inflicted.

The fact that the German political system is difficult to categorise in the universe of political systems and that its functioning is often poorly understood certainly contributes to the criticism. For it consists of an almost *sui generis* combination of negotiation and competition elements of democracy for which Lehbruch (1996b) has coined the phrase *korporative Verhandlungsdemokratie* (literally a corporative democracy based on negotiation). But contrary to, for example, the Swiss case in which parapublic institutions also play an important role in policy implementation (see Linder 1999, pp. 116–17), the German system is characterised by a far lower degree and tradition of *Konkordanz* between the political parties, which makes co-operation that much harder to attain.

But while many actors participate in German policy decisions and implementation, this does not necessarily mean that they all have the potential or willingness to act as ‘veto players’, as Merkel (2003) has shown. Indeed, reports of the ‘deadlock’ (Heinze 1998) in both German society and the German political system, as well as the hypothesis of incrementalism having turned into paralysis, may be premature as well as exaggerated. After all, game theory teaches us that strategic actors may opt for co-operation rather than veto if they find themselves in the situation of a repeated game from which they cannot escape. And their focus may be less on the ‘consensus’ that is often ridiculed in today’s political debate in Germany, but on ‘exchange’. Indeed, empirical studies that set out to test the hypothesis of the deadlocked German political system often find little evidence of it (Holtmann and Voelzkow 2000). In that political system, parapublic institutions are deeply embedded, and will remain so. Whether they can contribute to produce positive externalities depends, as the case studies here have shown, so much on circumstances that predictions about their future role are beyond generalisation.