

The Forgotten Center: The State as Dynamic Actor in Corporatist Political Economies

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Since the 1970s, a well-developed literature has explored the dynamics of policy-making in corporatist countries, emphasizing a high degree of involvement of societal interests, particularly employers and trade unions, in public-policy formation and implementation.¹ A number of scholars have shown how regularized channels of deliberation, consultation, and negotiation between labor and capital have contributed to economic growth and social peace in systems that often perform better, politically and economically, than liberal political economies, where questions of economic distribution and the organization of production are addressed primarily through (or remain unaddressed by) markets. While this rich body of work has provided an analytical framework for exploring policy and institutional regularities in non-liberal political economies, it has by and large neglected the role of the state, whose role is crucial to understanding how corporatist polities respond to shifting social and economic challenges. This flaw has resulted in a misleading image of corporatist systems requiring little regulation and in which the interests of social groups almost seamlessly produce policies concomitant with the public good.

This theoretical underdevelopment of the state in traditional accounts of corporatist governance, we suggest, renders them poorly equipped to account for recent political developments in many advanced industrial countries, corporatist and non-corporatist alike. Like much of the literature on corporatism, recent work on “Varieties-of-Capitalism” similarly under-theorizes the role of the state in corporatist, or “coordinated market economies.”² By doing so, such work offers limited analytical purchase on sources of political variation *across* corporatist systems, including the nature of the party system, the ideological postures of unions and employers’ associations, and idiosyncratic political factors such as the partisan character and strategic predilections of particular governments.

¹ For the classic formulation of corporatism, see Philippe C. Schmitter, “Modes of Interest Intermediation and Models of Societal Change in Western Europe,” *Comparative Political Studies* 10 (April 1977), 9. Other seminal works include Wolfgang Streeck and Philippe C. Schmitter, eds., *Private Interest Government: Beyond Market and State* (Sage: Beverly Hills, Calif., 1985); and Gerhard Lehbruch and Philippe C. Schmitter, eds., *Patterns of Corporatist Policy-Making* (Sage: Beverly Hills, Calif., 1982).

² See Peter A. Hall and David Soskice, “An Introduction to Varieties of Capitalism,” in *idem*, eds., *Varieties of Capitalism: The Institutional Foundations of Comparative Advantage* (Oxford: Oxford University Press, 2001).

Such variation noted, in *all* corporatist systems adjustment invariably entails a significant and continued level of involvement by the state, whose purview for autonomous action is critical to promoting needed reforms and institutional adjustment.

Although the positive economic climate of the corporatist heyday of the 1970s and 1980s has yielded to high rates of unemployment, sluggish growth, and fiscal austerity associated with the policy constraints of European Economic and Monetary Union (EMU), state intervention in facilitating adjustment in corporatist systems has remained vital. In fact, we contend that it is in hard economic times, when the relative scarcity of resources engenders competition among social groups and increases discrepancies between private interests and public weal, that the state's coordinating functions are *particularly* important. Such adverse economic contexts tend to intensify pressures on policy-makers, not only to formulate just and viable policies that reduce economic uncertainty, but also to promote negotiation between social partners whom strained circumstances have made more likely to dig in their heels.

Germany and the Netherlands represent excellent *prima facie* cases for a comparative study of the role of the state in corporatist systems for several reasons. First, the state in both countries has a tradition of sharing political space with the social partners. Employers are well organized, especially among large and medium-sized firms, and collective bargaining occurs predominantly at the sectoral level.³ Furthermore, the Netherlands and Germany both possess "Bismarckian," or "Christian Democratic," welfare states, characterized by occupationally distinct, employment-related social insurance programs co-managed by worker and employer representatives and financed by earmarked payroll contributions from employers and workers.⁴

³ German industrial relations take place under the *de facto* leadership of the metalworking sector, and separate wage bargaining from plant-level management. See Wolfgang Streeck, *Works Councils: Consultation, Representation, and Cooperation in Industrial Relations* (Chicago: University of Chicago Press, 1995); and Kathleen Thelen, *Union of Parts: Labor Politics in Postwar Germany* (Ithaca, N.Y.: Cornell University Press, 1991).

⁴ For the characteristics of Continental welfare states, see Kees van Kersbergen, *Social Capitalism: A Study of Christian Democracy and the Welfare State* (London: Routledge, 1995); Gøsta Esping-Andersen, *The Three Worlds of Welfare Capitalism* (Princeton, N.J.: Princeton University Press, 1990), 27 and *passim*; Fritz W. Scharpf and Vivien Schmidt, "Introduction," in *idem*, eds., *Welfare and Work in the Open Economy*, vol. II,

At the same time, however, the two countries are distinct in terms of the institutional frameworks of the political economy within which their welfare states and industrial-relations systems are embedded, suggesting possible sources of variation in policy outcomes. For example, state intervention has traditionally been very strong in Dutch industrial relations,⁵ while in Germany the constitutionally enshrined principle of *Tarifautonomie*, or “wage independence,” has limited intervention in this area. Likewise, in the Netherlands a decentralized but unitary state retains final authority in a wide range of policy domains, while German federalism and jurisdictional limits on state authority represent more substantial constraints on policy-makers, not only in wage bargaining but also in a whole host of other policy areas.⁶ As a result, the mechanisms through which the German state has facilitated adjustment have tended to be more informal and subtle than those in the Netherlands, although recent German governments have been far from passive observers of social and economic change, as we shall see.

During the past fifteen years, the Dutch and German states have been instrumental to promoting reform and compensating for the policy failures of corporatist institutions. Previously, corporatist policy-making, in Germany and the Netherlands as elsewhere, was widely celebrated for promoting social peace, wage restraint, and vibrant economic growth, and both countries served as standard-bearers for the possibilities of adjustment through organized political and social bargaining. In the 1990s, however, these stories of corporatist success yielded to narratives of failure, as past economic successes have been overshadowed by more recent economic problems, including sluggish or even stagnant growth, high levels of structural unemployment, apparently unbridgeable insider-outsider cleavages, and increasingly severe pressures on wage-based social-policy financing. As the Dutch and German economic picture has darkened, the same corporatist institutions that had once

Diverse Responses to Common Challenges (Oxford: Oxford University Press, 2000), 11-13; and Maurizio Ferrera, Anton Hemerijck, and Martin Rhodes, *The Future of Social Europe: Recasting Work and Welfare in the New Economy* (Oeiras: Celta Editoria, 2000), 40-45.

⁵ John P. Windmuller, *Labor Relations in the Netherlands* (Ithaca, N.Y.: Cornell University Press, 1969).

⁶ Peter J. Katzenstein, *Policy and Politics in West Germany: The Growth of a Semisovereign State* (Philadelphia: Temple University Press, 1987).

been credited with underpinning national prosperity came to be seen as the sources of sclerosis and failed adjustment. In response, the state in both countries (beginning in the 1980s in Germany and somewhat later in the Netherlands) has employed a variety of forms of intervention in an effort to fix dysfunctional corporatist policy-making structures. At times, both states have used administrative and financial pressure to coerce the social partners into undertaking desired policy changes. At others, they have bypassed corporatism and imposed policies of its own devising, while in a few instances they have suspended corporatist bargaining or even dismantled it altogether.

While the character of intervention has varied significantly between the two countries and within them over time, Germany and the Netherlands thus represent two salient examples of corporatist political economies in which state authorities have worked to devise effective responses to institutional and policy dysfunctions. In Germany, the 1980s witnessed a series of relatively timid reforms in social and labor-market policy, followed by a period of increasing state intervention in response to the seismic social and economic shocks of reunification in 1990. Thereafter, German governments of both Left and Right worked to promote corporatist negotiation, most notably in the case of the tripartite *Bündnis für Arbeit*, or “Alliance for Jobs,” even as they began to formulate policies that bypassed or suspended corporatist arrangements, given the limits placed *Tarifautonomie* on direct intervention in collective bargaining. The failure of attempts to reinvigorate corporatist wage-bargaining and social-protection reform in turn led German governments to adopt a series of “second-best” strategies for promoting reform, characterized by a more aggressive, interventionist posture and waning receptiveness to the concerns of the social partners and political opposition. In labor-market policy, for example, they have introduced a wide variety of training and placement programs, boosted subsidies to employers to create jobs, and stepped up pressure on the unemployed to search for work. In social policy, where there are fewer constitutional limits on their authority, governments have been even more successful in securing reforms, such as in the case of the recent restructuring of the pension system. Although federalism and the frequent control of the *Bundesrat*, or upper house of Parliament, by the political opposition, place significant limitations on state

capacity even in the realm of social security, governments have often been able to secure reforms in this area by buying off or otherwise undermining the opposition politically.

In the 1980s, the Netherlands witnessed a resurgence of corporatist bargaining in the wake of a severe recession, spiraling unemployment, and significant inflation. Under the threat of government-imposed austerity and mandated liberalization, the social partners chose to negotiate, with unions wishing to limit the pain resulting from reform and employers hoping to forestall a government takeover of the policy-making process. The resulting “Wassenaar Accord,” concluded in late 1982, provided for the de-indexation of wages, negotiations over work-time reduction and job creation, and the partial decentralization of wage bargaining. This agreement ushered in a period of vibrant, negotiated reform in the 1980s and early 1990s that underpinned the celebrated “Dutch miracle” of rapid job growth.⁷ With respect to social security and labor market, the Dutch picture has been more mixed, with alternating patterns of state intervention, suspensions of corporatism in social insurance, and, much to the chagrin of the social partners, independent state efforts to shape active labor-market policy after the failure of a tripartite experiment in the early 1990s.

These nationally distinct patterns of state intervention provide clear support for the two central arguments of this chapter. First, they demonstrate that careful attention to the state’s shifting role in remedying political-economic problems is crucial to a nuanced account of the dynamics of corporatist politics, particularly in periods of reform, fiscal austerity, and slowed economic growth. Second, they illustrate that corporatism is a dynamic and evolving process of dialogue and political exchange between the state and social partners, rather than a fixed institutional structure producing stable and predictable political patterns and policy trajectories. In our contribution to this volume, we focus on wage policy, social policy, and labor-market policy, domains that have moved to the center of recent policy debates. In each of these areas, the state has been instrumental to securing reforms, whether by promoting compromise among unions and employers, working indirectly to reshape the

⁷ See Jelle Visser and Anton Hemerijck, *“A Dutch Miracle”: Job Growth, Welfare Reform and Corporatism in the Netherlands* (Amsterdam: Amsterdam University Press, 1997), esp. ch. 5.

policy incentives faced by the social partners, or intervening directly to compensate for the failures of existing corporatist institutions. By exploring these areas of reform, we hope to shed light on how national constitutional and institutional particularities shape both the options available to state authorities and the resulting character of their efforts to repair broken corporatist arrangements. In the following section, we undertake a brief review of the literature on corporatism as a theoretical construct and empirical heuristic, emphasizing the extent to which leading scholars have addressed, or failed to speak to, the vibrant role of the state in corporatist governance.

The Forgotten Center: The State as Dynamic Actor in Corporatist Political Economies

The corporatist literature of the 1970s and 1980s made important contributions to the revival of the study of institutions mediating between state and market in advanced capitalist democracies. In the midst of the allegedly “ungovernable” 1970s, there was significant empirical support for the hypothesis that the capacity of advanced industrial societies to cope with social conflict and improve economic performance is increased by an institutional infrastructure which incorporates the societal interests of organized capital and labor into national economic-policy formation and implementation.⁸ Corporatist research during this period focused primarily upon the organizational attributes of organized interest groups and argued that tripartite incomes policies were almost indispensable tools of crisis management. In particular, so-called “encompassing organizations,” or highly centralized and concentrated functional interests, were believed likely to pursue responsible strategies of collective action supportive of the public goals of full employment and price stability.⁹ To a considerable extent, corporatist success in achieving economic and social stability was believed to be largely self-reinforcing, due to positive demonstration effects that reinforce mutual trust among the social partners and between them and the state.

⁸ See Lehbruch and Schmitter, eds., *op. cit.*; Suzanne Berger, ed., *Organizing Interests in Western Europe: Pluralism, Corporatism, and the Transformation of Politics* (Cambridge: Cambridge University Press, 1981); and John H. Goldthorpe, ed., *Order and Conflict in Contemporary Capitalism* (Oxford: Clarendon Press, 1984).

⁹ Mancur Olson, *The Rise and Decline of Nations: Economic Growth, Stagflation, and Social Rigidities* (New Haven, Conn.: Yale University Press, 1982); Michael Bruno and Jeffrey D. Sachs, *Economics of Worldwide Stagflation* (Cambridge, Mass.: Harvard University Press, 1985); and Peter Lange and Geoffrey Garrett, “The Politics of Growth: Strategic Interaction and Economic Performance in the Advanced Industrial Democracies,” *Journal of Politics* 47 (1985): 792-828.

In the 1980s, however, corporatist theory seemingly lost much of its rationale, as many corporatist political economies ran into serious employment, fiscal, and monetary difficulties, providing ammunition for neoliberal and other criticisms of political “interference” with market mechanisms. As the structural recovery of Western economies seemed increasingly elusive, a number of arguments were advanced for the putative demise of corporatism. Some authors were ready to predict “the end of organized capitalism,”¹⁰ while others discovered the “challenge of flexibility,”¹¹ arguing that pressures to decentralize collective bargaining and the shift from Fordist, standardized mass production toward craft-based, diversified methods of production were difficult to reconcile with corporatist interest intermediation.¹² Highlighting the historical correlation of corporatist success with Keynesian macro-economic intervention, other observers suggested that the liberalization of international capital markets in the 1980s had sharply curtailed the political capacities of national governments to offer full employment, in exchange for wage restraint, through the use of fiscal and monetary policy.¹³ Finally, with the introduction of the Stability and Growth Pact in the lead-up to EMU and the resulting shift toward hard currency policies across Europe, many observers feared that intensified régime competition would further jeopardize corporatist bargaining frameworks.

Departing from the prevailing intellectual fashion, Philippe Schmitter, one of the founding fathers of corporatist research, suggested the continued relevance of societal interest intermediation in an era of liberalization and slowed economic growth.¹⁴ Bearing out Schmitter’s contention, the fiscal and monetary pressures associated with qualifying for EMU generally did not lead to bold strategies of liberalization and deregulation. On the contrary, EMU seemed to spur a resurgence of national social pacts aimed at ensuring welfare-state sustainability, as the shift to a hard currency régime

¹⁰ Scott Lash and John Urry, *The End of Organized Capitalism* (Oxford: Polity Press, 1987).

¹¹ Guido Baglioni and Colin Crouch, eds., *European Industrial Relations: The Challenge of Flexibility* (London: Sage, 1990).

¹² Michael J. Piore and Charles F. Sabel, *The Second Industrial Divide: Possibilities for Prosperity* (New York: Basic Books, 1984); and Richard Locke, Thomas Kochan, and Michael Piore, *Employment Relations in a Changing World Economy* (Cambridge, Mass.: MIT Press, 1995).

¹³ Fritz W. Scharpf, *Crisis and Choice in European Social Democracy* (Ithaca, N.Y.: Cornell University Press, 1991).

¹⁴ Philippe C. Schmitter, “Corporatism Is Dead! Long Live Corporatism!,” *Government and Opposition* 24 (1989): 54-73.

unexpectedly brought the social partners in many countries closer together.¹⁵ This trend began in the Netherlands with the 1982 “Wassenaar” accord, followed by Denmark and Ireland in 1987 and Finland, Italy, Spain, and Portugal in the early to mid-1990s.¹⁶

Even many of those who pointed to the continued relevance of corporatist scholarship, however, tended to neglect the dynamic role of the state in facilitating and sustaining corporatist bargaining. From their earliest incarnations, most treatments of corporatist governance employed a rather narrow, “society-centered” perspective, centering on the organizational attributes of functional organized interests and largely neglecting the dynamic role of the state in what purported to be self-regulating political-economic models. To be sure, the state played a significant role in some of the earlier corporatist literature. According to Schmitter’s famous definition, for example, “societal corporatism” is characterized by a “limited number of singular, compulsory, non-competitive, hierarchically ordered and functionally differentiated categories, *recognized, or licenced (if not created) by the state, and granted a deliberate representational monopoly.*”¹⁷ Although such scholars acknowledged the importance of the state, they tended to limit their analysis of its role to the initial construction of corporatist systems, which thereafter were supposed to be more or less left to regulate themselves.

Not limited to such first-generation studies of corporatism, the absence of a dynamic conception of the state continues to characterize more recent work, such as the emerging literature on “Varieties of Capitalism” founded by Peter Hall and David Soskice.¹⁸ Viewing the political-economic dynamics of both “Coordinated Market Economies” (CMEs), such as Germany, and “Liberal Market Economies” (LMEs), such as the US and Britain, as self-reinforcing and highly path-dependent, Hall and Soskice overlook the role of politics and the state’s capacity to engineer novel adaptive strategies, except to argue that, over time, government policies reinforce the tendency of both CMEs and LMEs

¹⁵ Giuseppe Fajtag and Philippe Pochet, eds., *Social Pacts in Europe* (Brussels: ETUI, 2000).

¹⁶ David Cameron, “Unemployment, Job Creation, and Economic and Monetary Union,” and Martin Rhodes, “Globalization, Welfare States, and Employment: Is There a European ‘Third Way’?,” both in Nancy Bermeo, ed., *Unemployment in the New Europe* (Cambridge: Cambridge University Press, 2001).

¹⁷ Philippe Schmitter, “Still the Century of Corporatism?,” in *idem* and Gerhard Lehmbruch, eds., *Trends Towards Corporatist Intermediation* (Beverly Hills and London: Sage, 1979), 13. Emphases added.

¹⁸ Hall and Soskice, *op. cit.*

to revert to established practices.¹⁹ Accordingly, while Soskice and Hall admit that governments are important, they see their role as limited to supporting established patterns of coordination, particularly in CMEs, in response to pressure from economic shocks, both exogenous and endogenous.²⁰ As a result, not only is the state's role reduced to reinforcing established economic structures, but a whole host of other, political factors, including systems of social partnership and evolving relationships among governments and electorates, is largely ignored.

Recognizing the neglect of the state in such approaches, a separate strain of research since the mid-1980s has attempted to develop a more complex, "state-centered" perspective, emphasizing the state as an autonomous actor that critically affects the ways in which corporatist political economies adjust to shifting economic, social, and political challenges.²¹ Colin Crouch, in particular, has shown in great detail how organized interests define their strategies of collective action within an institutional setting involving distinctive state traditions and complex linkages between state and society.²² Insights such as Crouch's point to the fact that nearly all aspects of corporatist governance are profoundly affected by the state, which plays several key roles related to the construction of corporatist frameworks and support of vibrant political exchange within them. First, the state is an institutional regulator providing *Ordnungspolitik*, the legal framework and ground rules that govern corporatist negotiation among the social partners. Second, the state's legislative capacity in economic, social, and labor market policy-formation has a direct influence on relations among the government, trade unions, and employer organizations. Third, beyond facilitating the initial institutional infrastructure for corporatist encounters, the state frames and facilitates corporatist exchange, whether through side-payments or threats to bypass corporatist institutions. As new policy pressures and dysfunctions arise over time, state intervention in each of these areas is required to sustain a responsive system of meaningful corporatist exchange.

¹⁹ *Ibid.*, 62-64, 66-67.

²⁰ *Ibid.*, 63.

²¹ Gianfranco Poggi, *The State: Its Development, Nature and Prospects* (Stanford: Stanford University Press, 1990).

²² Colin Crouch, *Industrial Relations and European State Traditions* (Oxford: Clarendon Press, 1993).

The defining feature of the corporatist state lies in its willingness to share political authority with organized interests, with which it develops complex, reciprocal relationships,²³ a dynamic which Colin Crouch has aptly termed the “sharing of political space.”²⁴ Neither state capacity nor the power of interest organizations, in other words, is the sole determinant of the dynamics of corporatist governance.²⁵ In exchange for their acquisition of the status of public authorities and increased access to public-policy formation, voluntary associations share the burden of public administration, thereby becoming *staatsträgende Kräfte*, or “state-supporting powers.” By sharing public decision-making authority with civil society, the state devolves a portion of its most distinctive resources—namely legitimate coercion and the capacity to enforce binding agreements—to organized groups that it does not fully control administratively. At the same time, by bestowing private interests with circumscribed public authority, the state is able to expand its sources of information and professional expertise, resolve problems of public-policy implementation, and overcome dilemmas of policy coordination.

Effective corporatist adjustment is also crucially dependent upon a number of other institutional preconditions which cannot be taken for granted. For example, the role of bi- and tripartite institutional structures, which bring together state officials and the social partners within institutions for policy analysis, deliberation, and negotiation, is critically important. Repeated encounters within these fora encourage the development of solutions to distributive problems by allowing certain parties to accept outcomes undesirable to them in the knowledge that these arrangements can be adjusted in succeeding rounds of negotiations. This dynamic facilitates the realization of gains associated with positive coordination, the transformation of short-run, parochial interests into solidaristic interaction across the bargaining table, and, over time, the emergence of a shared view of political-economic problems and desirable policy solutions. It is therefore misleading

²³ Wolfgang Streeck, *Social Institutions and Economic Performance: Studies of Industrial Relations in Advanced Capitalist Economies* (London: Sage, 1992).

²⁴ *Ibid.*

²⁵ Colin Crouch and Alessandro Pizzorno, eds., *The Resurgence of Class Conflict in Western Europe since 1968* (London: Macmillan, 1978); and Marino Regini, “The Conditions for Political Exchange: How Concertation Emerged and Collapsed in Britain and Italy,” in Goldthorpe, ed., *op. cit.*

to view corporatist governance as inherently associated with state weakness. On the contrary, social compromise may well enhance the state's capacity to secure its policy objectives by mobilizing intellectual and administrative resources from the social partners and other stakeholders. Effective corporatist governance, therefore, requires state actors not merely to create and maintain a framework for exchange among organized interests, but also to use important capacities to guide policy outcomes.

The state's authority to approve and ratify also implies the power to nullify undesirable agreements, enabling it to ensure *bona fide* processes of negotiation. In this respect, the multifarious role of the state in corporatist governance corresponds to Scharpf's notion of the "shadow of hierarchy" in strategic games,²⁶ as the ultimate availability of hierarchical intervention and state ratification of agreements among private interests helps to curb distributive conflict and opportunistic "rent-seeking" among bargainers. This "relative autonomy of the state," however, does *not* suggest that state actors can change the institutional environment as if they were operating a lever; rather, state responses to corporatist policy exchanges shape and are shaped in turn by both the institutional framework within which they operate and the strategies of organized interests with which they are confronted.

Even in the presence of an active state role in guiding corporatist bargaining, however, conflicts among the multiple interests involved can result in failure, a situation to which Fritz Scharpf aptly refers as a "joint-decision trap."²⁷ The state will inevitably be confronted with tensions between recognized social partners, whose needs to represent rank-and-file demands effectively and regulate these demands are in constant tension. When the strain between what Schmitter and Streeck have called the "logic of influence" and the "logic of membership" is not successfully managed by the social partners, a "representation crisis" can result, jeopardizing the entire edifice of corporatist exchange.²⁸ In such a situation, capital and labor pursue their own versions of the national economic interest, and their respective strategies are influenced not only by divergent ideologies and economic doctrines, but also by

²⁶ Fritz W. Scharpf, *Games Real Actors Play* (Boulder, Colo.: Westview, 1997).

²⁷ Fritz W. Scharpf, "Die Politikverflechtungs-Falle: Europäische Integration und Deutscher Föderalismus im Vergleich," *Politische Vierteljahresschrift* 26, no. 4 (1985): 323-356.

²⁸ Streeck and Schmitter, eds., *op. cit.*

perceptions of their respective roles in the political economy and their self-regarding concerns with organizational survival and growth. Given that it is forced to rely upon the often-self-interested social partners for policy implementation, the government's capacity to respond creatively to changing external demands can become constrained in such a scenario. The advantages accruing from *Staatsentlastung*, or the state's sharing of policy responsibilities with the social partners, thus comes at a price, and much depends upon the institutional capacity of "consensus engineering" to generate, maintain, and adjust agreements in the face of changing political-economic circumstances and divergent interests, goals, and perceptions. Furthermore, the social partners' requisite willingness to accept unilateral sacrifices, on the understanding that they will not be exploited but rather reciprocated by others when the occasion arises, presupposes a high degree of mutual trust, which must be nurtured over time by enlightened state intervention.

Without effective consensus engineering, which relies heavily upon actual or potential state intervention, corporatist institutions can become barriers to effective policy coordination, economic performance, and social peace. Under such conditions of a corporatist "joint-decision trap," the state becomes imprisoned in an institutional setting that no longer functions as intended. Faced with such a situation, state authorities can choose one of two options. On the one hand, they can work actively to reinvigorate societal consensus in an attempt to relaunch more responsive corporatist bargaining processes. On the other, they can distance themselves from corporatist arrangements in an attempt to extricate the state from its dependence on the support of the social partners. Such a strategy of "corporatist disengagement" constitutes a reaction to prolonged corporatist immobility and is often accompanied by state's move to devise reforms directly rather than negotiating them with the social partners, or, in extreme circumstances, even by dismantling of part of the corporatist political apparatus.

This possibility noted, the availability of state-led corporatist disengagement is limited by the "path-dependent" character of established corporatist institutions, as the state's ability to dismantle or bypass corporatism very much relies upon the institutional capacities at its disposal. While enjoying a certain autonomy to address problems in an authoritative fashion, state actors will most likely believe

themselves to be in need of societal consensus and will thus be reluctant to break out of the stagnant corporatist policy framework or dismantle corporatist institutions in favor of untried alternatives. In the event of failed corporatist bargaining, state actors tend first to try to persuade organized interests by offering them side payments and other incentives, or work to adjust and recalibrate the corporatist model in order to revitalize joint policy-formation and implementation. While corporatism works best when there is a credible commitment on the part of the state not to intervene, however, accumulated failures on the part of the social partners to perform delegated policy functions create both opportunity and political pressure for the state to do just that. In short, neither the resurgence of social pacts nor the suspension of corporatist institutions is predetermined, and, in the event of corporatist failure, a series of carrots and sticks may or may not encourage participants to return to negotiated reform.²⁹

In the sections that follow, we show that such indeterminacy has characterized recent reform experiences in both Germany and the Netherlands. In each, state responses to the failures of corporatist institutions and the character of policy outcomes have been shaped by nationally distinct institutional and policy legacies. Institutional differences in the two countries, relating to both the character of their corporatist institutions and the broader political economy within which they are embedded, have shaped pressures and opportunities for particular kinds of state intervention designed to repair broken corporatist arrangements. We begin with the Dutch case, where the revitalization of corporatist wage bargaining in the 1980s and 1990s was prompted by an effective “shadow of hierarchy” supported by a high degree of institutionalized state capacity.

State Responses to the Contingencies of Dutch Corporatism

Most observers agree with Gerhard Lehbruch’s characterization of the Dutch political economy as an example of corporatism “*par excellence*.”³⁰ Far more than Germany, the Dutch

²⁹ Anton C. Hemerijck, “Corporatist Immobility in the Netherlands,” in Colin Crouch and Franz Traxler, eds., *Organized Industrial Relations in Europe: What Future?* (Brookfield, Vt.: Avebury, 1995).

³⁰ Gerhard Lehbruch, “Concertation and the Structure of Corporatist Networks,” in Goldthorpe, ed., *op. cit.*, 165.

political economy is furnished with a firmly established apparatus of bi- and tripartite boards for nation-wide social and economic policy-making. The Foundation of Labor (STAR, or *Stichting van de Arbeid*), owned by the central union and employers' organizations, is a private foundation, established in 1945 as a forum for meetings between the social partners. These meetings, attended by a delegation from the Cabinet, occur twice every year, once in the spring when the budget for the following year is prepared, and again in the fall, when a new round of wage negotiations is about to begin. The Social-Economic Council (SER, or *Sociaal-Economische Raad*), founded in 1950, is a tripartite advisory board. Since its recent reorganization in 1995, employers and unions each have eleven seats, while the other eleven are occupied by independent crown members appointed by the government, usually professors of Economics, the President of the Central Bank, and the Director of the Central Planning Bureau. As the foremost Dutch economic forecasting agency, the Central Planning Bureau (*CPB*, or *Centraal Planbureau*), enjoys a great deal of influence as the key supplier of economic projections, on the basis of which the social partners define their strategies of collective action. In this section, we focus on state responses to the constraints and opportunities of Dutch corporatism in the areas of wage bargaining, social security, labor-market policy and regulation, and pensions. As these components of the welfare state are governed by different mixes of associational self-regulation and government intervention, state strategies have differed widely across these domains, ranging from attempts to reinvigorate Dutch corporatism in the area of wage bargaining to deliberate efforts to dismantle corporatism in social insurance.

A distinctive feature of Dutch post-war economic policy has long been its state-led wage policy.³¹ In the 1960s and 1970s, responsibility for wage policy reverted to unions and employers. However, since they were unable to agree among themselves, actual negotiations frequently ended with state intervention. Particularly in the wake of the first oil shock of 1973, the center-Left Den Uyl government opted for a strategy of fiscal stimulation. This set the stage for a conventional Keynesian corporatist package of fiscal reflation in exchange for wage restraint. This strategy failed,

³¹ Windmuller, *op. cit.*

however, due to the radicalizing Dutch trade unions' refusal to support the government's loose budgetary policies with wage moderation. In response, in 1974 and 1976 the state imposed a wage freeze, but to no avail. A center-Right government was also forced to resort to wage intervention in 1979, 1980, and 1981.

Having failed to adjust to the first oil shock, the Netherlands experienced a much more severe recession in the wake of the second oil crisis in 1979 than did most other OECD countries. Levels of unemployment not seen since the Great Depression raised the degree of frustration over divided governments and repeated corporatist failures. New elections in 1982 brought to power an austerity coalition of the CDA and the VVD, led by the Christian Democrat Ruud Lubbers. The Lubbers government presented itself as a "no-nonsense" administration that was "there to govern." Ready to take on vested interests, the new government immediately suspended cost-of-living indexation in wage agreements and social benefits, while freezing minimum wages, social benefits, and public-sector wages. The stage was thus set for tough confrontation between the state and the social partners, especially the unions. Surprisingly, however, the inauguration of the new government was greeted with a social pact, the now famous Wassenaar accord of 24 November 1982, named after the place where it was signed.³² After a decade of corporatist failure, the Dutch social partners had come to recognize that promoting investment, essential for job-creation and the struggle against unemployment, required a higher level of profits, and hence, a lower wage share. Moreover, the unions, weakened by the severe recession, were hardly in a position to engage in industrial conflict, while the employers' organization feared political interference in the form of a statutory and uniform reduction of the working week. Trade unions accepted protracted real wage restraint in exchange for a so-called "cost-neutral" reduction of working hours and job-sharing.

The Wassenaar accord marked a shift from the failed tripartism in the 1970s to successful bipartism in the 1980s and 1990s. Despite the celebrated voluntary character of the bipartite agreement, it is crucial to emphasize that Wassenaar was prompted by an effective threat on the part

³² Visser and Hemerijck, *op. cit.*

of the Lubbers administration to intervene in wage setting. Compelled by this “shadow of hierarchy,” the social partners joined forces in striking a bipartite deal. Once the accord was signed, the government withdrew this “sword of Damocles” from the policy agenda. Helped by an international economic upswing, rising levels of profits and investment, and significant job-creation, Lubbers’ austerity policy paid off politically. In 1986 the center-right coalition was re-elected with gains for his CDA party. Two successive center-Right governments then engineered a clear break with corporatist immobility of the 1970s.

The resurgence of corporatism significantly altered the relationships among unions, employers, and the state. A new pattern emerged, characterized by centralized dialogue over legislative and substantive policy issues, combined with sectoral wage bargaining based on the primacy of industrial self-regulation.³³ In the wake of the Wassenaar Accord, the tripartite Social and Economic Council also gained a new lease on life and issued a range of unanimous policy recommendations regarding youth unemployment (1984 and 1986), training (1986 and 1987), long-term unemployment (1986 and 1987), minimum-wage costs (1988), and part-time work (1989).

This new corporatism proved fairly robust, although it was certainly not free of conflict. In 1989, the Christian Democrats exchanged their Liberal coalition partners for the Social Democrats after a break in the old coalition over environmental policy led to new elections in 1989. At the turn of the 1990s, German unification boosted Dutch economic growth, but high interest rates soon dampened economic activity, leading to a reversal of employment gains. In these troubled waters, the credibility and legitimacy of Dutch social partnership came under attack from parliamentary leaders of the liberal opposition and the social democrats in the government. While the Christian Democrats still defended social partnership, the secular VVD and PvdA maintained that consensual, negotiated adjustment occurred at too slow a pace to respond to economic crises.

³³ Jan Peter van Toren, *Achter Gesloten Deuren? CAO-overleg in de Jaren Negentig* (Amsterdam: Welboom, 1996).

Alarmed by mounting political pressures, the central employers' and union organizations moved closer together in the early 1990s. In another attempt to stave off government intervention, the social partners signed yet another multi-year agreement, the so-called "New Course" accord, in December 1993.³⁴ This accord was an heir to Wassenaar but went further down the path of organized decentralization and flexibility. Employers abandoned their categorical refusal of shorter working hours, and unions promised further wage restraint. This accord also embraced a new balance between flexibility and security by reducing levels of protection of existing ("core") workers, coupled with enhanced employment opportunities and social security for atypical workers.³⁵

While the social partners agreed in 1982 to a long-term strategy of organized wage restraint, it became increasingly clear towards the end of the 1980s that the intimate ties between sectoral industrial relations and payroll-tax-financed social security had allowed the social partners to externalize the costs of economic adjustment onto the social-security system, resulting in uncontrollable growth in the volume of claimants. In response, the second Lubbers coalition of Christian Democrats and conservative Liberals, in office between 1986 and 1989, enacted a package of cost-containment measures, including a reduction of replacement rate of social-security benefits from 80% to 70% of previous wages. Despite these cuts, in the second half of the 1980s the number of people receiving disability benefits continued to rise, leading to an explosion in costs. As the politically unacceptable number of one million disability claimants loomed in 1989, Prime Minister Lubbers publicly dramatized the issue by saying that the country was "sick" and required "tough medication." Using the mechanism of sickness and disability payments instead of layoffs, employers bought off worker resistance and maintained good relations with the unions.³⁶

Lubbers I and II had exhausted the "price" policy of bringing social expenditures under control by freezing and lowering benefits. Lubbers recognized that he needed the Social Democrats

³⁴ Anton Hemerijck, Marc van de Meer, and Jelle Visser, "Innovation through Co-ordination: Two Decades of Social Pacts in the Netherlands," in Fajertag and Pochet, eds., *op. cit.*

³⁵ Jelle Visser, "The First Part-time Economy in the World: Does it Work?," AIAS-CESAR research paper, Amsterdam, 1999.

³⁶ Leo Aarts and Philip de Jong, eds., *Curing the Dutch Disease* (Brookfield, Vt.: Avebury, 1996).

(*Partij van de Arbeid*, or PvdA), led by ex-union leader and Wassenaar negotiator Wim Kok, in the government to share responsibility for the unfinished business of welfare reform. As the PvdA re-entered the government in 1989 as a partner in Lubbers' third cabinet, the low employment/population ratio was singled out as the root cause of the crisis of the Dutch welfare state.³⁷ In response, the emphasis shifted to a "volume" policy, which aimed at reducing the number of benefit recipients. A new crisis of Dutch corporatism loomed large. The Social Economic Council proved unable to draft a unanimous recommendation on changes to the disability insurance scheme. This meant that the government had to act unilaterally. In the summer of 1991, after a great deal of agonizing, the government decided to restrict disability programs (WAO) and close off other routes to labor-market exit. The legal requirement that partially-disabled WAO benefit recipients accept alternative employment was strengthened. At the same time, access criteria for the WAO scheme were tightened. The proposal also included a reduction of replacement rates for all workers under the age of 50. Benefits would ultimately decrease to 70% of the statutory minimum wage plus an additional, age-related allowance. Furthermore, workers under age 50 filing disability claims would be subjected to new, stricter medical examinations. This episode had far-reaching political consequences, as the unions organized their largest post-war protest, with nearly one million participants, in The Hague. This unrest led to a profound internal crisis in the PvdA, nearly leading Kok to resign as party leader.

In 1992, the Public Audit Office (*Algemene Rekenkamer*) published a report highlighting the ambiguous distribution of power and responsibilities within the Dutch welfare system. In response, Parliament decided to apply the heaviest weapon, an All-Party Parliamentary Inquiry involving testimony gathered by numerous legal authorities. The commission undertaking the inquiry (often referred to as the Buurmeijer Commission after the name of its chairman) was crucial in triggering path-breaking institutional changes in the Dutch social-security system. In September 1993, the

³⁷ Wetenschappelijke Raad voor het Regeringsbeleid (WRR), *Een Werkend Perspectief. Arbeidsparticipatie in de Jaren '90*, Reports to the Government no. 38, The Hague, SDU, 1990.

Buurmeijer report revealed what everybody already knew, namely, that social security was being misused by the social partners for the purpose of industrial restructuring—a clear case of perverse corporatism—and advocated a fundamental recasting of bipartite governance in Dutch social security. Unsurprisingly, the social partners disputed this diagnosis, but, confronted with the Commission’s tough conclusions, they were in no position to defend the institutional *status quo*.

The 1994 elections took place in the shadow of popular discontent over welfare reform, and the Lubbers-Kok coalition was effectively voted out of power, losing 32 of its 103 parliamentary seats. The PvdA, losing 12 of its 49 seats, became the largest party. The progressive Liberals (the Democrats 66) persuaded the PvdA and the conservative-liberal VVD to form a coalition, resulting in the first government since 1917 without a confessional party as one of its members.³⁸ This new, so-called “purple” coalition, a mixture of socialist red and liberal blue, placed “jobs, jobs, jobs” at the center of its social- and economic-policy agenda when it took office in 1994. Its primary objective was maximizing employment, rather than combating unemployment through labor-supply reduction. The PvdA, however, stipulated a non-negotiable condition for its co-operation, based on a political hangover from the WAO crisis, namely, that the level and duration of social benefits remain untouched. Thus starting on the defensive, the new government was forced to turn to financial incentives for employers to create jobs, institutional reforms, and the development of active labor-market policies.

The restructuring of Dutch social security by the two “purple” governments under Wim Kok is best characterized as a case of “managed liberalization.”³⁹ This approach entailed two central components. In substantive terms, financial incentives were developed through a partial privatization of social risks, while, with respect to institutional design, a path-breaking overhaul in Dutch social

³⁸ Ruud Koole, *Politieke Partijen in Nederland: Ontstaan en Ontwikkeling van Partijen en Partijstelsel* (Utrecht: Het Spectrum, 1997).

³⁹ Romke van der Veen and Willem Trommel, “Managed Liberalization of the Dutch Welfare State,” *Governance* 12, no. 3 (1999); and OECD, *OECD Economic Surveys 2000: Netherlands* (Paris: OECD, 2000).

security administration was enacted in three steps between 1995 and 2000.⁴⁰ The majority of programmatic changes to the Dutch social-security system placed a heavier financial burden for covering sickness and disability risks on the shoulders of employers, so as to create incentives that would limit sickness- and disability-related absences, even as the state assumed a more active responsibility for the reintegration of sick-listed employees. Beginning with the privatization of the sickness scheme (through the ZW, or Sickness Benefits Act) in 1994, the responsibility for the first few weeks of workers' sickness-related absence was transferred from the sectoral funds to individual employers. In 1996, all employers became responsible for coverage of benefits up to a maximum of twelve months, at a rate of 70% of the most-recently-earned wage.⁴¹

The findings of Buurmeijer inquiry opened a policy window for a groundbreaking overhaul of the Dutch system of social security. In May 1998, the Kok administration was re-elected, thus rewarded for its excellent employment record and tough stance on social-security reform. The blessings of the Dutch "Polder Model," something of an alternative to both neo-liberal deregulation and traditional social democracy, were celebrated in the international media.⁴² While the economy grew in the 1990s by 2.9% per annum, the rate of unemployment fell to 3%, the lowest in the EU after Luxembourg. With 1.4 million new jobs, labor force participation rose from 59% to 67%, in 2000 a structural surplus of 0.3% of GDP was realized, and the public debt was reduced from 80% of GDP in 1994 to 54% in 2001.

Before the second Kok administration took office in June 1998, the social partners reached an agreement in the SER on the full privatization of the social-security implementation system, including both the intake of individual claimants and the administration of social-security provisions, as the

⁴⁰ Visser and Hemerijck, *op. cit.*

⁴¹ SZW, *Sociale Nota*, The Hague, SDU, 1998.

⁴² Gunther Schmid, "The Dutch Employment Miracle? A Comparison of Employment Systems in the Netherlands and Germany," Discussion Paper FS 96-206, Wissenschaftszentrum Berlin für Sozialforschung Berlin, 1996; Anton Hemerijck and Jelle Visser, "The Dutch Model: An Obvious Candidate for the Third Way?," *Archives Européennes de Sociologie*, vol. XL (1999), 102-121; and Joop Hartog, *Country Employment Policy Review: The Netherlands*, report for Symposium on "Social Dialogue and Employment Success" (Geneva: ILO, 1999). For a more critical reading, see Uwe Becker, "Miracle by Consensus? Consensualism and Dominance in Dutch Employment Development," *Economic and Industrial Democracy* 22 (2001): 453-483.

newly formed “Purple II” Coalition claimed that the intake of claimants could not be left to market forces. In late 1998, the basic outline for the newly integrated organizational structure was presented as part of the SWI process (“Co-operation, Work, and Income”). Subsequently, the SUWI report (“Structure of the Execution of Work and Income”), officially adopted in 1999, stated that social-insurance organizations and employment boards should join forces in so-called Centers for Work and Income (CWIs). The new “Work and Income (Implementation Structure) Act,” which radically altered the way in which a number of benefit schemes are implemented, came into force on 1 January 2002. The new Act reduced the roles of the social partners, while granting more responsibility to the Ministry of Social Affairs and Employment. The Work and Income Board (RWI), with representatives from employers, employees, and local authorities, was set up to help formulate overall policy directions in the areas of work and income but lacked any real executive authority.⁴³

Like most Continental welfare states, the Dutch welfare state lacked a legacy of active labor-market policies until the early 1990s. The Dutch Public Employment Service (PES) had been a state monopoly since 1930. Since the mid-1970s, a dormant state monopoly ran job-placement offices, shunned by employers and skilled workers and overrun by the unemployed for which little could be done. Then, after long preparation, in 1991 a new tripartite employment service came into being. While the demonopolization of placement services and the tenuous combination of functional and regional decentralization represented a major break in Dutch labor-market policy, corporatist innovation in this area failed to meet expectations. A 1995 official review of the new tripartite structure, written by a commission chaired by former Minister of the Interior Van Dijk (CDA), was overwhelmingly negative. The commission argued that the new PES had failed to take charge, decentralization had gone too far, finances were poorly managed, and decision-making procedures were cumbersome and unclear. The social partners were furious about the Van Dijk commission’s critique, which led the ambitious Social Democratic Minister of Social Affairs and Employment, Ad Melkert, to seek alternative solutions rather than patching up incipient corporatist arrangements.

⁴³ SZW, *Sociale Nota*, The Hague, SDU, 2001.

From the advent of the period of “purple” coalition governments, Melkert launched a number of labor-market policy instruments that were to remain independent of the tripartite PES.⁴⁴ Special “activation” programs, so-called “Melkert jobs,” were designed to promote participation among low-skilled workers, women, younger workers, foreign nationals, the long-term unemployed, and others who stood poor chances of labor-market success. On the demand-side, the “jobs, jobs, and more jobs” slogan was embodied in increased support for wage moderation through reductions in employers’ social contributions and greater tax incentives for workers to accept jobs, particularly at or near the minimum wage.

The introduction of the Jobseekers Employment Act (WIW) in 1998 marked a critical step in the shift in state policy focus from “active” to “activating.”⁴⁵ Henceforth, each new WIW entrant is to undergo an assessment interview, which is officially the responsibility of the municipalities but in practice is often delegated to social-service and employment organizations. In this interview, a person’s chances for employment or further education are assessed, after which an individual route to either work or social activation is sought. Participation in this scheme is obligatory for the unemployed, and a refusal can result in the withdrawal of the right to benefits.⁴⁶

Since the mid-1990s, labor market flexibility has become an integral part of the new policy mix of labor-market regulation and has enjoyed significant support from the social partners. In the meantime, the political exchange logic behind wage moderation changed character. Increasingly, wage moderation was matched by lower taxes and social contributions, made possible by improved public finances and a broader tax base, so as to “grease the wheels” of corporatist concertation. In 1995 unions and employers signed the first collective agreement for temporary workers, which introduced a right of continued employment and pension insurance after four consecutive contracts or 24 months of service. The collective agreement for temporary work prepared the ground for the 1996

⁴⁴ Visser and Hemerijck, *op. cit.*

⁴⁵ Henk Spies and Rik van Berkel, “Workfare in the Netherlands—Young Unemployed People and the Jobseeker’s Employment Act,” in Ivar Lødemel and Heather Trickey, eds., “*An Offer You Can’t Refuse*”: *Workfare in International Perspective* (Bristol: The Policy Press 2000).

⁴⁶ SZW, *Sociale Nota*, The Hague, SDU, 2001.

agreement on “Flexibility and Security” which in turn paved the way for a new Working Hours (Adjustment) Act in 2000. This measure gave part-time workers an explicit right to equal treatment in all areas negotiated by the social partners, including wages, basic social security, training and education, subsidized care provision, holiday pay, and second-tier pension rights. It is important to emphasize that the initiative for “flexicurity” came from the social partners on the basis of an innovative collective agreement, which then gained the status of law through state legislation. Together with the incremental individualization of the tax system since 1984, “flexicurity” legislation has contributed to the “normalization” of part-time employment in the Netherlands.

In the area of pensions, the purple coalition committed itself to guaranteeing the preservation of basic, public-sector pensions (governed by the AOW, or General Old Age Pension Act). Unlike that of Germany, the Dutch pension system combines a general, revenue-financed, basic pension guarantee with funded extensions of mandatory, earnings-related, occupational pensions. The government’s goal was to enable public pensions to increase proportionally with earnings. Expected increases in the public financing burden resulting from demographic aging were to be dealt with through a number of measures, including efforts to increase labor-force participation (especially by limiting early-retirement schemes), lowering interest payments through public-debt reduction, the establishment of a public pension-savings fund, and a broadening of the financing of the AOW. This last goal would be achieved by fixing pension premiums at their 1997 level of 18.25%.

Anxious to defend their much-cherished authority over supplementary pensions, the social partners within the Foundation of Labor formulated their own proposals for cost-containment and the modernization of supplementary pensions. They strongly opposed a forced change in the basis of benefit calculation from final salaries to average wages. They did agree, however, to increase the coverage of supplementary pensions and modernize benefit rules in order to increase flexibility and individual choice, while controlling pension expenditures and their contribution to total labor costs. This agreement led in turn to a “covenant” between the social partners and government at the end of

1997, which, like earlier accords, was concluded under a strong “shadow of hierarchy.”⁴⁷ This “covenant” was a compromise in which the government promised not to reduce the tax deductibility of pension premiums, in exchange for the social partners’ agreement to modernize pension schemes and limit the extent to which benefits would be calculated based upon final salaries.

Despite its effectiveness in terms of economic and employment growth, the magic of governing without confessional parties and the novelty of social liberalism in Dutch politics rapidly faded in 2002, an election year. As unemployment declined to nearly 3%, tight labor-market conditions strained the unions’ willingness to agree to moderate wage bargains. Even as other countries have begun to follow the Dutch example of wage-cost moderation, Dutch labor costs per-unit-product have, since 1997, been rising faster than the EU average.⁴⁸ Most critically, the competitiveness of the Netherlands *vis-à-vis* Germany, its main trading partner, fell by more than 16%. In the wake of the economic downturn of 2001, these developments spurred the first increase in unemployment since 1994, and the number of jobless claims was rising by 7000 per month by late 2002. These undesirable economic effects quickly began to reverberate across the Dutch political arena. In the wake of the stock market’s downward spiral and the terrorist attacks in the United States on 11 September 2001, the non-conformist, right-populist, Islamophobic politician Pim Fortuyn mobilized hidden anxieties and frustrations with the government. When, nine days before the elections, Fortuyn was murdered by a radical environmental activist, the elections of 15 May assumed an extremely emotional character, ultimately leading to a landslide victory of the List Pim Fortuyn (LPF), which won 26 new parliamentary seats to become the second largest party in Parliament. The Christian Democratic CDA returned to power with 43 seats. The “purple” coalition parties, however, were devastated, with the PvdA suffering the greatest loss (from 45 to 23 seats), the VVD declining from 38 to 24 seats, and D’66 representation in parliament halved from fourteen to seven seats. In July

⁴⁷ Bart van Riel, Anton Hemerijck, and Jelle Visser, “Is There a Dutch Way to Pension Reform?,” in Gordon L. Clarke and Noel Whitside, eds., *Pensions in the 21st Century: Re-drawing the Public-Private Divide* (Oxford: Oxford University Press, 2003).

⁴⁸ OECD, *OECD Economic Surveys 2002: Netherlands* (Paris: OECD, 2002).

2002, the VVD agreed to become the third coalition partner in a right-wing coalition with the CDA and the LPF, led by the Christian Democrat Jan-Peter Balkenende. The very short-lived Balkenende government was unable to have much of an impact in the area of economic and social policy, however. In office for only 87 days, the government fell as a result of a tussle within the populist LPF and a lack of leadership skills on the part of the young prime minister.

The German State and the Dilemmas of Corporatist Social-Protection Reform

From its inception, the post-war German Social-Market Economy was designed to support a self-regulating, virtuous circle between vibrant job growth and generous social policies, a model that worked well in the 1950s and 1960s and resisted relatively well through the 1970s and 1980s despite the economic crises of the time.⁴⁹ The chief policy-making goal before 1990 was to preserve the existing system and the social peace that it had supported by equitably dividing wealth between wages and profits and cushioning workers from the effects of (relatively rare) unemployment.⁵⁰ Although in the late 1980s the German model began to show signs of strain, including rising social contribution rates and increasing unemployment, it was reunification in 1990 that forced the system into full-blown crisis, as millions of poorly adapted Eastern workers entered the labor market, scores of uncompetitive Eastern firms went bankrupt, and rising economic vulnerability put intense pressure on the welfare state. As time went on, structural unemployment, pressures on social contributions, and increasing welfare expenditures came to represent serious threats to the German model's celebrated capacity for self-regulation.

In response, successive governments have undertaken initiatives designed to remedy the failures of corporatism and readjust the German political economy to new economic realities. State

⁴⁹ Based on data taken from Fritz W. Scharpf, "Economic and Institutional Constraints of Full-Employment Strategies: Sweden, Austria, and West Germany, 1973-1982," in Goldthorpe, ed., *op. cit.*, 258.

⁵⁰ In the words of Ludwig Erhard, Economics Minister in the 1950s and one of the conceptual "fathers" of the *soziale Marktwirtschaft*, "The restructuring of our economic order must thus create conditions such that the purchasing power associated with rapid economic growth can overcome obstacles and finally end the resentment between 'poor' and 'rich'." Ludwig Erhard, *Wohlstand für Alle*, ed. Wolfram Langer (Düsseldorf: Econ-Verlag, 1957), 7. Translation the authors'.

intervention in the German social-protection system began, somewhat tentatively, under the center-Right governments of Chancellor Helmut Kohl. Spurred on by the economic dislocations resulting from reunification, Kohl expanded social programs and labor-market schemes designed to absorb large numbers of unemployed, preserve social stability, and begin the task of adapting the Eastern workforce to a modern capitalist economy.⁵¹ By the mid-1990s, around 450,000 people were participating in federal training programs, with another 400,000 temporarily employed in temporary job schemes. As a result, as early as 1991 spending by the BA had become the largest single element of financial transfers from West to East, and by the end of 1994, the total volume of support offered by labor-market policies was actually above the level of registered unemployment.⁵²

As the 1990s wore on, it became clear both that high non-wage labor costs and exploding expenditure levels were unsustainable, while structural unemployment bore witness to the system's failure to manage adjustment in the face of strained public finances and slowed growth. In response, the current center-Left government of Chancellor Gerhard Schröder has stepped up state intervention in labor-market policy, building on the efforts of its predecessor. Authorities realized that such an approach would inevitably expose many problems, such as the unemployment "hidden" by existing BA training and make-work schemes, before it could begin to solve them. Despite the political risks, however, the government has considered the potential price of doing nothing to be greater.⁵³

Intensified state intervention grew out of a series of failed efforts to support corporatist bargaining over wages and social-policy reform. In 1995, the government created the *Bündnis für Arbeit*, or "Alliance for Jobs," a standing forum for the government and social partners jointly to

⁵¹ Quickly dropping to 60% after reunification, Eastern industrial output had recovered to only 68% of Western levels by 1993, resulting in the elimination of 3.9 million jobs between 1990 and 1993. By February 1996, unemployment in the East had reached 17%, with an additional 800,000 people participating in make-work schemes. Christopher Flockton, "Economic Management and the Challenge of Reunification," in Gordon Smith, William E. Patterson, and Stephen Padgett, eds., *Developments in German Politics 2* (Durham, N.C.: Duke University Press, 1996), 214-215.

⁵² Matthias Knuth, "Active Labor Market Policy and German Unification: The Role of Employment and Training Companies," in Lowell Turner, ed., *Negotiating the New Germany: Can Social Partnership Survive?* (Ithaca, N.Y.: Cornell University Press, 1997), 71-73.

⁵³ As one highly-placed labor-market-policy official put it, "one cannot wash one's hands without getting wet." Interview, Eden Andreas, Bundesanstalt für Arbeit, 18 April 2001.

develop social-policy and labor-market reforms. Revived under Schröder in 1998, the *Bündnis* seemed to augur a period of reinvigorated corporatist bargaining. Despite much fanfare, however, the forum produced very little in terms of tangible policy results. Neither employers (who wish above all to increase labor flexibility and limit social contributions and tax burdens) nor unions (who are more concerned with protecting the wages of their older industrial membership than promoting jobs in emerging, non-unionized sectors) demonstrated much interest in making sacrifices for the noble but less proximate goals of reducing unemployment and ensuring the viability of social protection. As a result, the institution tended to degenerate into a talking-shop. In early 2003, the government finally allowed the organization to lapse, thereby recognizing a failure that been evident for some time.⁵⁴

The failure of the *Bündnis* reflects the broader dilemmas faced by the German state in shaping labor-market and social policies. Because the purview for state intervention in the labor market is limited by both the principle of *Tarifautonomie* and the prerogatives of the tripartite *Bundesanstalt für Arbeit*, or Federal Labor Office (hereinafter BA), German governments have traditionally pursued reform by promoting bargaining among the social partners rather than through imposition. A characteristic example of this strategy has involved reforms of the extensive network of early-retirement schemes. Instituted in the 1980s, these programs exploded in the 1990s, with 809,000 people receiving benefits in 1999, not including disability pensions,⁵⁵ and around 20% of the population aged 55-65 in the West and 40% in the East participating in related programs by 1996.⁵⁶ Although such policies have the politically desirable effect of reducing the unemployment *rate*, in which participating workers do not officially count, they are extremely expensive and have at best

⁵⁴ Some observers went so far as to portray the *Bündnis* as a cartel in which unions and employers defend established interests rather than address unemployment and which the government uses to create a veneer of social dialogue. See “Der Fehler ist System: Das Bündnis für Arbeit schafft keine Jobs,” *Die Zeit* 10 (1 March 2001), 1.

⁵⁵ OECD, *OECD Economic Surveys 2000-2001: Germany* (Paris: OECD, 2001), 37. These policies have resulted in one of the lowest labor-market participation rates in the OECD for workers 55 and older (52.9% in 1995). See Philip Manow, “Social Insurance and the German Political Economy,” Max-Planck-Institut für Gesellschaftsforschung Discussion Paper 97/2, November 1997, 39.

⁵⁶ Philip Manow and Eric Seils, “Adjusting Badly: The German Welfare State, Structural Change, and the Open Economy,” in Scharpf and Schmidt, eds., vol. II, *op. cit.*, 294-295. Another 800,000 in 1999 were participating in various training and subsidized job schemes managed by the BA. See OECD, *OECD Economic Surveys 2000-2001: Germany*, 37.

questionable effects on actual joblessness, since firms have little incentive to replace workers “retired” at the expense of the social-security system,⁵⁷ particularly in strained economic circumstances.

In the wake of the post-reunification influx of unemployed Eastern workers, the federal government attempted to limit recourse to these schemes, in the process subtly assuming a degree of authority from the social partners. In particular, the government has worked within the BA to end some early-retirement programs and boost subsidies for part-time jobs for older workers with the aim of increasing their rate of exit from traditional employment while providing them with an income in the labor market. Unfortunately, this approach had the perverse effect of actually *increasing* the number of early retirees, since the greater availability of part-time work has enabled many older workers to compensate for the loss of income that early retirement entails.⁵⁸ Although the dire state of the Eastern economy has made curtailing these programs politically tricky,⁵⁹ the government has continued to tighten eligibility restrictions.⁶⁰

Recent governments have also worked to reform corporatist labor-market arrangements by promoting low-wage jobs through reimbursing employers’ social contributions and granting tax exemptions to low-wage workers. Although the Kohl government made tentative moves in this direction, such efforts have gained momentum under the Schröder administration. For example, in April 1999 the government extended the obligation to pay social-security contributions to “casual” employees, or those working fewer than fifteen hours per week, while shifting public revenues to the social-security system by reimbursing the taxes and contributions of all workers making slightly more

⁵⁷ *Ibid.*, 31.

⁵⁸ There are two categories of German early retirement programs, those for workers with “reduced capacity” to work (claims that are often specious) and benefits for those unable to find part-time work but who wish to retire from their full-time positions. Early retirees often base their claims on reduced capacity even as they continue to work part-time.

⁵⁹ Bernard Ebbinghaus, “Any Way Out of ‘Exit from Work’? Reversing the Entrenched Pathways of Early Retirement,” in Scharpf and Schmidt, eds., *op. cit.*, vol. II, 534-535.

⁶⁰ Christine Trampusch, “Die Bundesanstalt für Arbeit und das Zusammenwirken zwischen Staat und Verbänden in der Arbeitsmarktpolitik von 1952 bis 2001,” Max-Planck-Institut für Gesellschaftsforschung Working Paper 02/5, May 2002.

than DM630 (about €20) per month.⁶¹ The hope was to collect social-security contributions from lower-wage workers, improve collection from the so-called *Scheinselbständige*, or “supposedly self-employed” (a category often abused as a shelter from taxes and social contributions), and encourage job creation by preserving exemptions for workers earning the lowest incomes.⁶²

In other areas of labor-market policy, the state has been able to adopt a more direct approach to creating jobs, working to compensate for the failures of corporatist wage bargaining by expanding policies of labor-market activation. While the Kohl government focused efforts in this area largely in the East, the current administration has developed similar programs across the German economy. For example, the recent *Sofortprogramm zum Abbau der Jugendarbeitslosigkeit*, or “Immediate Program for the Reduction of Youth Unemployment” (suggestively referred to as “JUMP”),⁶³ created a wide range of training and apprenticeship measures, additional wage subsidies for firms that hire unemployed youth, and job-counseling services, devoting DM2 billion (€1.02 billion) annually (of which DM600 million derives from the European Social Fund) to the goal of creating 100,000 new jobs for workers under 25.⁶⁴ Whereas the BA has traditionally administered such programs with almost total autonomy, JUMP is run jointly by BA and the Labor Ministry, reflecting the same gradual centralization of authority seen elsewhere in labor-market policy. The BA claims that 43,000

⁶¹ OECD, *OECD Economic Surveys, 1998-1999: Germany* (Paris: OECD, 1999), 85, 177.

⁶² For a discussion, see Wade Jacoby, “Institutional Transfer and Institutional Experimentation: Four Cases from Eastern Germany,” Paper presented at the workshop “Semisovereignty Revisited,” University of Birmingham, April 2002, MS, 17; and Wolfgang Streeck, “High Equality, Low Activity: The Contribution of the Social Welfare System to the Stability of the German Collective Bargaining Regime,” MS, 10-11.

⁶³ Joblessness among workers under 25 rose significantly in the 1990s, reaching 10.4% in 1998 with 476,000 without either jobs or apprenticeship places. More alarmingly, between 1991 and 1998 the number of young applicants registered for apprenticeship slots increased from 541,790 to 796,400, while the number of available positions decreased from 830,940 to 603,900. Bundesanstalt für Arbeit, “Ausbildung, Qualifizierung und Beschäftigung Jugendlicher,” Informationen für die Beratungs- und Vermittlungsdienste der Bundesanstalt für Arbeit, 2/99, 13 January 1999, 69, 72.

⁶⁴ The law was intended to last twelve months but has been extended each year by agreement between the BA and the government. See Bundesanstalt für Arbeit, “Sofortprogramm zum Abbau der Jugendarbeitslosigkeit: Zwischenergebnisse aus der Begleitforschung,” Informationen für die Beratungs- und Vermittlungsdienste der Bundesanstalt für Arbeit, 20/00, 17 May 2000.

successful placements were made in 1999 and that, between 1998 and 2002, 406,000 people benefited from the program.⁶⁵

Reflecting a similar pattern of increased activism on the part of the federal government, the Law for “Job-Activation, Qualification, Training, Investment, and Placement (*Vermitteln* in German), or *Job-AQTIV Gesetz*, has focused on reintegrating the long-term unemployed in order to shrink the number of workers on the unemployment rolls and reduce benefit expenditures. Henceforth, regional or local branches of the BA must create personalized profiles for each job seeker, offering “appropriate” job openings and providing tailored advice and counseling services. In return, the unemployed person is obligated to accept “reasonable” job offers and make a concerted effort to find work or else risk seeing his benefits suspended.⁶⁶ The efficacy of this measure remains to be seen, but its contractual posture toward the unemployed—connecting the right to benefits to job-seekers’ obligations—reflects a major departure from the traditional view that unemployment (and other social) benefits are “rights” paid for by years of contributions.

Furthermore, while the BA still officially manages many such schemes, the federal government has recently assumed an increased degree of authority for their financing and administration in the hopes of increasing the BA’s responsiveness to worsening labor-market conditions. In 1993, for example, the government passed a law providing that the Labor Ministry would henceforth directly set the BA’s annual budget.⁶⁷ By 1999, the federal government was financing nearly a third of all employment programs, traditionally financed overwhelmingly by the BA, and has steadily increased the share of resources devoted to high-priority, active policies labor-

⁶⁵ Bundesanstalt für Arbeit, “JUMP: Das Sofortprogramm zum Abbau der Jugendarbeitslosigkeit,” special issue of *Direkt: Fördern und Qualifizieren* 10 (April 2000), 2; and Bundesministerium für Arbeit und Sozialordnung, “Jump ist ein voller Erfolg,” press release, 15 February 2002.

⁶⁶ The law also introduced new instruments to train and retrain workers, increased subsidies to employers to reduce non-wage labor costs and encourage hiring, and instituted additional job-creation schemes. See SPD und Bündnis 90/Die Grünen Bundestagsfraktionen, “Zur Reform der Arbeitsförderung: Eckpunkte der Fraktionen SPD und Bündnis 90/Die Grünen vom 3. Juli 2001 für ein Job-Aktivieren, Qualifizieren, Trainieren, Investieren, Vermitteln-Gesetz,” July 2001.

⁶⁷ Trampusch, *op. cit.*, 28. Previously, the government was obligated to cover the BA’s annual deficits but had no authority to set its budget.

market.⁶⁸ It has also partially shifted welfare funding from social contributions to general taxation in an effort to reduce non-wage labor costs. In 1999, for example, a new tax (the controversial *Ökosteuer*) on environmentally “dangerous” activities and materials funded the replacement of 0.8% of annual pension contributions with federal tax monies. The tax also aimed to compensate for the loss of revenue resulting from caps on social-contribution rates implemented as part of the 2001 pension reform in order to promote job-creation and to provide a shot in the arm for social-security funds by expanding their contribution base.⁶⁹

In 2002, the state began to assert even greater control over the BA after it was discovered that the agency had grossly inflated job-placement statistics.⁷⁰ Since March of that year, the BA has been governed by a three-person executive board appointed directly by the federal government. The following summer, the government established the “Hartz Commission,” an independent panel of experts from government ministries, employers’ associations, and unions, to make recommendations for further labor-market reforms. The Commission recommended reinforcing state influence over labor-market policy, including increased federal funding for active labor-market policies, the development of state-run temporary job agencies to promote flexible employment, and further reforms of the BA’s administration and employment services.⁷¹ To be sure, such policies in part reflect the government’s response to mounting public pressure, but they also indicate real concern

⁶⁸ Uwe Blien, Ulrich Walwei, and Heinz Werner, “Labour Market Policy in Germany” (Nürnberg: Bundesanstalt für Arbeit, 2002), 6.

⁶⁹ The 2000 tax reform, which reduced tax rates and liberalized restrictions on firms’ and banks’ sale of stock held in other companies, was another element of efforts to encourage investment and job growth.

⁷⁰ The highest German administrative regulatory agency concluded that as many as 70% of cases had been incorrectly reported and that it was doubtful whether the statistics issued by the BA “can at all be used as the basis for the law-making and budgetary decisions of the Bundestag and the government.” The report found confirmation in Labor Minister Walter Riester’s admission that “it cannot be excluded that workers in the labor office had an interest in falsely reporting statistics on successful job placement.” The scandal led to the resignation of BA President Bernhard Jagoda and proposals for major reforms of the BA. See “Bundesanstalt gerät immer stärker ins Kreuzfeuer der Kritik,” *Frankfurter Allgemeine Zeitung*, 6 February 2002, 13; and “Jagoda weist Rücktrittsforderungen zurück,” *Frankfurter Allgemeine Zeitung*, 7 February 2002, 13.

⁷¹ See Hartz Commission, “Moderne Dienstleistungen am Arbeitsmarkt: Vorschläge der Kommission zum Abbau der Arbeitslosigkeit und zur Umstrukturierung der Bundesanstalt für Arbeit,” August 2002. The qualified character of the Commission’s tripartism could also be seen in the selection of Peter Hartz, the personnel director at Volkswagen, with which Schröder has long had business ties, rather than a board of union and employers’ association leaders to direct its work.

about the apparent incapacity of Germany's tripartite labor-market institutions effectively to govern themselves. Less than two years after their introduction, the first round of Hartz measures seem to have had some effect, evidenced in a June 2003 reduction of 33,000 in the number of jobless with no concomitant upturn in the economy.⁷²

More recently, under the banner "Agenda 2010," the administration has passed additional reforms which aim to promote employment, reduce non-wage labor costs, and liberalize regulations on economically-motivated layoffs and shop hours.⁷³ In a series of measures passed in December 2003 after weeks of negotiations between the government and opposition CDU/CSU, the length of eligibility for primary unemployment insurance (*Arbeitslosengeld*) was reduced to twelve months for all workers, with the exception of those older than 55, who will enjoy eighteen months of eligibility. Moreover, unemployment-assistance benefits (*Arbeitslosenhilfe*), paid to workers at the end of their eligibility for the more-generous unemployment insurance, will, over a two-year period, be reduced to the level of *Sozialhilfe*, the basic income-support program. The measures also provided for the liberalization of protections against layoffs in Germany's smallest firms and the loosening of the country's notoriously strict shop-opening laws, with the social partners in a given sector limited to a passive veto authority.⁷⁴ As with the government's earlier measures, with "Agenda 2010" Schröder's strategy has been willing to risk significant political capital in order to see through reforms.

⁷² Officials attribute this positive outcome to the government's active labor-market policies. The remaining Hartz reforms were passed in October and December 2003. See Bundesanstalt für Arbeit, "Die Entwicklung des Arbeitsmarktes im Juni 2003," press release, 8 July 2003; and "Something Stirs: German Unemployment Is Responding to Chancellor Schröder's Measures," *The Economist*, July 26th-August 1st 2003, 48.

⁷³ Many of the October 2003 labor-market reforms were devised in response to the Hartz Commission's recommendations. The "Agenda 2010" program also involves proposals for health insurance, pensions, and income support.

⁷⁴ In order to secure the passage of the package's labor-market measures, the government was forced to make concessions on its tax-reform proposals that significantly reduced the total size of the reduction. It also made some concessions on some of its labor-market measures, including an obligation for the long-term unemployed to accept any legal job, rather than only those that are "appropriate" to their employment history. Other parts of the package, which did not require the *Bundesrat's* approval, had been passed unchanged by the *Bundestag* in October. For a discussion, see Thibaut Madelin, "Allemagne: L'opposition impose à Schröder de sérieuses concessions sur le marché du travail," *Les Echos*, 16 December 2003, 5; and "Von großen und kleinen Reformen: Die Agenda 2010 und was aus ihr geworden ist," *Frankfurter Allgemeine Zeitung*, 20 December 2003, 3.

Despite their relatively aggressive character, recent German measures have not resolved Germany's employment crisis. The country continues to struggle with record levels of unemployment, at 10.4% in May 2003 with 4.34 million on the official unemployment rolls,⁷⁵ persistently high non-wage labor costs, and rates of economic growth that range from sluggish to non-existent. Nonetheless, the cumulative effects of early reforms under Kohl and, more significantly, the measures undertaken by the Schröder administration, are beginning to make themselves felt. In addition to the payoffs of the early Hartz reforms, the prioritization of active labor-market policy has begun to remedy some of the German labor market's most trenchant problems. Although still at alarming levels, long-term unemployment decreased between 1998 and 2000, with those without jobs for twelve months or longer shrinking from 52.6% to 51.5% of total unemployment.⁷⁶ Efforts to promote part-time work have also begun to pay off, with the percentage of total employment represented by part-time jobs rising from 15.8% in 1997 to 17.6% in 2000.⁷⁷ Furthermore, despite an upturn in overall unemployment, joblessness among those over 50 decreased by 6% in 2002, and the number of workers aged 16-25 removed from the rolls increased by 10% between 2001 and 2002.⁷⁸

No longer able to rely upon a system of tripartite labor-market policy-making and increasingly vulnerable to criticism of its record on employment, Schröder's government has thus gradually assumed a variety of responsibilities that formerly lay within the domain of the social partners, increased public resources devoted to the labor market, and developed a range of new policies that parallel existing programs managed by the BA. Rising joblessness and increasing pressures on social-policy financing seem to confirm the suggestion of some observers that the high-wage, high-skill, high-employment economy upon which Erhard's *soziale Marktwirtschaft* was

⁷⁵ "Keine Wende auf dem Arbeitsmarkt: Aktive Arbeitsmarktpolitik hellt Statistik etwas auf," *Frankfurter Allgemeine Zeitung*, 6 June 2003, 13.

⁷⁶ OECD, *OECD Employment Outlook* (Paris: OECD, June 2001), Statistical Appendix, 227.

⁷⁷ *Ibid.*, 224.

⁷⁸ Bundesanstalt für Arbeit, *2002 Annual Report* (Nürnberg: BA, 2003), 8, 11.

founded may no longer be sustainable.⁷⁹ In any event, German corporatist labor-market institutions have clearly failed to adapt, leaving a policy vacuum that the state has begun to fill.

Recent pension reform has entailed even more direct state intervention, reflecting an erosion of the traditionally consensual rapport between the major political parties in this area and increasing strains between the state and social partners. The differences between trajectories in labor-market and pension policy result from the administrative structure of the pension system, which has long been directed by government experts—albeit in close consultation with the opposition, unions, and employers—in contrast to the tripartite administration of the labor market. Unimpeded by limitations such as *Tarifautonomie*, the German state has adopted a “go-it-alone” approach to pension reform, excluding unions and the opposition from the influence that they have traditionally enjoyed.

Created in 1957, the German pay-as-you-go pension system remained relatively untouched until 1989, when the Kohl administration raised the retirement age to 65, established a 0.5% per-year penalty for early and an equivalent bonus for later retirement, and slightly modified the benefit-calculation system. Passed before reunification, this relatively modest measure, which preserved an average replacement rate of 70% and involved significant concessions to the opposition SPD and the trade unions, was unable to cope with the huge additional burden of Eastern workers for whom the system assumed responsibility after 1990. When it assumed power in 1998, the new center-Left government understood that the consensual tinkering of the previous decade could no longer ensure the system’s future viability.⁸⁰

⁷⁹ For a particularly pessimistic perspective on the German economy’s capacity for adjustment, see Wolfgang Streeck, “The German Economic Model: Does It Exist? Can It Survive?” in Colin Crouch and *idem*, eds., *Political Economy of Modern Capitalism: Mapping Convergence and Diversity* (London: Sage, 1997), 33-54.

⁸⁰ Recent state intervention has also involved efforts to control spiraling health-care costs by rebalancing corporatist arrangements. In 1989, for example, the Kohl government passed a measure that limited physicians’ autonomy and introduced elements of competition and patient choice, while working within the existing corporatist framework. For details, see Susan Giamo and Philip Manow, “Welfare State Adaptation or Erosion? The Case of Health Care Reform in Britain, Germany, and the United States,” Paper presented at the American Political Science Association Annual Meeting, 28-31, Washington, D.C., August 1997.

In August 2000 Schröder's government released its pension proposals, which went far beyond Kohl's 1989 measures and contravened the preferences of the SPD's union allies.⁸¹ The initial draft envisioned a reduction in total average benefits from 70% to 64%,⁸² and, from this adjusted rate, an additional annual reduction of 0.3% for those retiring in or after 2011 (the disputed *Ausgleichsfaktor*, or "Equivalence Factor").⁸³ The measure also created a legal right to firm-level pensions and introduced caps on contribution rates and subsidies for low-wage workers' pensions. The reform's centerpiece and most controversial part, however, was the unprecedented introduction of supplemental private accounts, into which each worker would deposit up to 4% of his annual income (beginning with 0.5% in 2001 and increasing by 0.5% annually until 2008), supplemented by generous government subsidies and tax exemptions.⁸⁴ In addition, the government was to pay annual supplements to the system, increasing from DM8.1 billion in 2001 to DM43.7 billion by 2030.⁸⁵

The proposals elicited sharp protests, as women's groups, the opposition CDU/CSU, pensioners' associations, and the Left of his own party demanded major changes to the measures.⁸⁶ Decrying a "privatization of social risk,"⁸⁷ unions demanded the preservation of total average benefits at 67% the quashing of the *Ausgleichsfaktor*, said to disadvantage younger workers, increased state and employer support for firm-level pensions, and the abandonment of the proposal for private accounts. This last demand was the highest priority, for unions suspected that employers' exemption

⁸¹ The reforms incorporated and extended a measure passed by the Christian Democrats in 1997 but quashed by the incoming administration in 1998, suggesting that increased intervention in the pension system crosses partisan lines.

⁸² This actuarial figure is deceptive, since it represents the benefits of a notional worker having contributed for 45 years. Most workers' benefits would thus actually be lower.

⁸³ This provision meant that each cohort's benefits would be 0.3% lower than those of the previous year's retirees, with each individual retiree's benefits remaining constant.

⁸⁴ Bundesministerium für Arbeit und Sozialordnung, "Die Rentenreform 2000: Ein mutiger Schritt zu mehr Sicherheit" (Bonn: Bundesministerium für Arbeit und Sozialordnung, August 2000).

⁸⁵ SPD und Bündnis 90/Die Grünen Bundestagsfraktionen, "Entwurf eines Gesetzes zur Reform der gesetzlichen Rentenversicherung und zur Förderung eines kapitalgedeckten Altersvorsorgevermögens," 14 November 2000, 4.

⁸⁶ In one famous incident during a congress of the moderate public-service union, the Chancellor declared in response to heckling from the audience, "It is necessary, and we are going to do it. Basta." See "Schröder bleibt bei der Rentenreform hart: 'Wir werden es machen. Basta,'" *Frankfurter Allgemeine Zeitung*, 6 November 2000, 1.

⁸⁷ Interview, Ludger Loop, Gesellschaft für Innovation, Beratung und Service, IG Metall, 13 March 2001.

from contributing represented the beginning of the end for Germany's cherished system of parity financing.⁸⁸

Declaring itself willing to discuss "the details, but not the principle" of the reform, the government adopted a multi-pronged strategy to secure the reform's passage while making the fewest possible concessions. The first aspect of this approach involved separating the reform into two laws. The first law, involving changes in the basic pension régime, was opposed by the CDU/CSU, and, to a lesser extent, by the unions. Since the German constitution makes the federal government responsible for guaranteeing social protection and because the basic pension scheme does not affect the financial burdens of the *Länder*,⁸⁹ however, the law did not need the approval of the upper house of Parliament, or *Bundesrat*, where the CDU had the votes to block it. As a result, the reform of the basic pension scheme, adopted by the *Bundestag* on 26 January 2001 and heralded by Riester as "the greatest social reform of the post-war era,"⁹⁰ incorporated almost none of the CDU's priorities.

By contrast, the second law, which created the supplemental accounts, required a majority in both houses, and in particular the votes of Berlin and Brandenburg, both of which were governed by SPD-CDU "grand coalitions." As a result, the government could ignore neither the *Länder*'s concerns about the increased costs that the reform would entail nor the CDU's opposition to both laws, centering on the *Ausgleichsfaktor*, said to deal a serious blow to "generational justice," the law's alleged lack of consideration for families with children, and the use of federal money to subsidize pensioners below the poverty level.⁹¹ In navigating the law through the *Bundesrat*, the government employed a strategy that permitted it to preserve the law's core provisions. It agreed to

⁸⁸ In the words of one union leader, "the welfare state has the task of holding society together." Accordingly, unions feared that the partial exit of employers from pension financing would jeopardize the integrity of German society. Interview, Michael Gu gemos, IG Metall Vorstand, 19 January 2001.

⁸⁹ Much has been made of the *Bundesrat*'s ability to block legislation. As the pension reform demonstrates, however, the government's control over the ways in laws are drafted and gray areas in the constitution provide flexibility in determining which laws are subject to the upper house's approval.

⁹⁰ "Riester spricht von der 'größten Sozialreform der Nachkriegszeit'," *Frankfurter Allgemeine Zeitung*, 27 January 2001, 1.

⁹¹ In part, the incoherence of these objections reflected competition among various CDU constituencies, but it also mirrored internal disorganization resulting from a major party financing scandal that broke in 1999. One CDU member actually admitted privately that his party had no coherent positions on social-policy reform. Interview, member of CDU/CSU Arbeitsgruppe Arbeit und Soziales, 15 March 2001.

delay the application of the law until 2002 in order to relieve some of the costs of implementation to the *Länder*, at an additional expense of DM1 billion to the federal government,⁹² and provided DM21 billion to cover administrative costs and subsidies to participating workers. This federal money and the lure of the administrative jobs that the law would require prompted Berlin and Brandenburg to support the reform.⁹³ Even in the face of CDU and public opposition, the clever navigation of the legislative process had allowed the first major structural reform since the current pension system's inception.

In the case of pension reform, exclusion and control rather than consensus and compromise were thus the hallmarks of the government's approach. While the tripartite structure of German labor-market policy and the principle of *Tarifautonomie* have called for a subtle and shifting combination of incentives and intervention, significant pension reform has required a more unalloyed interventionist strategy. These policy-specific dynamics noted, the German state has played a critical role in shaping reforms in both areas, even when it has not been able alone to dictate their character. Although authorities have had to confront the constraints represented by inherited corporatist institutions, they have in some cases also been able to exploit possibilities for more unilateral action. To the extent that the German state has been able to see through policy changes, therefore, it has done so by both recognizing its limitations and working to convert institutional liabilities into assets.

Conclusion: The State and Future Prospects for Corporatist Governance

In our contribution to this volume, we have traced the experience of social-protection and labor-market reform in Germany and the Netherlands since the 1980s, emphasizing the shifting and dynamic role of the state in these two corporatist political economies. As we have shown, *Staatsentlastung*, or relieving the state of a share of the burden of policy-making, cannot be taken for

⁹² The additional money was required because the *Länder* were already suffering decreased revenues as a result of the 2000 tax reform. This DM1 billion supplement was provided in addition to existing subsidies to the pension system, which by 2001 had risen sharply to an annual DM14 billion.

⁹³ The government used a similar strategy in the case of the 2000 tax reform, for which it secured *Bundesrat* approval by granting federal money for infrastructure projects to *Länder* whose votes were needed.

granted, but rather requires skillful state action in order to encourage the social partners to adopt public-regarding strategies of collective action. This is particularly the case under hostile economic climates marked by fiscal austerity, slow or absent growth, structural unemployment, and intense pressures on welfare financing. When this strategy fails, inherited corporatist arrangements can become significant barriers to effective reform, prompting the state to adopt riskier strategies of corporatist disengagement or legislative imposition. As a result, the state may regain a degree of autonomy *vis-à-vis* the social partners in important policy areas, at the cost, however, of increased policy and administrative burdens.

As the cases of Germany and the Netherlands amply demonstrate, the particular character of state responses to corporatist failures varies significantly with both national institutional capacities and specific policy legacies. Forms of intervention can range from stimulating corporatist accords in wage-bargaining and pensions, to legislating corporatist agreements in labor-market regulation, to bypassing corporatism in labor-market policy, to the dismantling of corporatism in social-security administration. In the Netherlands, where the state is unitary but decentralized rather than federal, authorities have at times been able to intervene more directly than their German counterparts. That said, both Germany and the Netherlands have witnessed greater assertiveness on the part of state actors relative to earlier periods. At times, they have been successful in rebalancing or relaunching corporatist policy-making, while at others, they have “gone it alone” and suspended or even dismantled corporatist institutions that have failed to produce necessary reforms. While both German and Dutch policy-making have thus been vulnerable to national variants of Scharpf’s “joint-decision trap,” both states have met with considerable success in overcoming this dilemma and lent renewed momentum to the reform process. In each country, these myriad of forms of state intervention have also begun to alter the character of politics and policy-making in two political economies traditionally celebrated as exemplars of gradual, consensually negotiated political-economic change.

In retrospect, the success of the “Dutch,” or “Polder Model,” is often explained as a result of the long-term compromise of the social partners over wage moderation in the 1980s and more flexible

employment relations in the 1990s. In fact, the revitalization of corporatist wage bargaining in the 1980s and 1990s was prompted by a highly effective “shadow of hierarchy” that grew out of the 1970 Wage Law and was supported by a high degree of institutionalized capacity for autonomous state action. The state, for example, more or less forced the social partners into the path-breaking Wassenaar and New Course accords of 1982 and 1993. It is important to note, however, that the institutional framework of the bi- and tripartite institutions of the Foundation of Labor and Social and Economic Council did not have to be invented, but rather involved turning inherited corporatist structures to new purposes. The result was a synthesis of moderate wage increases with a high degree of flexibility at the micro-level, as well as a rather smooth interplay among wage setting, monetary and fiscal policy, economic growth, and moderate inflation. Since Wassenaar, however, there has been limited political intervention in wage setting. Although the Minister of Social Affairs and Employment has the authority to declare (parts of) collective bargaining legally binding (or not) for all workers and employers in a certain branch of industry, in practice extension is routinely applied. In other words, the Dutch state has still considerable power in industrial relations but has increasingly exercised this power indirectly.

In the equally important area of social security, governments in the 1990s had the courage to break with the joint control over the system exercised by the social partners. The field of social security has witnessed considerable institutional discontinuity and disagreement among unions, employers, and the government. Dutch welfare reform was an explicitly political attack on the privileged positions of the social partners and their failure to adopt needed reforms. It is not insignificant that in the past twenty years all major political parties, from Left to Right, in various grand coalitions, have participated in welfare reform, often involving significant departures from traditional paradigms of policy-making.

In the lengthy process of negotiated welfare and labor-market reform in the Netherlands, the rules of Dutch corporatism have been rewritten, and the boundaries between the respective responsibilities of the state and social partners have been redrawn. In contrast to the bipartite “de-

politicization” of collective bargaining since the early 1980s, characterized by a shift in the direction of *de facto Tarifautonomie*, the last decade has witnessed a significant re-politicization of social security, with the exception of pensions.⁹⁴ Accompanying this development has been a shift in policy paradigms, from fighting unemployment through labor-market exit, the typical continental welfare state’s response to industrial restructuring, to raising employment levels for both men and women through organized wage restraint since the 1980s, to a social-liberal mixture of fiscal austerity, “flexicure” labor markets, and activating welfare policies in the 1990s. In each case, the policy agenda was set by the government rather than the social partners. However, the respective cabinets of Ruud Lubbers and Wim Kok could never have been successful without the support of the social partners on a majority of social and economic policy issues. Furthermore, the second Kok administration’s failure to achieve a structural reduction in inactivity rates, despite a fundamental overhaul of the Dutch social-security system, demonstrates that suspending corporatism is not a panacea.

In contrast to the significant institutional resources available to their Dutch counterparts, German policy-makers have had to work within an institutional context marked by greater institutional, legal, and political impediments to unilateral state action. In the area of labor-market policy, German authorities continue to be constrained by the prerogatives of the tripartite Federal Labor Office and the legally enshrined principle of *Tarifautonomie*. As a result, German reform strategies in the early to mid-1990s tended to focus on efforts to revive moribund corporatist institutions and initiatives designed to reduce unemployment through the wage-bargaining process, in the Dutch manner. With the failure of this strategy in the late 1990s, the German government has turned to a series of “second-best” labor market policies, involving a series of independent policy initiatives to reduce unemployment, including job-creation and training programs, pressures on the unemployed to accept available work, and limiting recourse to traditional mechanisms of labor-supply

⁹⁴ Hans Slomp, “The Netherlands in the 1990s: Toward ‘Flexible Corporatism’ in the Polder Model,” in Stefan Berger and Hugh Compton, eds., *Policy Concertation and Social Partnership in Western Europe: Lessons for the 21st Century* (New York: Berghan, 2002).

reduction, notably early-retirement schemes. While somewhat limited in scope, all of these policies have been undertaken by state actors largely independently of the social partners, who have seen their authority over German labor-market policy shrink considerably.

In the domain of social policy, likewise, state intervention has been critically important in shaping reform outcomes. In this policy area, the state is not constrained by the kinds of legal impediments that it faces in labor-market policy. As a result, governments have been able to see through more ambitious reforms, again without significant input from either the social partners or political opposition. To be sure, German authorities have been in a somewhat weaker position than their Dutch counterparts, due to the federal structure of the German political system and the frequent existence of blocking majorities in the *Bundesrat*. The unavailability of a Dutch-style “grand coalition” over social policy, however, has not precluded significant social-policy reform, as the case of the 2000 pension reform amply demonstrates. Instead, German governments have had to seek other ways to secure the passage of reforms, such as making side-payments to certain *Länder* represented in the upper house of Parliament and accepting some limited compromises over policy content. Although the existence of institutional constraints has resulted in more modest social-policy reforms in Germany than in the Netherlands, they have thus not prevented authorities from securing major changes in the German social-protection system. Although the political dynamics of the reform process have differed significantly by policy area, in labor-market and social policy the German state has played a critical role in shaping both the character of political discourse and the policy outcomes that this discourse has engendered.

While nationally distinct institutional and political contexts have shaped Dutch and German policy trajectories, so, too, has a challenging economic context that makes future prospects for reform far from certain. In both countries, unemployment is on the rise, pension systems are under growing financial and demographic pressures, economic growth is sluggish or stagnant (in 2003 it was actually negative in both countries), and policy-makers are experiencing considerable difficulties in meeting EMU limits on deficits and public spending. In the face of these increasingly severe challenges, it is

unclear whether Germany and the Netherlands will be able to continue to devise successful strategies for adjustment. That being said, the German and Dutch experiences offer several important lessons about the role of the state in corporatist political economies. First, conventional notions of “state strength” have little to offer analytically in terms of capturing states’ ability to secure reforms, which are defined instead by the state’s capacity to negotiate varying policy contexts and devise flexible responses to changing political-economic circumstances. Second, to the extent that they are able to do so, the successful adjustment of corporatist systems invariably requires the state to play a central role. Finally, the procedures and outcomes of corporatist decision-making are not beyond criticism, but rather require a certain degree of societal and political consensus. In all democratic polities, corporatist and non-corporatist alike, governments must ultimately answer to parliaments and voters. If it is to be successful, therefore, corporatist adjustment thus requires the support of a strong and vibrant democratic politics.

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