

DIW Roundup
Politik im Fokus

Early Retirement at 63: Compensation or Pension Giveaway?

Early Retirement at 63: Fair Compensation or Pension Giveaway?

Anika Rasner | arasner@diw.de | Socio-Economic Panel at DIW Berlin

After Easter, Germany's new labor and social affairs minister Andrea Nahles will be presenting the grand coalition's first major reform proposal for parliamentary debate: a bill to improve the benefits provided under the statutory pension system. A centerpiece of the reform package is early retirement on a full pension at 63 for those who have been paying into the state pension system for a long period of time. In defense of the proposal, Nahles has launched an information campaign emphasizing that "It's not a giveaway; it's earned." Critics, however, call early retirement at 63 a costly political gift to favored groups of voters with dubious social policy value, and warn that it could unleash a new wave of early retirement. In their view, the reform could undermine recent successes in securing the long-term financial sustainability of the pension system and in gradually extending working life.

Background

After four years of legislative inertia on the issue of pension reform, labor minister Andrea Nahles has set the tone for action with a draft bill to improve benefits provided under the statutory pension system (*Gesetz über Leistungsverbesserungen in der gesetzlichen Rentenversicherung*). Alongside a new "mother pension" that would let women with children born before 1992 count more of the years they spent at home caring for children as if they had worked and paid full pension contributions, the bill also improves pension benefits for the disabled and older employees who are no longer able to work full-time ([Kemptner, 2014](#)) and introduces early retirement on a full pension at 63 for those who have contributed to the pension system for at least 45 years.

According to current plans, as of July 1 of this year, when the reform is set to take effect, it will allow people who have contributed to the system for at least 45 years, whether through work, care for children or other family members, or even short-term unemployment (receipt of unemployment benefits) to retire early and receive a full pension without any reductions to their pension payments ([Bundesregierung, 2014](#)). The regulation will only benefit the baby boomer generation: those born between 1953 and 1963 ([Sellin, 2013](#)).

Retirement on a full pension at 63 is a clear break with the pension policies of past decades. All of the previous reforms passed since 1989 have been aimed at extending working life without significantly reducing pensions or significantly increasing pension contributions ([Bundesministerium für Gesundheit und Soziale Sicherung, 2003; Rürup, 2005](#)). These past reforms were designed to distribute the financial burdens fairly between those actively contributing to the pension system and those already receiving pensions. Policy makers have repeatedly questioned whether an acceptable level of fairness in the system has been achieved ([Bäcker & Koch, 2003](#)). Enduring

controversy surrounds the issues of benefit reductions for early retirement, the increased retirement age, and the elimination of special pensions that allow for early retirement if employees meet certain eligibility criteria.

Public discourse on the proposed full pension at 63 revolves around three main questions: First, who will profit from the rule, and is that fair? Second, will the possibility to retire on a full pension at 63 unleash a new wave of early retirement? And third, who will pay for it?

Is retiring on a full pension at 63 fair?

In the labor minister's view, a full pension at age 63 is "not a giveaway; it's earned" ([Bundesministerium für Arbeit und Soziales, 2014a](#)). To support this view, she argues that those who have paid into the pension insurance system for many years have been supporting it with their contributions, and that their lifetime contribution to the system should not be whittled away by lifelong pension reductions. For pensions expert Bert Rürup, the proposal of retirement on a full pension at 63 looks more like "an attempt to reconcile labor unions somewhat with the idea of retirement at 67" ([Rürup, 2014](#)).

From an individual point of view, retirement on a full pension at 63 may appear to be a justified social policy. Opponents of the planned reform, however, point out its financial implications and undesirable redistribution effects, arguing that it shifts the costs to future generations while failing to consider what would be fair to them ([Stiftung für die Rechte zukünftiger Generationen, 2013](#)).

The Confederation of German Employers' Associations claims that the proposal violates the principle of fairness in the system of pension contributions ([Bundesvereinigung der Deutschen Arbeitgeberverbände, 2014](#)). They point out that those with 45 years or more of contributions to the pension system would receive preferential treatment over their colleagues who are the same age, even if the actual amount they had contributed over the course of their working lives were the same. Similarly, those born before 1951, who are subject to pension reductions for early retirement under the present legislation, have no hope of having their pensions recalculated under the new legislation even if they otherwise qualify for a full pension at 63 by having contributed for at least 45 years (Boehringer, 2014).

Of those eligible for benefits under the proposed legislation, the majority are men. In order to receive the full pension amount, insured people must have contributed to the pension system for at least 45 years, whether through employment, through credits earned by caring for children or other family members, or through short-term unemployment. According to the federal government's 2012 pensions report, this applies to 43.5 percent of men but only 18.3 percent of women who retired in 2011 ([Bundesregierung, 2012](#)). Although the reform takes periods spent on childcare into account, a large majority of women do not qualify because, in many cases, the female life course still deviates significantly from the ideal of the "benchmark pensioner" ([Simonson et al., 2012](#)).

Critics also note that those who qualify for a full pension at 63 have no gaps in their employment histories and have faced very few labor market risks over the course of their working lives ([Bundesvereinigung der Deutschen Arbeitgeberverbände, 2014](#)). If one compares the long-term insured (who have contributed to the system for 45+ years) with all other pensioners, it becomes apparent that the former have significantly higher pensions, a longer period of pension receipt, and higher average income than the latter ([Krickl & Hoffmann, 2013](#)). The long-term insured could therefore represent a positive selection of people in their age cohort, characterized

by above-average life expectancy and therefore a longer period of time in which they benefit from full pensions.

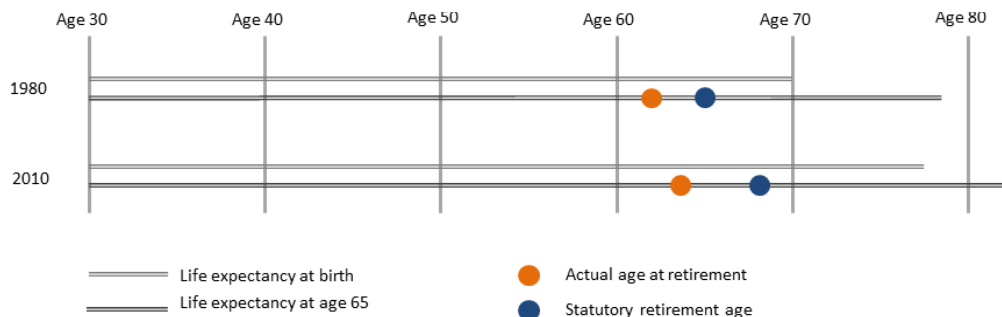
	Pensioners with 45+ years contributions		Total pensioners	
	Men	Women	Men	Women
Average pension (in €)	1.411	1.085	899	532
Years of pension contributions	49.2	46.6	39.8	30.4
Average pension entitlement points	1.18	0.91	1.06	0.74
Age at payment of first pension contribution	14.8	15.3	16.6	18.2

Comparison of the group of “long-term insured” with “total pensioners”
Source: [Krickl & Hoffmann \(2013\)](#)

An early start of working life could be an indicator of low education in the group of long-term insured. Although there have been no studies on the longevity of this group, a DIW study reports that individuals with low education show a significantly higher mortality risk starting at the age of 65 ([Kroh, Neiss, Kroll, & Lampert, 2012](#)). In general, however, the effect of education on mortality patterns in old age remains unclear.

Will the possibility to retire on a full pension at 63 unleash a new wave of early retirement?

While average life expectancy has increased constantly over the last few decades, the statutory retirement age has remained largely unchanged (Bloom, Canning, & Fink, 2010). Longer periods of pension receipt and the accompanying financial burdens on pension funds motivated the reform initiatives of recent decades. Figure 2 depicts the rationale underlying these reforms. Between 1980 and 2010, the average life expectancy at birth for West German men increased from 70 to 78 years, and the residual life expectancy at age 65 went from 78 to 82.6 years. During the same period, the legal retirement age was raised from 65 to 67 years ([Statistisches Bundesamt, 2012](#)). The increase in the actual age of entry into retirement from 62.2 to 64.1 years ([Deutsche Rentenversicherung, 2013](#)) shows that the reforms have produced the desired effect.



Evolution of the retirement age, statutory retirement age, and life expectancy
Source: Pension insurance in time series and mortality tables of the Federal Statistical Office 1980/1982 and 2009/2011, diagram by the author.

Retiring on a full pension at 63 thus represents a retreat from efforts to extend working life. This turnaround has aroused fears of an impending wave of early retirement (Schnabel, 2014). Employers argue that if periods of short-term unemployment counted toward retirement on a full pension, people could register as unemployed and thereby “bridge” the period up to retirement without working while sustaining no losses in pensions (Bundesvereinigung der Deutschen Arbeitgeberverbände, 2014). It should be noted, of course, that this possibility also exists today, but is not being measured systematically.

If possibilities exist for early retirement, both employers and employees use them. In the 1980s and 1990s, labor market policy measures, early retirement laws, tax exemptions for redundancy payments, and flexible age limits were all coordinated to enable older employees to retire as early as possible (Gatter & Hartmann, 1995). In some cases, people stopped working at 55 and “bridged” the period up to full retirement with wage compensation payments (Rosenow & Naschold, 1994) without having to look for work or take jobs offered to them by the employment agency (Mümken & Brussig, 2013). It is planned that legislators will develop regulations to prevent the misuse of early retirement in the future (Bundesministerium für Arbeit und Soziales, 2014b).

When evaluating the proposed full pension at 63 for the long-term insured, it should be kept in mind that voters overwhelmingly support the planned reduction of the retirement age. When asked for their views on the coalition agreement between CDU and SPD, the majority of the population answers that they consider retirement on a full pension at 63 after 45 years of contributions the grand coalition’s most important project to date (Infratest Dimap, 2013). Furthermore, over half of Germans surveyed report that they intend to retire at 63, even if they have to accept pension reductions due to early retirement. This means that if the opportunity exists to retire early—whether or not this comes at a cost in terms of pension reductions—people use it (von Borstel, 2014). A survey conducted by Allensbach last year (Institut für Demoskopie Allensbach, 2013) shows that more than half of the population considers a fair distribution of burdens between generations an important policy objective, although it remains unclear what this implies specifically for policy implementation.

Who is paying for the new pensions?

Projections on the financial implications of the pension package are still subject to rather wide margins of error since it is unknown whether all those eligible will want to make use of the new regulation. In an article in the newspaper *Wirtschaftswoche*, Axel Börsch-Supan points out that the reform offers numerous incentives to retire early but no financial incentives to retire later (Wirtschaftswoche, 2013). As a result, he argues that, first, the pension insurance system loses payments from jobs that are subject to social insurance contributions, and second, the duration of pension receipt is extended by two years but without any reductions in the total amount of the pension. The costs are estimated at up to 30 billion euros (Schnabel, 2014).

Those who profit most from retirement on a full pension at 63 are members of the baby boomer generation. When these cohorts retire, it will create a massive demographic shift. And if they retire early, this will accelerate the reduction in labor force potential and will lead in turn to a reduction in wages (Schnabel, 2014).

The bulk of the financial burden of such a shift will fall on future contributors to the pension system (Bach et al., 2013). This will bring about a major redistribution of wealth from young to old (Fratzscher, 2014). Since the expansion of benefits will be paid for mainly through pension contributions, the scheduled reduction in the pension contributions from 18.9 percent to 18.3 percent will be postponed. It would have taken place automatically because of the record pension insurance revenues,

with a sustainability reserve of 1.8 monthly payments ([Bundesversicherungsamt, 2014](#)). The German Council of Economic Experts has warned sharply against postponing the reduction in the contribution rate ([Sachverständigenrat zur Begutachtung der gesamtwirtschaftlichen Entwicklung, 2013](#)).

Rough estimates suggest that the costs of the new pension will amount to around 2.5 percent of total pension expenditures ([Börsch-Supan, 2014](#)). Pensioners will also incur some of the costs of the reform since the increased expenditures and changed relationship between contributors and recipients will lead to lower pension adjustments in the long term ([Schnabel, 2014](#)). The net pension level will thus, *ceteris paribus*, sink faster.

Sources

- Bach, S., Buslei, H., van Deuverden, K., Duso, T., Fichtner, F., Fratzscher, M., Geyer, J., Gornig, M., Haan, P., Kemfert, C., Lüthen, H., Michelsen, C., Müller, K.-U., Neuhoff, K., Schulz, E., Schupp, J., Spieß, C. K., & Wagner, G. G. (2013). Der Koalitionsvertrag nimmt die Gesellschaft in die Pflicht. DIW Wochenbericht(50), 13.
- Bäcker, G., & Koch, A. (2003). Die Jungen als Verlierer? Alterssicherung und Generationengerechtigkeit. WSI Mitteilungen(2), 111-117.
- Bloom, D. E., Canning, D., & Fink, G. (2010). Implications of population ageing for economic growth. *Oxford Review of Economic Policy*, 26(4), 583-612. doi: 10.1093/oxrep/grq038
- Boehringer, S. (2014). Hoffen auf den Ausstieg, *Süddeutsche Zeitung* vom 15./16. Februar 2014.
- Börsch-Supan, A. (1992). Population Aging, Social Security Design, and Early Retirement. *Journal of Institutional and Theoretical Economics (JITE) / Zeitschrift für die gesamte Staatswissenschaft*, 148(4), 533-557. doi: 10.2307/40751550
- Börsch-Supan, A. (2014, 28. Januar 2014). Rente: Rolle Rückwärts? Paper presented at the INSM Frühstücksdialog, Berlin.
- Börsch-Supan, A., & Schnabel, R. (1998). Social Security and Declining Labor-Force Participation in Germany. *The American Economic Review*, 88(2), 173-178. doi: 10.2307/116914
- Bundesministerium für Arbeit und Soziales. (2014a). Das Rentenpaket. Retrieved 10. Februar, 2014, from <http://www.rentenpaket.de/rp/DE/Startseite/start.html>
- Bundesministerium für Arbeit und Soziales (Producer). (2014b). Nicht geschenkt. Sondern verdient. Bundespressekonferenz am 29. Januar 2014.
- Bundesministerium für Gesundheit und Soziale Sicherung (Ed.). (2003). Nachhaltigkeit in der Finanzierung der Sozialen Sicherungssysteme: Bericht der Kommission. Berlin.
- Bundesregierung. (2012). Rentenversicherungsbericht (pp. 101). Berlin: Bundesministerium für Arbeit und Soziales.
- Bundesregierung. (2014). Entwurf eines Gesetzes über Leistungsverbesserungen in der gesetzlichen Rentenversicherung (pp. 23). Berlin: Bundesregierung.
- Bundesvereinigung der Deutschen Arbeitgeberverbände. (2014). Abschlagsfreie Rente mit 63 wäre ein kapitaler Fehler. Berlin: Bundesvereinigung der Deutschen Arbeitgeberverbände.
- Bundesversicherungsamt. (2014). Liquiditätsentwicklung 2013. Retrieved 11. Februar, 2014, from <http://www.bundesversicherungsamt.de/aufsicht/rentenversicherung/liquiditaet.html>
- Deutsche Rentenversicherung. (2013). Rentenversicherung in Zeitreihen (Vol. Band 22). Berlin.
- Fratzscher, M. (2014, 11. Februar 2014). Vorsicht, Rentenreform, *Handelsblatt*.
- Gatter, J., & Hartmann, B. K. (1995). Betriebliche Verrentungspraktiken zwischen arbeitsmarkt- und rentenpolitischen Interessen. *Mitteilungen aus der Arbeitsmarkt- und Berufsforschung*, 28(3), 412-425.
- Infratest Dimap. (2013). ARD Deutschland-Trend - Dezember 2013. Berlin: Infratest Dimap.
- Institut für Demoskopie Allensbach. (2013). Was ist gerecht? Gerechtigkeitsbegriff und -wahrnehmung der Bürger. Allensbach: Institut für Demoskopie Allensbach.
- Kemptner, D. (2014). Erwerbsminderung als Armutsrisiko DIW Roundup No. 8. Berlin: Deutsches Institut für Wirtschaftsforschung.

- Krickl, T., & Hoffmann, J. (2013). Rentenzugang 2012: Die Anhebung der Altersgrenzen hat begonnen. *RVaktuell*, 9, 222-230.
- Kroh, M., Neiss, H., Kroll, L., & Lampert, T. (2012). Menschen mit hohen Einkommen leben länger. *DIW Wochenbericht*(38), 3-15.
- Mümken, S., & Brussig, M. (2013). Sichtbare Arbeitslosigkeit: Unter den 60- bis 64-Jährigen deutlich gestiegen. In I. A. u. Q. (IAQ) (Ed.), *Altersübergangsreport* (pp. 14). Duisburg: Institut Arbeit und Qualifikation.
- Oeppen, J., & Vaupel, J. W. (2002). Broken Limits to Life Expectancy. *Science*, 296(5570), 1029-1031. doi: 10.1126/science.1069675
- Rosenow, J., & Naschold, F. (1994). *Die Regulierung von Altersgrenzen*. Berlin: Sigma.
- Rürup, B. (2005, 1. Dezember 2005). Soziale Sicherheit: Solidarität versus Markt. Paper presented at the FNA Jahrestagung "Das Soziale in der Alterssicherung", Erkner bei Berlin.
- Rürup, B. (2014, 1. Februar 2014). Alte Fehler in der Rente, *Frankfurter Allgemeine Zeitung*.
- Sachverständigenrat zur Begutachtung der gesamtwirtschaftlichen Entwicklung. (2013). *Gegen eine rückwärtsgewandte Wirtschaftspolitik - Jahresgutachten 2013/2014*. Wiesbaden: Sachverständigenrat zur Begutachtung der gesamtwirtschaftlichen Entwicklung.
- Schnabel, R. (2014). *Rentenpolitik: Wiedereinstieg in die Frühverrentung* (pp. 5). Duisburg Essen: Universität Duisburg Essen.
- Sellin, P. (2013). *Rentenpaket der Großen Koalition: Mütter und Babyboomer gewinnen - Altersarmut wird zunehmen*. Berlin: Heinrich Böll Stiftung.
- Simonson, J., Kelle, N., Romeu Gordo, L., Grabka, M. M., Rasner, A., & Westermeier, C. (2012). Babyboomer: Mehr Brüche im Erwerbsleben, weniger Rente. *DIW Wochenbericht*, 23/2012, 3-14.
- Statistisches Bundesamt. (2012). *Periodensterbetafeln für Deutschland* Wiesbaden: Statistisches Bundesamt,.
- Stiftung für die Rechte zukünftiger Generationen. (2013). *Der Koalitionsvertrag CDU/CSU/SPD 2014: Kurzanalyse aus Sicht der Generationengerechtigkeit*.
- von Borstel, S. (2014, 1.2.2014). Mehrheit der Deutschen will mit 63 Jahren in Rente, *Die Welt*.
- Wirtschaftswoche. (2013). *Das raten Top-Ökonomen der Großen Koalition*. Retrieved 16.12.2013, from <http://www.wiwo.de/politik/deutschland/regierung-das-raten-top-oekonomen-der-grossen-koalition-seite-all/9212582-all.html>

Translation: Deborah Anne Bowen, Dipl. Trans. IoL

Imprint

DIW Berlin – Deutsches Institut
für Wirtschaftsforschung
Mohrenstraße 58, 10117 Berlin

Tel. +49 (30) 897 89-0
Fax +49 (30) 897 89-200
<http://www.diw.de>

ISSN 2198-3925

Technical Editing

Alfred Gutzler
Brigitta Jähnig
Lana Stille

All rights reserved.
© 2014 DIW Berlin

Reprint and further distribution
–including extracts–
with complete reference and
consignment of a specimen
copy to DIW Berlin's
Communications Department
(kundenservice@diw.berlin) only.