Germany

Statutory Social Security

Introduction

The statutory pension system is one of the five pillars of Germany's social security system and represents the area to which most of the public and private financial resources are committed. In spite of dramatic demographic changes (one of the lowest birthrates and highest life expectancies in Europe), the German government's aim is to keep the contribution rates to the state pension system stable under 20% p.a. This will strain state pension payments even more in the long run. The normal retirement age at which full (unreduced) old age annuities can be drawn, will increase on a tiered basis from age 65 to age 67 from 2012 until 2029. Approximately 90% of the population in Germany benefits from the mandatory social security system. In addition to the five types of social insurances financed by both, employees and employers, the social network also comprises services financed through taxes, such as family benefits and social assistance.

Contributions 2018 (% of salary, max. ceiling)	**Employee**	**Employer**	**Social Security Contribution Ceiling (SSLC)**	
	Tax deductible within certain limits	Tax deductible	West Germany	Former East Germany
State Pension System (retirement, survivors', LTD)	9.3%	9.3%	78,000 €	69,600 €
Unemployment	1.5%	1.5%	78,000 €	69,600 €
Health insurance	approx. 8.3%	7.3%	53,100 €	53,100 €
Long-term nursing care	1.275% (1.525%*)	1.275%	53,100 €	53,100 €
Industrial Injury / Workers' Comp.	0%	0.6% - 2%		
	20.325% - 20.575%	**20.025% - 21.425%**		

*= Childless employees have to pay a surcharge of 0.25% as of their completion of age 23, no surcharge for the employer

State Pension System

Pensions are not accumulated into a cash-backed fund on behalf of the particular employee, but are paid from current income from pension insurance by means of an allocation process (pay-as-you-go system). The statutory pension scheme is complemented by state grants for voluntary, private pension plans (the so-called "Riester-Rente"). Their aim is to compensate for the reduction of pension levels projected for the long term. The state pension covers retirement pensions as well as death and long-term disability benefits. The monthly pension is a product of the pension factor, the pension points, the pension value and the access factor. The pension factor takes into account the type of benefits to be paid. Pension points represent the ratio between the individual's covered earnings and the National Average Earnings. The pension value states the monthly amount of pension payable for each pension point and is fixed by the government. Finally, the access factor is the actuarial factor for early or late retirement. The monthly gross normal retirement pension amounts currently to approx. €1,266 based on 45 yrs. of contribution and an average income over the years. Early retirement is possible from age 62, albeit with reductions of 0.3% per month. Due to changes in the pension law, pensions are now subject to tax, however, said tax is applied on a gradual basis for pensions already in payment in order to avoid undue hardship for the pensioners.

Unemployment insurance

Every person in gainful employment working at least 18 hours a week is insured against unemployment. Benefits are payable from the first day of unemployment due to involuntary termination (dismissal) and after 12 weeks for voluntary termination (resignation), provided the unemployed person has been employed gainfully for at least 12 months during the previous 2 years. The amount and duration of the benefit depends on the income and duration of the previous employment. In general, one receives 60% of their net earnings in the last 12 months if they do not have children and 67% if they have children. The duration for which it is paid also depends on the length of the period during which contributions have been paid and on the claimant's age. It is generally paid for a minimum of 6 months and up to a maximum of 18 months. After this period the benefit continues at a reduced rate of about €374 per month with an additional child allowance which varies depending on the child's age. The benefits are tax-free.

Health Care System

All employees with income up to the salary limit for mandatory health care (€59,400) are obliged to join one of the state sickness funds. Persons earning the above mentioned salary limit for more than 1 year are free to opt out for private health insurance. In the case of sickness, employees continue to receive their salary from their employer for up to six weeks (short term disability benefit). After this, the state sickness fund or private insurer provides sickness benefits for up to 78 weeks. All insured persons may choose any doctor or hospital under contract with their sickness fund. Patients are required to pay a portion of the costs for prescription medicines (drugs) and certain services. Exemptions are possible. Benefits are tax-free.

Long term/nursing care

Long term/nursing care is mandatory for all members of state sickness funds. Employees who are members of a private health insurance scheme are required to purchase coverage for long term care. Benefits include home and long-term inpatient care depending on the level of care required. Benefits are tax-free.

Industrial injury/Workers' Compensation (statutory employers' liability insurance)

Assistance after accidents at work is provided by the statutory workers compensation insurance. Tax-free benefits can be claimed in case of an accident at or on the way to work or an occupational disease, leading to injury, illness or death.

Useful link:

http://www.deutsche-sozialversicherung.de

Germany

Supplementary Benefit Plans

Introduction

Supplementary retirement and benefit plans are common among larger companies as well as in many of the medium and small-sized companies. Since the introduction of the employees' right to participate in a salary sacrifice scheme in 2002 (employee-funded company pension, similar to US 401k plans), the number of employees in the private industry with an entitlement to a company pension has risen significantly from 35% to 48%. In the long-term, the government estimates the share of employees with pension plan benefits to be $^{2}/_{3}$ to $^{3}/_{4}$ of all employees. On average, in 26% of the companies with pension plans in place, the funding is exclusively effected through salary sacrifice. The number of retirement plans exclusively funded by the employer decreased from 54% to 47%. Purely employer funded retirement plans can be found in industries, where the “war of talents” still exists (IT, internet, media, pharmaceutical, telecommunications, legal and business consultancy, technical engineering, etc.). One trend that is growing is that of matching contribution pension plans. Within the last couple of years, its share has risen from 27% to 39%.

Retirement Plans

The retirement plans currently implemented are based on defined contribution or so-called hybrid defined contribution approaches. The DC rates are in the range between 2% of pensionable pay up to 5% of pensionable pay, depending on industry, company size and the type of employees participating in the plan. Matching contribution plans are often designed as 1:1 or 1:½ matches with a maximum employer contribution according to the given employer contribution limit. The retirement benefits are designed in the form of an annuity or as retirement lump sums normally paid out at age 67. When they become due, retirement benefits are subject to income tax for the employee. Contributions to a pension plan are tax-deductible. From January 1, 2018, the legal vesting period reduces from 5 to 3 years; however, immediate or contractual vesting after 1 or 2 years of plan membership is quite common. For salary sacrifice arrangements, benefit entitlements are immediately vested. Normally, all employees of a company are eligible to join a pension plan, no matter whether they are full or part-time employees. A 6 month waiting period is sometimes a precondition for plan participation, however, only a very small minority of employers require employees to fulfill a waiting period prior to plan membership.

Life Insurance

Usually, 1 or 2-times pensionable pay, sometimes a fixed amount (e.g., €170,000) is paid as a lump sum to the employee's survivors. Life insurance benefits are subject to income tax for the beneficiaries on payment. Premiums paid to cover the life insurance benefits are however tax-deductible.

Long-term disability

In case of occupational or total disability, most occupational supplementary plans provide LTD or TPD benefits. The TPD benefit is defined as a lump sum (typically 2-times pensionable pay) and the LTD benefit as an annuity. The LTD annuity is payable until recovery or completion of the normal retirement age or death, whichever case occurs first. LTD/TPD benefits are subject to income tax for the employee when they become due. Premiums paid to cover LTD/TPD benefits are tax-deductible.

Funding

In Germany, employers may choose among as many as five different funding vehicles to finance occupational supplementary plans:

●Direct Pension Promise (book reserves) ●Direct Insurance ●Pensionskasse (traditional pension fund) ●Pensionsfonds (equity-oriented pension fund) ● Support Fund (≅ secured trust)

Although direct pension promises (book reserves) are still the most popular funding vehicle for occupational pension plans in Germany, a clear trend shows a move to external, asset-backed funding vehicles. This is due to accounting reasons, but it also improves the quality of the investment process and increases plan members’ security.

With regard to salary sacrifice schemes, the direct insurance is the most favored at this time. The direct insurance must be financed according to actuarial principles, ensuring that the necessary means to fulfill pension liabilities are available at any time. Detailed regulations about the requirements are laid down in the Insurance Supervisory Law. *The Law on Strengthening Occupational Pensions* came into effect on January 1, 2018. Among other things, this will increase the tax free limit for contributions to a direct insurance from 4% to 8% of SSCL (€6240 p.a. in 2018). Previously, employees with “old” grandfathered direct insurance could add €1,800 to their tax free contributions; this will no longer be possible following the aforementioned tax free limit increase. In addition, starting from January 1, 2018, employers are required to pay 15% of any social security contribution savings they make from an employee’s salary sacrifice by way of a direct insurance, a traditional or capital market oriented pension fund, to the employee. As the threshold for social security contributions remains 4% of the SSCL in 2018 (€3120 p.a.) an employer will pay a maximum of €468 p.a. per employee under the 15% rule. Although the law became effective on January 1, 2018, said rule will first apply in January 2019 to contracts concluded in 2018 and then from January 2022 to all other contracts, i.e., those concluded prior to and after 2018.

Most occupational supplementary plans are funded via a fully reinsured support fund (similar to a secured trust). This applies for pure employer funded plans as well as for employer matching contributions to a retirement plan. A support fund is a separate legal entity (independent from the sponsor company, e.g. the employer) and tax exempt social benefit institution, set up mostly as an association, which receives the plan contributions from the employer. This guarantees the external status of plan assets and thus prevents on-balance sheet effects for the employer. The full contribution amount transferred to the fully reinsured support fund is tax-deductible. According to the law, each fully reinsured support fund must invest the plan contributions from a sponsor company with an investment fund of a mutual life insurance company, providing a guaranteed return on investment of 0.9% p.a. Therefore, the conservative investment fund strategy is fixed so employees do not have access to a range of funds.

Accidental Death & Dismemberment

In addition to the above mentioned employee benefits, AD&D programs are quite common in Germany. These cover death or occupational disability risks only if the incident is caused by an accident (sudden, involuntary, and external incident). Typical AD&D programs offer worldwide 24-hour coverage. The benefit level is often equal to the life insurance or long-term disability benefit amounts. Accidental death and dismemberment benefits are normally funded via local AD&D insurance and the premiums are fully tax-deductible.