The Investment Climate in Germany

Openness to Foreign Investment

The German government and industry actively encourage foreign investment in Germany, and German law provides foreign investors national treatment. Under German law, foreign-owned companies registered in the Federal Republic of Germany as a GmbH (limited liability company) or an AG (joint stock company) are treated no differently from German-owned companies. Germany also treats foreigners equally in privatizations. There are no special nationality requirements on directors or shareholders, nor do investors need to register investment intent with any government entity except in the case of acquiring a significant stake in a firm in the defense or encryption industries. The investment-related problems foreign companies do face are generally the same as for domestic firms, for example high marginal income tax rates and labor laws that impede hiring and dismissals. The German government has begun to address many of these problem areas through its reform programs. German courts have a good record in upholding the sanctity of contracts.

The 1956 U.S.-FRG Treaty of Friendship, Commerce and Navigation affords U.S. investors national treatment and provides for the free movement of capital between the U.S. and Germany. Germany subscribes to the OECD Committee on Investment and Multinational Enterprises' (CIME) National Treatment Instrument and the OECD Code on Capital Movements and Invisible Transactions (CMIT). While Germany's foreign economic law contains a provision permitting restrictions on private direct investment flows in either direction for reasons of foreign policy, foreign exchange, or national security, no such restrictions have been imposed in practice. In such general cases, the federal government would first consult with the Bundesbank and the governments of the federal states. Specific legislation requiring government screening of foreign equity acquisitions of 25% or more of German armaments companies took effect in July 2004.

Under the 2004 law, foreign entities that wish to purchase more than 25% equity in German manufacturers of armaments or cryptographic equipment are required to notify the Federal Economics and Technology Ministry, which then has one month in which to veto the sale. The transaction is regarded as approved if the Economics and Technology Ministry does not react in that time. A new law passed by Parliament in March 2009 broadened these rules and established a procedure similar to the U.S. CFIUS. Industrial policy considerations and lobbying by business interests have occasionally delayed decision-making on investment.
Germany ranks 14th in the Transparency International Corruption Perception Index (CPI) that compares 180 countries worldwide (rank 1 being the country with least corruption).

Conversion and Transfer Policies

As a result of European Economic and Monetary Union (EMU), the Deutsche Mark (DM) was phased out on January 1, 2002, and replaced by the euro, which is a freely traded currency with no restrictions on transfer or conversion and which is the unit of currency in Germany and 20 other European countries. There is no difficulty in obtaining foreign exchange. There are also no restrictions on inflows and outflows of funds for remittances of profits or other purposes.

Expropriation and Compensation

German law provides that private property can be expropriated for public purposes only in a non-discriminatory manner and in accordance with established principles of constitutional and international law. There is due process and transparency of purpose, and investors and lenders to expropriated entities receive prompt, adequate and effective compensation.

Dispute Settlement

Investment disputes concerning U.S. or other foreign investors and Germany are rare. Germany is a member of the International Center for the Settlement of Investment Disputes (ICSID), as well as a member of the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards. German courts are fully available for foreign investors in the event of investment disputes. The government does not interfere in the court system and accepts binding arbitration.

Performance Requirements and Incentives

European Union, federal and state authorities offer a broad range of incentive programs for investors in Germany. Cash Grants under the Joint Agreement for the Improvement of Regional Economic Structures is one available instrument for improving the infrastructure of regional economies and the economy as a whole – a primary objective of the German federal and state governments.

A comprehensive package of federal and state investment incentives, including cash, labor-related, and R&D incentives, interest-reduced loans, and public guarantees is available to domestic and foreign investors. In some cases, there may be performance requirements tied to the incentive, such as employment creation and maintaining a certain level of employment for a prescribed length of time. There are no requirements for local sourcing, export percentage, or local national ownership.
Offsets have been a part of procurements by some state and local governments and by the federal government for some defense procurement, but they are infrequently used at present. Germany is in compliance with its WTO TRIMS notification.

The government has emphasized investment promotion in the states of the former East Germany and offers several programs only in these regions. The major program is the Investment Allowance Act, which provides tax incentives for investments in the eastern states in the form of tax-free cash payments or tax credits. With the beginning of the new budgetary period of the EU, which starts in January 2007 (and runs through 2013), Germany is going to receive a total of EUR 26.3 billion. The accession of new EU member countries in 2004 reduced subsidy levels for Germany beginning in 2007. The German states located in former East Germany receive the majority of the EU subsidies allocated to Germany, EUR 15.1 billion, for the budget period of 2007-2013.

Foreign investors are generally subject to the same eligibility conditions as German investors for incentive programs.

**Programs in Germany:**

**Investment grants:** Cash incentives in the form of non-repayable grants usually based on investment costs or assumed wage costs. Incentives vary according to the economic development level of the region and the overall investment costs, with up to 30 percent of eligible expenditures channeled to large enterprises, 40 percent to medium-sized enterprises and 50 percent to small enterprises.

**Credit programs:** Loans at below-market interest rates from the Bank for Reconstruction, the European Recovery Program, and other programs for small technology firms and environmental demonstration projects.

**Public guarantees:** Public guarantees for companies which do not have the securities private banks ordinarily require.

**Labor incentives:** Recruitment support from 800 local job centers, including of free services, training support, wage subsidies, and on-the-job training.
Firms from the United States and other countries may also participate in government and/or subsidized research and development programs, provided that:

- The company is legally established in Germany
- The activity is a long-term operation with significant R&D capacities
- The firm can exploit intellectual property rights independent from a parent company
- Preference is given to locating manufacturing facilities in Germany for any production resulting from the research
- The project engages in sponsored research entirely performed in Germany.

American business representatives generally report that these formal requirements and the administration of the programs by German authorities do not constitute barriers for access to R&D funding.

**Right to Private Ownership and Establishment**

Foreign and domestic entities have the right to establish and own business enterprises, engage in all forms of remunerative activity, and acquire and dispose of interests in business enterprises.

**Protection of Property Rights**

The German Government adheres to a policy of national treatment, which considers property owned by foreigners as fully protected under German law. There is almost no discrimination against foreign investment and foreign acquisition, ownership, control or disposal of property or equity interests, with airline ownership being an exception based on EU regulations, which require an EU majority ownership of shares to obtain an operating permit as an EU airline. In Germany, the concept of mortgages is subject to a recognized and reliable security. Secured interests in property, both chattel and real, are recognized and enforced.

Intellectual property is well protected by German laws. Germany is a member of the World Intellectual Property Organization (WIPO). Germany is also a party to the major international intellectual property protection agreements: the Bern Convention for the Protection of Literary and
Artistic Works, the Paris Convention for the Protection of Industrial Property, the Universal Copyright Convention, the Geneva Phonograms Convention, the Patent Cooperation Treaty, the Brussels Satellite Convention, and the Treaty of Rome on Neighboring Rights.

National treatment is also granted foreign copyright holders, including remuneration for private recordings. Under the TRIPS agreement, the federal government also grants legal protection for practicing U.S. artists against the commercial distribution of unauthorized live recordings in Germany. Germany has signed the WIPO Internet treaties and ratified them in 2003. Foreign and German rights holders, however, remain critical of provisions in the German Copyright Act that allow exceptions for private copies of copyrighted works. Most rights holder organizations regard German authorities' enforcement of intellectual property protections as sufficient, although problems persist due to lenient court rulings in some cases and the difficulty of combating piracy of copyrighted works on the Internet.

In 2008, Germany implemented the EU enforcement directive with a national bill, thereby strengthening the privileges of rights holders and allowing for improved enforcement action.

**Transparency of the Regulatory System**

Germany has transparent and effective laws and policies to promote competition, including anti-trust laws. German authorities recently lifted many restrictions on store business hours, which had formerly restrained competition and business opportunities. There are concerns in Germany and abroad about the level of regulation prevailing with regulatory authority dispersed over the federal, state, and local levels. Many investors consider Germany's bureaucracy excessive, which has prompted most state governments to establish investment promotion offices and investment banks to expedite the process. The Merkel government has talked about the need to cut red tape in Germany and in the EU as a whole. New rules have simplified bureaucratic requirements, but industry must sometimes contend with officials' relative inexperience with deregulation and lingering pro-regulation attitudes.

In response to the problem, the federal government continues to reduce bureaucracy. In 2006, the National Regulatory Control Council was established, tasked with evaluating policy and assessing the impact of lawmaking. Based on its findings, the council reports annually and recommends further measures. The federal government also set the target of reducing the costs of law-induced bureaucracy by 25 percent by 2011. The new Economics Minister Rainer Brüderle (pro-market FDP) seems to be very interested in reducing the bureaucratic burden and has moved the section within the Economics Ministry dealing with bureaucracy reform closer to his own office. Germany now uses the Standard Cost Model to quantify and identify bureaucratic costs in every new legislative proposal. This provides increased transparency about the amount of time and cost that companies and citizens have to spend because of bureaucratic requirements. The German National Regulatory Control Council estimates that applying the Standard Cost Model has reduced
bureaucratic costs by 3 billion euros in the past two-and-a-half years, measured against the 
bureaucratic burden that was in effect before new, improved legislation.

Laws and regulations in Germany are routinely published in draft and public comments are 
solicited. The legal, regulatory and accounting systems can be complex but are transparent and 
consistent with international norms.

**Efficient Capital Markets and Portfolio Investment**

Germany has a modern financial market sector but is often considered "over-banked," as evidenced 
by on-going consolidation and low profit margins. The country’s so-called “three-pillar” banking 
system, made up of private commercial banks, state-owned and cooperative banks, and savings 
banks, survived the global financial crisis, but pressures to consolidate are increasing. To improve 
their international competitiveness, the large privately-owned banks in particular have launched 
massive cost-cutting programs. Regional state-owned banks ("Landesbanken") were among the 
hardest hit by the crisis. Their future seems unclear, as the EU Competition Commissioner has 
attached tough downsizing conditions in return for approving federal and state government bailout 
packages. The financial crisis also triggered the take-over of Dresdner Bank by Commerzbank and 
that of Post Bank by Deutsche Bank. This has effectively reduced the number of top German banks 
to just two.

In the midst of the financial crisis, the German government passed a bank rescue plan ("SOFFIN") 
worth 480 billion euros. The two most prominent recipients of rescue funds were Commerzbank 
(its take-over of Dresdner Bank brought it to the brink of bankruptcy) and Hypo Real Estate 
(HRE). In the case of HRE, the government even departed from its long-standing tradition and 
nationalized the bank in order to prevent a breakdown of the German (and European) covered bond 
market – which is the backbone of German real estate financing. The law permitting the 
expropriation of HRE was designed for that institution only and expired in June 2009. There are 
currently several court cases pending in which the government action of “squeezing out” HRE’s 
old owners is being challenged. One such high-profile case is that of U.S. private equity firm, JC 
Flowers, which led a consortium of investors owning nearly 25 percent of the troubled bank prior 
to nationalization. The government argued that without its actions, HRE would have been 
insolvent, and owners would have lost their assets anyway. At 1.30 euros per share, the German 
Government paid an estimated 10 cents more than the actual market value of HRE stock.

Credit is available at market-determined rates to both domestic and foreign investors, and a variety 
of credit instruments are available. Legal, regulatory and accounting systems are generally 
transparent and consistent with international banking norms, but in light of the current global 
financial turmoil, Germany is pushing for even more transparency in international financial 
markets. Germany has a universal banking system that is effectively regulated by federal 
authorities. There is currently some concern that the economic crisis in connection with tougher
capital requirements for banks mandated in the G-20 may cause a shortage of credit in the German economy. The German government has taken action to ease the situation through the offer of additional state financing options through its state lender KfW.

Given the prevailing overall economic conditions, mergers and acquisitions (M&A) have decreased in recent years in line with global trends. Prior to the global financial crisis, Germany had seen an upswing in M&A transactions due to improved economic conditions, the increased financial assets of the top 30 companies listed in the German stock exchange (DAX), and the high value of the euro. "Cross shareholding" exists among some large German companies, in particular among banks that hold shares in large industrial customers. However, Germany's major banks have been reducing their cross-shareholdings in recent years.

In response to a 2004 EU directive, the government has implemented legislation that established new rules to ensure greater transparency for takeovers. The new law went into effect in 2006.

In recent years, Germany has implemented a series of laws to improve its securities trading system, including laws against insider-trading and the Fourth Financial Market Promotion Law in 2003. In 2002, a corporate governance code was adopted, which, while voluntary, requires listed companies to "comply or explain" why the code or parts thereof have not been followed. The code is intended to increase transparency and improve management response to shareholder concerns. The Finance and Justice Ministries drew up a ten-point plan in 2003 to improve investor protection. As a part of that plan, the government tabled a bill in November 2004 that would (a) increase the liability of boards of directors for false or misleading statements; and (b) improve oversight of auditing operations. The EU's Financial Services Action Plan – an effort intended to create a more integrated European financial market by 2005 – has helped stimulate changes in the German regulatory framework, including adoption of International Accounting Standards for listed firms and use of company investment prospects on an EU-wide basis. In 2008, Germany passed legislation that makes private equity firms subject to greater transparency rules, including the publication of a business plan for the acquired company.

**Competition from State Owned Enterprises**

State-owned or partially state-owned enterprises still exist in several sectors, most importantly in postal services, railroads, telecommunications and the banking sector.

Privatization of state-owned utilities has promoted competition and led to falling prices in some sectors. Following deregulation of the telecommunications sector in 1998, scores of foreign and domestic companies invested vast sums in that sector. Since then, former state monopolist Deutsche Telekom (DT) has lost more than 48% of the fixed-line market to competitors (while at
the same time profiting from them, as they must lease the last mile from DT), and it still controls 47% of DSL broadband connections. The 2003 introduction of call-by-call and pre-selection in the local loop allowed competitors to increase their share of the local call market to an estimated 49% by mid-2006. In June 2004, a new telecommunications law to implement EU directives entered into force. The law mandates less regulation in some areas while giving the regulator new powers to address abuse of market dominance and ensure competitors’ access to services. A second amendment to the telecommunications law became effective in early 2007. Aimed at strengthening consumer rights, it also includes a controversial component entitling the incumbent to a regulatory holiday in return for a sizeable investment in a VDSL network, providing the investment creates a "new market." The regulator determines the definition of "new markets" and can subsequently rule on the entitlement to a regulation-free timeframe. However, in 2009 the European Court of Justice ruled that the regulatory holiday granted to DT infringes on European law. The German government continues to hold a 32% share in DT, although it has expressed its desire to sell these shares eventually.

Competition has come to the electricity market since 1998, especially since the German Government began to take serious measures to open the market. The gas sector has proved particularly resistant to the EU Directive in 2000 to liberalize the market but is opening now. In July 2005, the Regulatory Authority for Telecommunications and Post (RegTP) became the Federal Network Agency (FNA) and took over responsibility for gas and electricity network prices and access. In summer 2006, it began issuing orders to incumbents in the electricity market to cut prices. Action against gas suppliers started a year later. The FNA is currently preparing new regulations to force pipelines to accept more gas from competitors and increase cross-border pipeline capacity. Rising energy prices and rising profits in the energy sector increased consumer and political pressure on the industry to contain prices. Legislation to force utilities to accept new competing power stations into their nets went into force in 2007 and to increase the authority of the Federal Cartel Office (Bundeskartellamt) in this sector in 2008. The Cartel Office has used this authority to force approximately 30 gas suppliers to lower their prices and in many cases to repay customers. However, the severe economic downturn has reduced the demand for energy and created upward pressure on electricity prices. Ironically, gas prices are tending down because of market saturation. The EU has withdrawn plans to bring charges of price fixing and territorial demarcation against leading German energy utilities after two utilities agreed to sell their long-distance power or gas transmission lines, thereby submitting to the EU’s unbundling demands. One has finalized the sale of its transmission lines, a second is finalizing the sale. Both buyers are foreign net operators. The sale of long-distance gas pipelines has not yet been realized. As consumers begin to change suppliers in the electricity market in particular, courts are also increasingly supporting consumers against energy suppliers, usually gas providers. After years of competitive stagnation, some new foreign competitors have entered the power market in recent years and are beginning to move into the gas market.

The government partially privatized Deutsche Post (DP) in November 2000 and is slowly divesting its remaining shares. It currently holds a 30.5% share in DP. After successive rounds of liberalization, DP's monopoly on letter delivery expired on December 31, 2007; full competition now exists in the German postal sector. A new minimum wage law in the postal sector was regarded by some competitors, however, as favoring Deutsche Post and as leading to the demise of several major competitors. DP to date still enjoys VAT exemption (of 19%) for offering universal
service. However, VAT exemption will likely be reduced to private individual’s letters and light parcels in July 2010, following a ruling by the European Court of Justice in late 2009. According to draft legislation, competitors will also be entitled to VAT exemption if they offer universal service. Germany’s Cartel Office, which enjoys an excellent international reputation, and Germany’s other regulatory agencies address problems and settle complaints brought forward by foreign market entrants and bidders. However, as noted above, German law and court decisions have limited these agencies' effectiveness in some areas.

The planned sale to private investors of just under 25% of the 100% government-owned railway Deutsche Bahn (DB) did not take place. The government scaled down the original privatization plan for just below 50% to just below 25%. The change was largely due to unresolved disputes within the CDU/SPD coalition government over the retention of ownership of both rolling stock and the rail network. The SPD supported the position of DB and the unions to retain DB control over both rolling stock and the rail network in the midst of increasing grass roots opposition to any privatization at all. The CDU was also divided but generally favored unbundling ownership of rolling stock and the rail network for competitive reasons. On January 1, 2006, the Federal Network Agency took over responsibility for access and prices issues regarding competitors’ access to the railroad network. A series of data privacy scandals forced the resignation of the DB CEO in 2009, when DB also started to have serious safety problems with high-speed, freight and Berlin light rail rolling stock, primarily due to lack of maintenance. Public and political outrage at the perceived attempt to cut costs to improve DB’s attractiveness for privatization, but at the expense of safety, has led to the new coalition government putting the privatization on ice, officially because of poor market conditions in the financial crisis.

Three different types of banks exist in Germany: privately-owned banks, state-owned banks (Landesbanken) and cooperative banks. The Landesbanken used to have advantages over privately-owned banks in obtaining credit. Under the pressure of Germany’s privately-owned banks, the EU forced an end to these advantages in 2005. This means that the Landesbanken can no longer raise money cheaply with a AAA rating because of state guarantee. At the moment, foreign banks do not have to fear any unfair competition from state-owned or cooperative banks.

**Corporate Social Responsibility**

The Federal Ministry of Labor and Social Affairs is the leading ministry for CSR within the German government, and it is currently developing a national CSR strategy. The Ministry of Labor has installed a CSR Forum in January 2009 as a platform for dialogue with relevant stakeholders. The CSR Forum consists of around 40 organizations from business, unions, civil society and politics. Its task is to develop recommendations for the Labor Ministry’s national CSR Strategy and to participate in its implementation once the strategy has been adopted. Because of the restructuring of the Labor Ministry after the elections, the work of the CSR forum is currently stalled.
On the business side, the American Chamber of Commerce in Germany (AmCham Germany) is active in upholding the standards of social responsibility within the realm of their members’ corporate business. AmCham Germany issues regular publications on companies’ CSR approaches and has established a committee on corporate social responsibility as a platform for the exchange of best practices, to identify trends and to discuss regulatory initiatives.

**Political Violence**

Political acts of violence against either foreign or domestic business enterprises are extremely rare. Isolated cases of violence directed at certain minorities and asylum seekers have not affected U.S. investments or investors.

**Corruption**

Among industrialized countries, Germany ranks in the middle, according to Transparency International's corruption indices. The construction sector and public contracting, in conjunction with undue political party influence, represent particular areas of continued concern. Nevertheless, U.S. firms have not identified corruption as an impediment to investment.

The German government has sought to reduce domestic and foreign corruption. Strict anti-corruption laws apply to domestic economic activity and the laws are enforced.

Germany ratified the 1998 OECD Anti-Bribery Convention in February 1999, thereby criminalizing bribery of foreign public officials by German citizens and firms abroad. The necessary tax reform legislation ending the tax write-off of bribes in Germany and abroad became law in March 1999. Germany has signed the UN Anti-Corruption Convention but has not yet ratified it. The country participates in the relevant EU anti-corruption measures. Germany has increased penalties for bribery of German officials, for corrupt practices between companies, and for price-fixing by companies competing for public contracts. It has also strengthened anti-corruption provisions applying to support extended by the official export credit agency and tightened the rules for public tenders. Most state governments and local authorities have contact points for whistle-blowing and provisions for rotating personnel in areas prone to corruption. Government officials are forbidden from accepting gifts linked to their jobs.

Opinions, however, differ on the effectiveness of these steps, particularly in the area of foreign corruption. German industry - while generally in favor of creating a central, national-level register of corrupt companies that would be barred from bidding for public contracts - refrained from openly calling for its creation out of fear of added regulatory burden. Draft legislation to create such a register passed the lower chamber of the German Parliament but was blocked by opposition...
parties in the upper chamber in 2002. The CDU-SPD Government, which took over in November 2005, did not include a similar initiative in its program. Nevertheless, some individual states maintain their own registers. Transparency Deutschland, the German Chapter of Transparency International, sees a national corruption register as one of its main goals in Germany and a speedy ratification of the UN Anti-Corruption Convention placing bribery of parliamentarians on the same level as bribery of public officials. Federal freedom of information legislation entered into force in January 2006, but is seen by many as ineffective. Several states have introduced their own freedom of information laws. The German government has successfully prosecuted hundreds of domestic corruption cases over the years. Numbers rose especially significantly in the three years. To date, only a small number of charges have been filed involving the bribery of foreign government officials since the 1999 changes in German law to comply with the OECD Anti-Bribery Convention were enacted. However, the corruption scandal involving Siemens AG with its ongoing litigation and fines and the recent agreement with the Securities & Exchange Commission on an $800 million fine has focused attention on foreign bribery for the first time.

**Bilateral Investment Agreements**

Germany has investment treaties in force with 121 countries and territories. Of these, eight are with predecessor states and indicated with an asterisk (including Czechoslovak SFR, Soviet Union, Yugoslavia [SFRY]). Treaties are in force with the following states: Afghanistan; Albania; Algeria; Angola; Antigua and Barbuda; Argentina; Armenia; Azerbaijan, Bangladesh; Barbados; Belarus; Benin; Bolivia; Bosnia and Herzegovina; Botswana; Brunei; Bulgaria; Burundi; Cambodia; Cameroon; Cape Verde; Central African Republic; Chad; Chile; China (People's Republic); Congo (People's Republic); Congo (Democratic Republic); Costa Rica; Croatia; Cuba; CSFR**; Czech Republic*; Dominica; Ecuador; Egypt; El Salvador; Estonia; Ethiopia; Gabon; Georgia; Ghana; Greece; Guatemala; Guinea; Guyana; Haiti; Honduras; Hong Kong; Hungary; India; Indonesia; Iran; Ivory Coast; Jamaica; Jordan; Kazakhstan; Kenya; Republic of Korea; Kuwait; Kyrgyzstan*; Laos; Latvia; Lebanon; Lesotho; Liberia; Lithuania; Macedonia; Madagascar; Malaysia; Mali; Malta; Mauritania; Mauritius; Mexico; Moldova*; Mongolia; Morocco; Mozambique; Namibia; Nepal; Nicaragua; Niger; Nigeria; Oman; Pakistan; Panama; Papua New Guinea; Paraguay; Peru; Philippines; Poland; Portugal; Qatar; Romania; Russia*; Rwanda; Saudi Arabia; Senegal; Sierra Leone; Singapore; Slovak Republic*; Slovenia; Somalia; South Africa; Soviet Union**; Sri Lanka; St. Lucia; St. Vincent and the Grenadines; Serbia; Sudan; Swaziland; Syria; Tajikistan*; Tanzania; Thailand; Togo; Tunisia; Turkey; Turkmenistan; Uganda; Ukraine; United Arab Emirates; Uruguay; Uzbekistan; Venezuela; Vietnam; Yemen (Arab. Rep.); Yugoslavia (SFRY)**; Zambia; and Zimbabwe.

(Note: Asterisk * denotes treaty in force with predecessor state; Asterisks ** denote continued application of treaties with former entities, which have not been taken into account in regard to the total number of treaties.)

Germany does not have a bilateral investment treaty with the United States, but an FCN treaty dating from 1956 remains in force. Taxation of U.S. firms within Germany is governed by the 1989 "Convention for the Avoidance of Double Taxation with Respect to Taxes on Income." It has been in effect since 1989 (and since January 1, 1991, for the area that comprised the former
German Democratic Republic.) With respect to income taxes, both countries agree to grant credit to their respective federal income taxes for taxes paid on profits by enterprises located in each other's territory. The German system is more complex, but there are more similarities than differences between the German and U.S. business tax systems. On December 28, the U.S. and Germany ratified the Protocol of June 1, 2006, amending their 1989 income tax treaty and protocol. The new protocol updates the existing treaty and includes several changes, including a zero-rate provision for subsidiary-parent dividends, a more restrictive limitation-on-benefits provision and a mandatory binding arbitration provision.

Labor

The German labor force is generally highly skilled, well educated, disciplined, and very productive. The complex set of reforms of labor and social welfare-related institutions implemented under the former SPD/Greens Government contributed to overcoming structural weaknesses of the German welfare state and creating an institutional setup more conducive to strong employment growth and lower unemployment. A series of changes in collective bargaining has supplemented government efforts in recent years.

Chancellor Angela Merkel’s Grand Coalition initiated more reform measures, such as a gradual increase in the mandatory retirement age from 65 to 67 – a move that would add 2.5 million to the workforce by 2030 – and an initiative aimed at reducing unemployment among older workers and discouraging early retirement. The former grand coalition also encouraged female labor market participation by measures that would make it easier for mothers to work – for example, longer school hours and more day-care centers. To address the problem of Germany’s low birth rate, it also adopted a new “parents’ allowance,” which entitles parents who give up work or reduce their hours of work to care for their newborn children to a compensatory monthly payment for a period of one year.

To address rising health care costs, Germany implemented numerous health care reforms, most recently in April 2007. The introduction of a Health Fund is the key pillar of reform: Beginning in 2009, insured persons’ contributions to the statutory health insurance companies are standardized. For each insured person, the health insurance companies receive a flat rate from the Health Fund. At the same time, tax financing of health insurance services, such as contribution-exempt insuring of children of insured parents, commenced. From 2009 onward, insurance has become compulsory for everyone, and private health insurance companies are obliged to accept insured persons at the base rate.

Germany does not have a statutory minimum wage. However, binding minimum wages have been established in 14 sectors (e.g., construction, electrical trades, painting, mail) covering an estimated 1.4 million workers. In August 2009, employers and union representatives agreed to introduce minimum wages for approximately 170,000 workers in waste management, large-scale laundries,
and special mining services. The new CDU/CSU-FDP coalition is opposed to the introduction of a national minimum wage but advocates a legal ban on “immoral” wages, i.e., wages which are one-third below average wages in a given sector.

After several years of solid economic growth and declining unemployment, the global financial crisis finally hit Germany at the end of 2008. Although the collapse in global demand had an especially damaging effect on Germany’s export-driven economy, the labor market weathered the economic crisis exceptionally well, with employment levels down a mere 0.2% to 40.4 million year-on-year in contrast to a GDP collapse of about 5%. The number of persons out of work averaged 3.423 million in 2009, an increase of 155,000 as compared with 2008. The average unemployment rate as a percentage of the total civilian labor force rose 0.4 percentage points to 8.2% in 2009.

Among the reasons behind the surprising resiliency of the labor market – in addition to the widespread use of government-funded short-time work programs – is one explanation why the massive economic collapse came unexpectedly and employment could not be adjusted from one day to the next because of institutional barriers such as employment protection. More likely, however, many companies entered the recession with a better capital cushion than previously and deliberately decided to keep highly skilled labor in hopes of riding out the crisis. In addition, large sections of the services sector (e.g., health and welfare, education and training) have not been hit by the recession and are continuing to create jobs. But unemployment will certainly increase in 2010, since the labor market traditionally lags other macro-economic indicators, which in late 2009 showed first signs that the recession was easing. Hence, the German government expects unemployment to average 3.6 to 3.7 million in 2010.

In June 2009, the Institute of Economic and Social Research presented its interim report on Germany’s 2009 round of collective bargaining. The study evaluates the collective agreements concluded in the first half of 2009, affecting about 25% of all employees covered by such agreements. Calculated on an annual basis, the average increase in wages and salaries amounts to about 3% in 2009, which is slightly above the average pay increase of 2.9% in 2008.

There is still a considerable gap in earnings between men and women in Germany. Collective agreements concluded in the first half of 2009 did not include provisions to tackle wage discrimination and to promote equal opportunity.

Since the late 1990s, Germany’s system of wage determination through multi-company, industry-wide contracts has become considerably more decentralized. Although sector-wide labor agreements can set wages and working conditions at high levels in some industries, company-level agreements frequently deviate significantly from them. Many industry-wide contracts have been
revised in recent years, not only to include highly flexible working time arrangements but also to introduce escape clauses for ailing companies, and to lower entrance pay scales and performance-based annual bonuses. Moreover, the coverage of collective agreements has been declining. Multi-company, industry-wide contracts cover about 43.4% of all firms; 5.3% are covered by a company-level agreement; and 51.3% are not covered at all. Coverage in the eastern states is even lower than in the west. In terms of workers covered by a collective agreement, 73.6% of workers are covered, while 26.4% are uncovered. Again, the coverage is higher in the west than in the east.

To cope with the impact of plant closures and redundancies, several unions negotiated a new type of collective agreement (Sozialtarifverträge) to regulate plant closures or relocations of sites. These agreements usually provide for the transfer of employees to “job creation” agencies, training, and redundancy payments.

Germany’s education system for skilled labor, combining on-the-job and in-school training for apprentices, produces many of the skills employers need. There are rigidities in the training system, however, such as restrictions on night work for apprentices, to which some employers object. Another criticism is that the system is inflexible with regard to occupational categories and training standards. Labor unions complain employers do not establish enough training slots and do not hire enough of the trainees after their training is completed. Regulatory obstacles to workers’ mobility remain high in Germany (and throughout the EU) and have also contributed to serious labor shortages in many high-skilled fields, above all for engineering, technical professions and manufacturing trades. An important element of German labor market policy is public support for training. The country’s response to the crisis has included an expansion of existing measures as well as the introduction of new schemes, with total additional spending estimated at €1.97 billion, or 36% of the labor market part of the government’s stimulus program. A 2009 case study found that the publicly funded training is helping to address skills shortages present before the advent of the crisis.

While trade union membership has continued to decline since the beginning of the 1990s, there has been a notable slowdown of this development in recent years. About 21% of the workforce is organized into unions. The overwhelming majority are in eight unions largely grouped by industry or service sector. These unions are affiliates of the German Trade Union Federation (DGB). Several smaller unions exist outside the DGB, principally in white-collar professions. Since peaking at more than 13 million members shortly after German re-unification, total union membership has steadily declined to 6.3 million at the end of 2008.

Unions’ right to strike and the employers’ right to lock out are protected in the German constitution. Court rulings over the years have limited management recourse to lockouts, however. Institute of Economic and Social Research data published in April 2009 reveal that industrial action in Germany in 2008 involved 1.6 million striking workers – about one million more than in
2007. However, the estimate of 542,000 days not worked was about 25% less than in 2007. On the other hand, the official records of the Federal Employment Agency counted just 154,052 strikers, amounting to 131,679 days not worked; incomplete reporting may explain this disparity.

At the company level, works councils represent the interests of workers vis-à-vis their employers. A works council may be elected in all private companies employing at least five people. The rights of the works council include the right to be informed, to be consulted, and to participate in company decisions. Works councils often help labor and management to settle problems before they become disputes and disrupt work.

“Codetermination” laws give the workforce in medium-sized or large companies (stock corporations, limited liability companies, partnerships limited by shares, co-operatives, and mutual insurance companies) significant voting representation on the firms’ supervisory boards. This codetermination in the supervisory board extends to all company activities.

**Foreign Trade Zones/Free Trade Zones**

There are seven free ports in Germany established and operated under EU Community law: Bremerhaven, Cuxhaven, Deggendorf, Duisburg, Emden, Hamburg and Kiel. These duty-free zones within the ports also permit value-added processing and manufacturing for EU-external markets, albeit under certain requirements. All of them are open to both domestic and foreign entities. Falling tariffs and the progressive enlargement of the EU have in recent years gradually eroded much of the utility and attractiveness of duty-free zones, but there are currently no plans to eliminate them.

**Foreign Direct Investment Statistics**

According to the U.S. Department of Commerce’s Bureau of Economic Analysis, in 2007 German direct investment in the United States was worth $ 203 billion while U.S. direct investment in Germany was worth $107 billion. Foreign investment has been particularly strong in eastern Germany where about 1 trillion Euros have been invested since 1991, of which an estimated 84% came from private, non-government sources. Some 2,000 foreign companies, including 300 U.S. firms, have invested in eastern Germany since reunification.

[Read the full market research report](#)