Post-Industrial Welfare States in Comparative Perspective

by

Joel Philip Michaels
Class of 2018

A thesis submitted to the faculty of Wesleyan University in partial fulfillment of the requirements for the Degree of Bachelor of Arts with Departmental Honors from the College of Social Studies

Middletown, Connecticut April, 2018
# Table of Contents

List of Figures and Tables 3

Acknowledgements 4

Introduction 5

1 Literature Review and Genealogy 16

2 Toward a New Understanding of Welfare State Change 53

3 U.S. Old Age Pensions and Guided Institutional Drift 91

4 Unemployment Insurance and the Erosion of the German Model 133

Conclusion 168

Bibliography 175
List of Figures and Tables

<table>
<thead>
<tr>
<th>Figure 3.1</th>
<th>Public and Private U.S. Pension Spending, 1975-2014</th>
<th>99</th>
</tr>
</thead>
<tbody>
<tr>
<td>Figure 3.2</td>
<td>Number of Pension Plans by Type, 1975-2014</td>
<td>104</td>
</tr>
<tr>
<td>Figure 3.3</td>
<td>Private Benefit Disbursements by Type, 1975-2014</td>
<td>104</td>
</tr>
<tr>
<td>Figure 4.1</td>
<td>Unemployment in Germany, 1975-2016</td>
<td>140</td>
</tr>
<tr>
<td>Table 2.1</td>
<td>Summary of Welfare State Scholarship</td>
<td>54</td>
</tr>
<tr>
<td>Table 4.1</td>
<td>Overview of Hartz “Laws for Modern Services on the Labour Market”</td>
<td>149</td>
</tr>
</tbody>
</table>
Acknowledgements

This thesis bears one name, but many sets of fingerprints. First thanks must go to my advisors, Professors John Bonin and Gil Skillman, whose simultaneous attention to granular detail and overarching argument have strengthened this thesis immeasurably. Professors Richie Adelstein, Marc Eisner, and Victoria Smolkin, as well as Professor Jacob Hacker at Yale, also offered valuable feedback and support. I am likewise grateful to Professors László Bruszt and Carsten Schneider of Central European University, whose political economy seminar first introduced me to the world of comparative capitalism.

My theoretical orientation to labor markets and social policies has been greatly influenced by these professors and mentors. As to learning how those concepts work in practice, I am indebted to my past colleagues at the U.S. House Committee on Education and the Workforce. In particular, I wish to thank Tylease Alli, Denise Forte, Brian Kennedy, Richard Miller, Véronique Pluviose, and Liz Watson, and not least Ranking Member Bobby Scott.

With respect to institutions, a Davenport Study Grant from Wesleyan’s Public Affairs Center supported earlier comparative research on labor markets. The librarians at the Hagley Museum and Library in Wilmington, Delaware were gracious in their help with my research. Most of all, the tutors and students of Wesleyan’s College of Social Studies have taught me much about the world and built an incomparable arena in which to develop and refine my ideas.

My friends at Wesleyan and beyond have been a fount of moral and intellectual support. Mihai Olteanu read an entire draft of this thesis in manuscript form; Zach Tan looked after me during a workshop session; Gabriel Kachuck and Brendan McGlone proved excellent editing companions; and Sallie Fullerton and Ernie and Jeri Drucker opened their homes to me at various stages along the way. Many others, some merely by feigning interest in my project, have sustained me over the past months.

Finally, I am grateful for the loving care of my family, without whom I would be in no position to even begin to understand the topics discussed here, much less write about them. The memory of my late grandparents, in a time of great political darkness, serves as a guiding light towards the possibility of a more just order. I am nothing without Lila Michaels, who knows what to ask; David Michaels; who knows what must be done; and Gail Dratch, who knows what it will take.

I have long been puzzled by the exceeding generosity of those in my life—in their time, their candor, their willingness to put up with my foibles—and have come to understand it in part as a long-term investment, in the hopes that I might build upon my privileged upbringing to do something socially useful. This represents a first attempt.
Introduction

“The whole problem is rooted in the question: does the state have the responsibility to care for its helpless fellow citizens, or does it not? I maintain that it does have this duty, and to be sure, not simply the Christian state, as I once permitted myself to allude to with the words ‘practical Christianity,’ but rather every state by its very nature.”

— Otto von Bismarck, “Speech on the Law for Workmen’s Compensation” (1884)

“The belief that the object of government in peace and in war is not the glory of rulers or of races, but the happiness of the common man...is a belief which...unites...democracies and all their Allies.”

— Sir William Beveridge, Social Insurance and Allied Services (1942)

With these two statements, Bismarck and Beveridge helped lay the foundations for the modern welfare states of Germany and Great Britain. In their rhetorical appeals, each spoke to a universal obligation of the state, seeking to bolster concrete policy proposals with a sense of fundamental imperative. Yet tellingly, the universal principles each alluded to are not the same. For Bismarck, speaking in favor of a workers’ compensation bill before a fiercely divided Reichstag, the state’s duty was to help the “helpless,” reducing the risk of destitution for those who might encounter it out of no fault of their own (such as through an industrial accident). For Beveridge, writing the report that would spur the creation of the National Health Services (NHS), the state’s

---


duty was instrumental, in helping “the common man” achieve what he could only find individually: a sense of “happiness.” 3 To speak of the ‘welfare state,’ out of context, then, is to speak of very little: collections of social policies in different jurisdictions with widely varying philosophical purposes, not least formal attributes. But to speak of ‘welfare states,’ in a comparative light, is another matter. Doing so allows for analysis not only of how different states treat their citizens, but of how different political economies develop in response to different environments, and of how they have changed over time. By comparing the trajectories of multiple ‘welfare states,’ one might catch a glimpse of the intrinsic qualities of the ‘welfare state.’

This thesis begins with a question of institutional diversity; by its conclusion, it offers a portrait of institutional homogeneity. It surveys a wide range of literature demonstrating how welfare states in different industrialized countries vary from one another, and probes different theories for why this is the case. But while acknowledging the historical variance of social policy regimes, it argues that welfare states in advanced economies are actually becoming more similar to one another, and have been progressing in this direction since the 1970s. They are gradually converging upon what might be called a neoliberal model of the welfare state: that is, though global welfare states have moved closer to or doubled down on features that historically characterized a ‘Liberal’ institutional model like that of Great Britain or the United States—such as

---

3 Note that the NHS, in part because of the influence of early Labour Party administrator Aneurin Bevan, is arguably the most redistributive component of the British welfare state, in some sense the exception rather than the rule. Beveridge himself belonged to the Liberal Party, and though he did not personally support means-testing (see below for a definition) of social benefits, that sort of policy is typical of the Anglo-American welfare ‘model.’ The epigraph is intended to demonstrate the philosophical basis of one historic variety of the welfare state. Moving forward, the example of Great Britain will be discussed only tangentially.
dualized welfare benefits disparately benefiting different social strata, and means-testing of those benefits for low-income individuals—those residual benefits are imbued with a new kind of institutional logic. Rather than offering individuals social protection against destitution or a disadvantageous position in labor market bargaining, welfare states are being reoriented to the task of expanding the scope of national labor markets, and employers’ bargaining power within them.

This thesis’ primary aim is to lay out and corroborate the convergence hypothesis. Its secondary goal, of nearly equal importance, is to supplement it with a corresponding theory of institutional change, positing the underlying causes of convergence and the historical actors who have acted in its service. At once emphasizing structure and agency, I will describe some of the shared systemic conditions of post-industrialism that have motivated welfare state change across diverse national contexts, and the very real advocacy of firms and their representatives who have worked to implement such change. Institutions, as Wolfgang Streeck and Kathleen Thelen have argued, are formed in the interaction between ‘rule-makers’ and ‘rule-takers,’ bounded by the larger environment in which those rules operate. The task at hand is to examine how the rules are changing and why, and whether the change is parochial in nature or will come to affect wide swaths of the global population. The answer to this question—especially if it is the latter—may well prove critical to understanding the shape of the ‘welfare state’ today.

Defining Terms

An inquiry of this sort must begin with some definitions. The ‘welfare state’ is a particularly amorphous term, as it can refer to a wide variety of benefit programs constituted along different lines. Welfare policies may benefit the elderly, the unemployed, the disabled, or the generally downtrodden; they may be distributed through public expenditures or by subsidy of private ones; they may be offered on the basis of occupational status, or on the basis of citizenship status; and they may be constructed through social insurance, with benefits calculated in proportion to past contributions, or as redistributive programs, based upon the principle of social solidarity. Sometimes scholars refer to the ‘welfare state’ extremely broadly, as a way of describing the general character of governments in industrialized countries in the post-war West. But the most proper definition of the welfare state is the means with which societies have marshalled their collective tools—pooling risk across great numbers of individuals or sharing the fruits of general prosperity—to protect individuals from economic hardship, and especially the kinds of hardship particular to contemporary life. In advanced economies, the greatest threat to an individual is not of death by interpersonal violence, or of being left to the wolves, but of losing one’s means of

---

5 Welfare benefits distributed by exempting private expenditures from taxation—for example, by deferring capital gains taxes on investment income or by allowing employers to deduct their contributions to employee benefit plans from corporate taxes—are referred to here as part of the ‘submerged state.’ The term references the structure of an iceberg: while government appropriations are visibly above water, other programs are supported by declining to collect revenues, and are thereby effectively invisible. For appropriations and tax-exemptions of equal size, the net effect on the treasury is identical, but the public visibility of those programs—and their corresponding politics—is very different. Importantly, unlike appropriations, tax exemptions usually do not have to renewed by statute on an annual basis.
If one seeks a single variable by which to measure the strength of a welfare state, the best option is to examine how much it ‘de-commodifies’ the labor power of an average individual in that society. The more developed the welfare state, the less that individual feels the obligation to take up employment irrespective of its potential undesirability—whether because of low wages and benefits, or their own old age, health, or familial issues—in order to achieve a reasonable standard of living.

Welfare states are comprised of ‘social policies’ which establish legal rights to benefits, technical formulas used to calculate them, and funding mechanisms by which to pay for them. They are examples of political-economic ‘institutions,’ another term that will appear frequently throughout this thesis. Though changes to policies very well may (and nearly always do) result in changes to institutions, the two concepts are not fully coextensive. Evolving labor market or demographic conditions may change the character of an institution even while the statutory rules that underlie it remain the same. The establishment (or elimination) of one program may have a carry-over effect, decreasing (or increasing) benefit claims on another. Even social attitudes towards welfare states—the degree of confidence that an entitlement or earned benefit will be available long into the future, or the stigma associated with being a recipient of a particular benefit—impact the behavior of those who rely upon them, and therefore their institutional character. Institutions, per Streeck, “are norms that regulate social behavior; they are realized and reproduced in practice through human agents applying

---

* The scourges of gun violence and police brutality, it must be noted, complicate this generalization with respect to the United States.
them to their specific situations.”7 When discussing the structural causes and agents behind institutional change, this thesis refers specifically to changes to the welfare state. But if successful, the underlying framework may also have broader applicability, and could be used to examine changes to corporate finance, corporate governance, or vocational training institutions, to name just a few.

Finally, this thesis will make repeated references to the concept of ‘retrenchment.’8 I employ this term because of its widespread usage in the literature but aim not to be constrained by its frequent dictionary definition as mere ‘cost cutting.’ In this thesis, retrenchment is understood as the broader phenomenon of reductions in the generosity of a given welfare state, which may or may not coincide with a reduction in expenditures. Means-testing of benefits—conditioning them on the relative impoverishment of recipients—or the addition of work requirements are forms of retrenchment. A welfare state may offer consistent benefit levels but to a shrinking population of eligible individuals, perhaps by virtue of changing labor market status. Some scholars have referred to this phenomenon as a form of institutional ‘drift,’ but it nonetheless fits within the rubric of retrenchment. Defining this concept, and that of the welfare state more largely, is necessary for the sake of analytical clarity. But the true

8 There exists a significant literature on the concept of retrenchment itself, chiefly in the domain of political science, which focuses on the political barriers to retrenchment. The seminal work is Paul Pierson, Dismantling the Welfare State: Reagan, Thatcher, and the Politics of Retrenchment, Cambridge Studies in Comparative Politics (Cambridge: Cambridge University Press, 1994). I reference this literature but it is not a main focus of the thesis, which is less interested in the obstacles to retrenchment than the efforts of those attempting to surmount them and, moreover, those efforts’ apparent success across very different political-economic contexts.
task is to uncover why the concept of retrenchment is relevant, and to such different political economies at the same time.

**Plan of the Text**

The thesis that follows is divided evenly between theoretical and empirical work. In the first half of the text, I develop a working hypothesis of how and why welfare states in advanced economies have changed over the past several decades; in the second half, it is evaluated in light of two case studies. Chapter 1 is structured as a literature review, broadly focusing on two different schools of thought that seek to explain welfare state diversity. ‘Historical institutionalists’ offer an account of different welfare states constructed through dialectical conflict between market and society, with their characteristics largely contingent upon the strength and effectiveness of working class mobilization. Conversely, ‘rational choice institutionalists’ have an essentially functionalist and equilibrium-oriented view of welfare state formation, wherein agents of capital support different kinds of welfare states (at times even highly generous ones) depending on the larger institutional environment in which they operate. In addition to summarizing these literatures, I attempt to highlight the inconsistencies in their understandings of the agents of welfare state development and how institutional change occurs more generally. This is achieved in part by tracing upward the intellectual genealogies of both literatures, from the historical institutionalists to the work of Karl Polanyi, and from the rational choice institutionalists to that of mid-twentieth century modernization theorists.
The analytical core of the thesis, chapter 2, attempts to synthesize these two literatures while also rejecting some elements of both. In place of a static typology of different kinds of welfare regimes, I argue that the best way to compare welfare states is to examine how they have evolved over the last several decades, probing whether those processes and their underlying causes bear any structural similarity to one another. A working hypothesis of this sort is laid out, bolstered by the two literatures and their antecedents from chapter 1. I contend that firms have acted as primary agents of welfare state liberalization across diverse post-industrial political economies, in part by pursuing legislative policies and collective bargaining strategies that weaken the power of labor unions as a countervailing force to resist such changes.9 They are responding, I hypothesize, to a structural ‘logic of post-industrialism’ involving the prospect of secular stagnation, greater financialization of the world’s economies, the changing nature of work in favor of service sector employment, and globalization more generally. Collectively, these forces have placed pressure on firms to reduce payroll expenses and maximize their market power in labor negotiations, which they have sought to do through welfare state retrenchment. I then lay out an array of tools that firms have used in pursuit of this goal, from political lobbying to funding intellectual work to the threat of capital flight unless welfare state reforms are put in place. The overall hypothesis can be thought of as extending Polanyian theory into the present day, observing how firms

9 Indeed, the few cases that throw into question the idea of welfare state convergence around the retrenchment of benefits in order to liberalize labor markets are ones where trade union strength has been consistently robust. See chapter 2 for a more detailed discussion of this point.
in very different national contexts have sought to dis-embed the social protections achieved by working class movements throughout the twentieth century.

Chapters 3 and 4 examine the working hypothesis through two detailed case studies. Their selection is intended to capture the diversity of welfare state models discussed in chapter 1, searching for shared systemic trends in very different political-economic contexts. The first case study is an analysis of the evolution of private old age pensions in the United States, chiefly from generous defined benefit plans to defined contribution ones, such as 401(k)s, that place greater risk on individual workers. The analysis is aided by primary source research into the papers of the National Association of Manufacturers and U.S. Chamber of Commerce, which indicates the central role of U.S. firms in spurring welfare state retrenchment in this area. Though the story of the ‘401(k) revolution’ has been told many times over, my analysis is unique in emphasizing the precursory role of anti-labor legislation in the late 1940s, which prohibited unions from controlling old age pension funds. It also highlights how U.S. firms sought to incentivize individual worker responsibility for retirement savings—and prevent the federal government from stepping in to provide greater social protections—well before the proliferation of defined contribution plans.

The case study in chapter 4 analyzes changes to unemployment insurance in Germany that have reduced eligibility for benefits and the maximum amount of time a worker can receive them. Particular focus is placed on the 2003-4 ‘Hartz’ reforms that reorganized unemployment insurance, and the role of German employer associations in mounting a public relations campaign in favor of the legislation and supporting the government ministers who promulgated it. The case study also traces the connection
between declining unemployment insurance coverage and the erosion of German industrial relations more broadly. Decentralization of collective bargaining has not only paved the way for greater numbers of low-wage, welfare-ineligible workers, but also (paralleling the U.S. case study) weakened the power of trade unions to resist welfare state reforms.

These case studies provide strong evidence of convergence of social policy regimes in the U.S. and Germany, two countries held up as archetypal models of different kinds of welfare states by both historical and rational choice institutionalists. The timeframe of the U.S. case study, which begins in the heyday of the postwar economic order, brings into question the idea that welfare state retrenchment is everywhere a response to the exogenous shocks of globalization and the logic of post-industrialism more generally. In Germany, however, the 1970s do seem to be a historical tipping point in evolving character of that country’s welfare state. On this element of the working hypothesis, the evidence is murky. But in both cases, it is clear that welfare state retrenchment was not an automatic consequence of structural conditions: it found strong advocates in firms and their representatives. Both indirectly, such as through their approach to labor relations, and directly, through their advocacy for government policies, firms have been on the frontlines of retrenchment.

*On Political Economy in the Time of Cholera*

One of the major challenges of academic writing is limiting oneself to a contained area of inquiry. To submit a thesis discussing the situation of post-war Germany, for example, without referencing the horrors of the wartime period, is a very
strange thing indeed (especially for the present writer, a descendant of German Jewish refugees). Yet one must be careful not to bite off more than he can chew; upon finishing this thesis, the reader may nonetheless conclude that I have done just that. One way I have limited my inquiry is by skirting the question of whether or not global welfare states are converging upon a ‘neoliberal’ institutional model. Although I believe this to be the case, absent the discussion above, I will scarcely use the term neoliberal or its derivatives in the text at all. The aim here is to identify substantive policy similarities between previously diverse political economies, not to get bogged down in proving their correspondence to a larger concept whose contours (and indeed, very existence) are acutely controversial. ¹⁰ This thesis strives to be diagnostic, rather than prescriptive, about changes to global welfare states over the past several decades. But it remains my hope that examining the symptoms of the patients, in one limited sphere of political economy, might help with identification of the disease.

1 Literature Review and Genealogy

Introduction

A thesis positing that welfare states are becoming more similar to one another must first begin with an examination of why they are different in the first place. Fortunately, there already exists a great deal of literature on this subject. It has strived to identify the historical antecedents of welfare regimes and couple them with a theoretical conception of how institutions behave over time. The ultimate aim is to produce a classification of observed welfare states clustered around multiple abstract ideal types, or a ‘typology.’ In this manner, scholars seek to isolate the unique characteristics of different kinds of welfare states and offer a predictive model for what kinds of social policies might develop in a given political-economic context. Later in the thesis, I will question this methodology in its entirety, largely because it rests upon an a priori understanding of welfare state diversity. But a review of this literature is not only important for the sake of context and scholastic continuity. It will also offer the building blocks for developing a new theory of welfare state change.

The literature as described here is largely divided between two different schools of thought, and two corresponding welfare state typologies. On the one hand, there is a long tradition of scholarship seeking to describe welfare state formation in terms of ‘historical institutionalism.’ It emphasizes contingent historical factors such

---

1 I use the admittedly amorphous word “behave” precisely because the literature offers highly different conceptions of institutions more generally. As will become apparent, one school of thought emphasizes welfare state development alongside a clear vision of institutional change, while the other imagines it occurring in reaction to an essentially extant institutional environment.
as constitutional design, religious divisions, and demographic structures as important determinants of the character and pace of welfare state formation. One particularly important component of this literature, exemplified by the work of Theda Skocpol, focuses on the role of the state in social policy development. But by far the most influential work within this literature emphasizes welfare states as the product of protracted class struggle, often referred to as ‘power resource theory.’ This narrative is as much a product of historical evidence documenting the importance of labor unions and social democratic parties in welfare state development as it is the necessary consequence of the way its adherents understand the function of the welfare state at its apotheosis: to ensure downward redistribution of resources to lower-income individuals. The arguably definitive statement in the historical institutionalist school—Gøsta Esping-Andersen’s *The Three Worlds of Welfare Capitalism*—quantifies social policies chiefly by how much they ‘de-commodify’ the need of an average citizen to work in order to maintain a given standard of living.

On the other hand, the last two decades have seen a proliferation of literature in the vein of ‘rational choice institutionalism,’ which broadly understands social policies as the consequence of actors responding to market incentives. In this telling, firms usually play a critical role in explaining welfare state development and are hypothesized to *support* generous social policies under specific circumstances, such as where they allow for advantageous distribution of labor market risk or bolster firms’ ability to differentiate skilled workers’ compensation. Because this literature emphasizes the role of firms in creating social policies, it necessarily rejects the idea that they are meant to ‘de-commodify’ labor. Instead, rational choice institutional
theorists often conceptualize social policies by the degree to which they *bind* workers to a given firm or industry, frequently by incentivizing them to acquire particular skills. This mode of scholarship is exemplified by Peter A. Hall and David Soskice’s formulation of ‘Varieties of Capitalism,’ which describes different capitalistic production regimes as underpinned by complementary bundles of institutions, formed because each institution maximizes the efficacy of the others: essentially, formed because the inherent logic of institutions dictates as much.

The distinctions between these two literatures will become more evident by tracing their intellectual genealogies. As I will contend here, the rational choice literature is rooted in comparative industrial policy work dating from the 1960s, which hypothesized the convergence of institutions in developed nations because of a shared structural ‘logic of industrialism.’ Historical institutionalist scholarship on the welfare state can be seen as an extension of Karl Polanyi and T.H. Marshall’s ideas about tensions between market and society. Though some authors in both schools have gestured at one another as if to suggest their findings are mutually compatible, in reality the gap between them is quite significant. The historical school, in essence, describes welfare states as the consequence of dialectical struggle between labor and capital; labor is the protagonist in the sense that the more effectively it organizes for political action, the stronger the resultant welfare state. The rational choice school has a functionalist conception of the welfare state—it develops when it enhances other factors of production—and sees social policies as corresponding to the needs of capital. Put otherwise, the two literatures contest whether forces of labor or capital are
the true progenitors of welfare states, as well as whether they are actually formed through active contestation between labor and capital.

The literature on the welfare state—a central feature of modern-day governments—is vast, and combing through it a formidable task. This chapter first examines scholarship that can be thought of as fitting into the historical institutionalist school, then looks back to the school’s theoretical ancestors. Next comes an in-depth treatment of Esping-Andersen’s text, which offers a typology of welfare regimes in line with historical institutionalist scholarship. The second half of the chapter replicates these three components for rational choice institutionalist scholarship, but in a different order: first genealogy, then typology, followed by the broader literature.² There is a great deal of material here, much of which paints a picture of national welfare states that is no longer descriptive of the way they appear today. This is no accident. The aim is to examine historical explanations for the rise of different kinds of welfare states with an eye to re-orienting those theories to explain how they are changing in the present moment. Moreover, highlighting the contradictions in the literature—concerning the agents of welfare state development, their motivations, and how they come to shape institutions over time—will demonstrate both the need for a new kind of synthesis, and the tools with which one might be constructed.

² I have intentionally sacrificed structural symmetry for the sake of narrative continuity.
Efforts to parse the historical development of welfare states in Western Europe and North America have placed emphasis on a great variety of explanatory variables. Some historical institutionalists have drawn a linkage between religious legacies and welfare states: Huber and Stephens describe conflict between Catholics and Protestants (particularly in the European Lowlands) as preventing the emergence of unified labor movements, and by extension strong welfare states, prior to World War II.  

Crouch emphasizes the Catholic Church’s sponsorship of religious-affiliated unions as a key influence for the emergence of corporatist—rather than pluralist or adversarial—labor relations and social policy. In addition to the Church’s influence on labor organizing, Catholic doctrinal teachings have also been cited as determinants of welfare policies. Huber and Stephens (in the same volume) suggest that strongly Catholic countries tend to distribute welfare benefits through male bread-winners, with the aim of reinforcing single-family social units.  

Compston argues that Christian emphases on “class cooperation” and “social harmony” have resulted in greater willingness to accept work-sharing initiatives in the Netherlands, Belgium, and Italy. In those countries, where social benefits are largely determined based on

---

the level of workers’ contributions to insurance schemes, increasing part-time work necessarily affects the generosity of welfare payments.

Others contend that legacies of political authoritarianism—and different paths to democratization—are in part responsible for welfare state diversity. Flora and Alber hypothesize that monarchical states and those where suffrage was exercised only by a small landed elite were likely to dole out poor relief in place of entitlements to welfare benefits. In constitutional monarchies where suffrage was more widespread, as under Bismarck’s Germany, welfare institutions formed “a defense against full participatory rights and a means to strengthen working class loyalty for the authoritarian state.” 7 Other authors consider the effects of more recent authoritarianism. Huber and Stephens, for example, contend that the experience of totalitarian regimes in Germany and, to a lesser extent, occupied France during World War II prevented post-war implementation of comprehensive social insurance schemes in those countries. 8

A number of authors have explicitly examined constitutional design as predictive of welfare state development. Comparing public health insurance systems across Western Europe, Immergut contends that states with diffuse power relations—whether through federalism, bicameralism, or separate elections of the legislature and executive—create multiple ‘veto points’ wherein minority constituencies can block

social reform. Writing on a similar topic, Maioni attributes the discrepancy in national health insurance coverage between the United States and Canada in part to the two-party duopoly in the U.S. and relatively rigid party discipline amongst lawmakers. King and Wood, differentiating the degree of welfare state retrenchment under Reagan and Thatcher in the U.S. and U.K., respectively, remark upon the speed with which legislation can be passed under parliamentary systems. Others contend that states with majoritarian legislatures tend to enact greater increases in social spending in response to economic downturns than states with proportional legislatures.

One particularly influential segment of the literature contends that state agents such as civil servants, motivated more by ideology than pecuniary concerns, are a key force behind welfare state development. Heclo argues that social policy ideas influence bureaucratic behavior more than they do electoral outcomes, and that changes to the welfare state often occur through personnel or administrative budget changes. Skocpol and her collaborators have elaborated on this theory at length,

---

12 Torben Iversen, “Economic Shocks and Varieties of Government Responses,” in *Beyond Varieties of Capitalism: Conflict, Contradictions, and Complementarities in the European Economy*, ed. Bob Hancké, Martin Rhodes, and Mark Thatcher (New York: Oxford University Press, 2007), 294. Note than while this insight is consistent with the larger literature emphasizing the role of constitutional design on welfare state formation, Iversen’s research generally adopts a rational choice methodology in place of historical institutionalism. See the discussion of his work, particularly with David Soskice, later in this chapter.
claiming that state agents play a critical role as catalysts in “establishing the power of key actors, [and] in influencing the kind of coalitions that were likely to come together” to enact legislation.\textsuperscript{14} According to one version of this thesis, bureaucrats also act as ‘rent-seekers,’ independently of other constituent groups, in order to entrench government agencies and secure their own power. Skocpol and Ikenberry highlight the scale of civil war pensions in the U.S. during the Gilded Age and suggest that they resembled a kind of proto-welfare state, but claim that progressive reformers failed to build upon veterans’ pensions because they saw them as evidence of pernicious graft.\textsuperscript{15} More pertinently, they argue, there was far less administrative bureaucracy in the United States during this period than was present in Continental Europe, and thus fewer individuals with a vested interested in increasing the size of the state.\textsuperscript{16}

This statist conception of social policy development is usually thought of as analytically distinct from the social democratic or ‘power resource’ approach (which I address momentarily).\textsuperscript{17} Here, I consolidate them, because the underlying conception


\textsuperscript{15} Theda Skocpol and John Ikenberry, “The Political Formation of the American Welfare State in Historical and Comparative Perspective,” \textit{Comparative Social Research} 6 (1983). Civil war pensions were the largest single federal expenditure from 1885 to 1897, and in 1890 made up a full one-third of the federal budget.

\textsuperscript{16} Ibid., 101-2.

of institutional development they offer is similar, or at the very least more so than either is with that of rational choice institutionalism. Even if state agents acted on their own to build the institutions of the welfare state—the most reductive possible reading of the statist literature—they still did so in active conflict with those who wished to stem the growth of the state: presumably, the agents of capital. The statists’ story is one of dynamic political contestation, and as I have shown, its proponents explain disparate welfare state development by the differential strength of bureaucratic actors to engage in such contestation. This argument is reconcilable with an approach emphasizing the role of working class mobilization—different interest groups can and do work together to achieve common goals—but far less so with the rational choice view that welfare state institutions are established as stable, long-term equilibria.

The penultimate version of historical intuitionalism considered here is less one of a particular historical antecedent than a general process: the role of path dependence. In his analysis on welfare state retrenchment, Pierson argues that social policies are subject to a ‘ratcheting’ effect of continuously increasing expenditures, and are difficult to eliminate once they develop a constituency of financial beneficiaries.18 This is particularly true of old age pensions, as retired voters are among the most likely to exercise the franchise. Huber, Stephens, and Ray adopt a power resource approach on the whole, but similarly argue that because many welfare state programs benefit voters outside the core base of the center-left, political debates over

retrenchment are less aggressively contested than those surrounding expansion. This approach has come under fire from Crouch and Farrell, who deem it a form of “institutional determinism,” and claim that it ignores the fact that the initial establishment of welfare state institutions occurred as the result of prolonged political struggle. Welfare state longevity, then, is less the consequence of ‘path dependency’ than the deep roots of continued political consensus. Hacker critiques the path dependency theorists from a different angle, arguing that their narrow focus on budget expenditures ignores actual changes to social policy coverage in the U.S. He maintains that established social insurance programs have failed to respond to new emergent labor market risks outside of their coverage areas, and moreover, that those “mismatches should be seen as a direct outgrowth of political struggles over social policy.”

Among these divergent strands within the historical institutional literature, ones stands out as the most consequential: the school which emphasizes working class mobilization, through organized labor or the political Left, as an explanatory variable for the development of welfare states. This approach is descriptive of the work of Korpi; Hicks and Swank; Rueschemeyer, Huber, and Stephens; and (as I describe in

---

more detail later) Esping-Andersen. Even at this level of specificity, there is significant variation within the literature. Hicks and Swank, for example, emphasize the role of labor leaders in welfare state formation and correlate increases in social welfare spending as a proportion of GDP with the incidence of industrial strike actions and general working-class protests. Others, notably Huber and Stephens, understand welfare state development as mediated through the central role played by left-leaning political parties. They also measure the strength of the welfare state in terms of government expenditures as a proportion of GDP—a rather limited measure, as Jensen points out—but find the percentage of cabinet members from such parties to be the most important explanatory variable. This approach resembles the ‘median voter theory’ famously proposed by Meltzer and Richard, which understands redistributive agendas as flowing from electoral preferences rather than interest group power or corporatist bargaining with labor unions. Irrespective of this quarrel over the means with which the Left exercises power, this literature concludes

---


that welfare states largely emerged as a result of political victory for the Left’s own redistributive ends. Welfare states are seen as a consequence of working class accumulation of power resources to force institutional change; hence, this argument has come to be known as “power resource theory.”

Power resource theory has strongly dominated scholarship within the historical institutionalist school. As Shalev noted in his 1983 review of the literature thus far, a welfare state might develop under non-social democratic conditions, “but its emergence is hastened, its growth is speeded, and its consequences for the class distribution of resources are arguably greater under social democracy.” Where scholars have emphasized other explanatory variables, from the role of religion to constitutional design, they have often done so as to explain how these factors aided or impeded working class mobilization. But though power resource theory has gained widespread credence in some circles, others have rejected its vision of welfare states originating through left-wing political struggle. As I will argue in short order, power resource theory is fundamentally at odds with the account offered by the rational choice institutionalists. The dispute is visible on its face, but even more so after considering the different theoretical roots these two literatures draw upon. In the following section, I offer a genealogy of the power resource theory of the welfare state, with the aim of illuminating this conflict further.

---

25 Capital-owners and employers are also theorized to hold ‘power resources,’ of course. But according to these scholars, welfare states develop as a consequence of the employment of power resources by the working class, and, in the case of generous welfare states, more effective employment than that of capital-owners and employers. For a discussion of the mechanics of distributional conflicts that employs power resource theory, see Walter Korpi, “Conflict and the Balance of Power,” Acta Sociologica 17, no. 2 (1974).

The Origins of Power Resource Theory

The opening pages of Karl Polanyi’s seminal 1944 economic history, *The Great Transformation*, outline its methodology in terms that could be used to describe this thesis. “Ours is not a historical work” *per se*, Polanyi wrote; “what we are searching for is not a convincing sequence of outstanding events, but an explanation of their trends in terms of human institutions. We shall feel free to dwell on scenes of the past with the sole object of throwing light on matters of the present.”

Polanyi’s treatise is relevant here in more than mere disciplinary approach. Through his analysis of the evolution of the Poor Laws in Great Britain, Polanyi challenged Adam Smith’s description of a natural human propensity to truck, barter, and exchange. For most of history, he postulated, individuals traded goods on terms of mutual reciprocity, and had to be actively (even coercively) shaped into ‘rational’ economic agents. But as market institutions embedded themselves within society, they were confronted with a counter-cyclical “double movement.” Market economies, Polanyi insisted, formed “a threat to the human and natural components of the social fabric…what else would one expect than an urge on the part of a great variety of people to press for some sort of protection?”

For the most part, Polanyi talked about “protection” in terms of antitrust policies, literal tariff protection of domestic industries, and the like. Within a decade, sociologist T.H. Marshall made explicit the connection between market-society conflict and welfare provisioning. For Marshall, the dialectical struggle was between

---

28 Ibid., 150.
capitalism, an inherently inequitable system of property relations, and democratic citizenship rights, which guarantee equal participation in a given community. Increasing relative inequality, alongside rapidly improving standards of living in the nineteenth century, profoundly altered the setting in which the progress of citizenship took place. Social integration spread from the sphere of sentiment and patriotism into that of material enjoyment. The components of a civilized and cultured life...were brought progressively within reach of the many, who were encouraged thereby to stretch out their hands towards those that still eluded their grasp.29

The distinction between this formulation and Polanyi’s is subtle but critical, as it informs the analytical lens later employed by the power resource theorists. While Polanyi described the societal reaction of the “double movement” as one seeking to protect the ‘losers’ of market transactions from suffering, Marshall described a reaction whose aim was the reduction of relative inequality in order to maintain a functional polity. Indeed, he argued, “class-abatement...is no longer merely an attempt to abate the obvious nuisance of destitution in the lowest ranks of society...social rights in their modern form imply an invasion of contract by status, [and] the subordination of market price to social justice.”30

Marshall’s brief 1950 essay, Citizenship and Social Class, proved to be enormously influential, but it lacked Polanyi’s historical grounding or a detailed description of how social rights are contested. Enter the ‘power resource theorists.’ Their writings take the position that “economic resources form the basis of power,”

30 Ibid., 153-54.
and that class divisions are often channeled through electoral participation.\textsuperscript{31} When the working class pools its labor power (in collective bargaining or in strength in numbers at the ballot box), the political Left is stronger, and the relatively downtrodden have more power to secure Marshallian social rights; this, they argue, is the primary causal explanation for the emergence of redistributive welfare states. The debt of this approach to the Polanyian “double movement” is clear, and even more apparent when considering who its proponents, like Walter Korpi, describe their theory in opposition to. Korpi criticizes Skocpol for assuming that political actors will implement major institutional change independent of pressure from social interest groups, and criticizes both ‘pluralist industrialism’ and neo-Marxism alike for a functionalist understanding of welfare states as greasing the wheels of industrial capitalism. One author in the pluralist industrialism school claims that that “the central false description of social insurance is that it is ‘redistributive’…a second major misperception of social insurance is that it was instituted in response to trade unions and the labor movement.”\textsuperscript{32} For Korpi and the power resource theorists, however, this is \textit{precisely} the purpose for and mechanism by which social insurance was created.

\textbf{The Three Worlds of Welfare Capitalism: \textit{A Power Resource Typology}}

These advances inform Gøsta Esping-Andersen’s text \textit{The Three Worlds of Welfare Capitalism}. I have allocated so much space to its theoretical underpinnings because it is perhaps the seminal text on welfare state development in the historical


institutionalism literature. Rather than comparing net social policy expenditure levels, Esping-Andersen offers an index of “de-commodification” as the primary metric for capturing welfare state diversity. The index is informed by the generosity of pension, sickness, and unemployment benefits—to what degree they replace (pre-tax) labor income—and their availability to the average citizen of a given population. To this end, the index incorporates the maximum length of time one can continue receiving social policy benefits, and the degree to which means-testing or past insurance contributions determine benefit levels. A “de-commodification” index of this sort speaks to an understanding of welfare states as the product of market-society conflict, for it implies that the more all-encompassing the welfare state, the less citizens have to sell their labor in order to enjoy a comfortable existence relative to the expected standard of living in a given society (c.f. Marshall). The aim of social policies, in this telling, is not to serve the logic of industrialism but to reify popular demands for social rights.

Though Esping-Andersen’s work is directly linked to Marshallian thought and power resource theory, he also makes some significant modifications to this framework. As proponents of power resource theory readily acknowledge, the strength of labor unions and social democratic parties cannot alone explain cross-national variance in welfare states. If nothing else, such a reductive approach offers little insight into a secondary question it necessarily provokes: how is one to explain cross-national variance in the power of the Left? In attempting to build out the power resource approach into a descriptive typology, Esping-Andersen thus expands his

palate of causal factors. He describes struggles for social rights as mediated through institutions like guilds and the Catholic Church, as well as through elected bodies. In addition to emphasizing pure class struggle through “social categories,” he highlights the importance of inter-class coalitions in sustaining the durability of welfare state institutions.34 Finally, he differentiates between cultural and political environments in which Left parties are more or less likely to be historically successful.

The core of Esping-Andersen’s text is an analysis of the titular “three worlds of welfare capitalism,” loosely based off a descriptive typology first introduced by Richard Titmuss. 35 Esping-Andersen sorts social policy regimes in developed countries into three categories: Liberal, Conservative, and Socialist, each reflecting progressively higher levels of de-commodification. Befitting his theoretical pedigree, Esping-Andersen finds that working class mobilization, measured through the duration that left-leaning parties spend in power, accounts for 43 percent of the variance in welfare state de-commodification.36 But much of his text is devoted to analyzing the different historical conditions under which the working class can (or cannot) successfully mobilize. In Liberal states, typified by Anglophone countries like Great Britain and the United States, dominant classical liberal ideology defined itself in opposition to statist social protection. Such measures were “equated with undesirable stratification outcomes: paternalism and elitism; dependency on the state;

34 Ibid., 18.
35 Ibid., 20; Richard M. Titmuss, Essays on ‘the Welfare State’ (London: Unwin University Books, 1963). Titmuss’ primary contribution was differentiating between ‘residual’ welfare states that seek to prevent extreme poverty (typified by the English Poor Laws), and ‘institutional’ ones whose aim is continual redistribution of resources.
[and] the perpetuation of pauperism.”\textsuperscript{37} Liberalism, where successful, entailed an ideological project to bury both class distinction and class solidarity in favor of a cult of individual opportunity. Poor-relief systems were largely set up to distribute means-tested benefits, with the aim of spurring individuals off the dole so they could maximize their inherent potential. Private insurance schemes and employment benefits were conceived of as rewards for highly-valued individuals in a competitive labor market. Perversely, Esping-Andersen, writes, efforts to eliminate class divisions in actuality produced a system of highly stratified social benefits, with “one group at the bottom primarily reliant on stigmatizing relief...[and] one privileged group capable of deriving its main welfare from the market.” There is social insurance in ‘Liberal’ countries, of course: for some workers, it comes in the form of health insurance worth many thousands of dollars. But for the average worker in that context, welfare policies are not seen as having a particularly de-commodifying effect on work.\textsuperscript{38}

Whereas in Esping-Andersen’s ‘Liberal’ ideal-typical model, social policies developed with the aim of making status divisions irrelevant, in the ‘Conservative’ model, social policies instead aimed to cement them. The possibility of class mobility under \textit{laissez faire} market economies—whether genuine or not—represented a threat to the power of the landed elite and Catholic Church. “Labor as a commodity,” writes Esping-Andersen, “clearly would tear asunder feudal and absolutist systems of labor

\textsuperscript{37} Ibid., 62.  
\textsuperscript{38} Ibid., 65.
Conservative leaders thus designed welfare policies that would substantially de-commodify labor without striving to eliminating social difference. Bismarck’s pioneering pension scheme was designed such that workers in different industries would receive benefits proportional to their social status, and the Catholic Church explicitly endorsed corporatist welfare policies in papal encyclicals such as *Rerum Novarum* (1891). Indeed, Esping-Andersen argues, Continental welfare regimes are exemplified by those that were enacted under German and Italian fascism, wherein social rights “were conditional upon appropriate loyalty and morality” to the state and reverence for existing power relations. In this model, it is the conservatives who guarantee social rights in order to cement power hierarchies and quell labor unrest. In countries where strong social democratic parties developed alongside conservative institutions—including Austria, Belgium, and the Netherlands—the result was simply welfare policies with even greater de-commodifying effects.

The third and final model in the triptych, that of the ‘Socialist’ Nordic countries, exemplifies the historical success of the mechanism of institutional change proposed by power resource theorists. Esping-Andersen proposes that like the Liberal countries, the Socialist countries have a legacy of opposition to top-down authoritarian rule. Yet the historical paths of the two models—and the extent to which they de-commodify labor—bifurcated depending on whether social democratic parties successfully took power. In Liberal contexts like the United States, labor

---

39 Ibid., 39.  
40 Ibid., 61.  
41 Ibid., 40.  
42 Ibid., 53.  
43 Ibid.
unions often focused on collective bargaining advancements and securing the most generous social benefits for their individual members. Indeed, the American Federation of Labor (AFL) originally opposed federal social insurance on the grounds that it would encroach upon its unions’ fiefdom in securing benefits for their members. In contrast, labor activists in the Socialist model perceived different obstacles in their path to power: the need to stymie a potentially reactionary lumpenproletariat, as well as to ensure the durability of social transfers by aligning them with interests of white collar workers. The result was a national program of welfare benefits commensurate with “middle-class expectations,” and a high level of de-commodification. Whereas organized labor in Anglo-American countries to some extent embraced the possibilities of liberalism—to the best workers accrue the best benefits—in Nordic countries the elimination of class hierarchies was a springboard to broader social solidarity.

Esping-Andersen’s historical analysis is not based upon a single variable: there is no identical correspondence between working class strength and welfare state de-commodification. But at its core, his thesis is clearly derived from power resource theory. Esping-Andersen differentiates between political and ideological contexts by examining how effective they are in deflecting the demands of labor. His account of Conservative welfare state development is still one of social protection demands spurred by economic change, merely demands appropriated by powerful entrenched actors and modified for their own ends. In the Liberal context, Esping-Andersen

argues, trade unions’ non-solidaristic policies prevented them from sustaining political power in the way that their Nordic counterparts were able to. That those unions exercised power on behalf of a relatively small group of skilled craftspeople does not refute the power resource theory, but merely exemplifies the failure of the broader working class to mobilize its power resources. The overarching narrative Esping-Andersen offers remains one of social conflict: he makes no claim that de-commodifying welfare policies emerged because they improve systems of industrial production. But this position is not descriptive of the literature as a whole. The next section turns to a group of authors offering a very different basis by which to compare disparate welfare state development, bolstered, in turn, by a very different theoretical genealogy.

*The Roots of Rational Choice Scholarship*

In contrast to the Polanyian theory of market-society conflict underlying the historical institutionalist literature, ‘rational choice intuitionalism’—somewhat surprisingly—is indebted to mid-twentieth century work on comparative industrial policy. Specifically, it has roots in a wide-ranging project funded by the Ford Foundation beginning in 1952, entitled the ‘Inter-University Study of Labour Problems in Economic Development.’ The central achievement of this group (comprised primarily of labor economists) was outlining a theory of institutional convergence among developed nations based on their shared underlying “logic of industrialism.” For Clark Kerr and his colleagues, industrial development had four

---

major consequences: it required (1) rapid technological progress, (2) urbanization, a 
(3) “wide range of professions and skills” represented in the labor force, and (4) a 
“consensus’ which relates individuals and groups to each other and provides a 
common body of ideas, beliefs and value judgments.” These requirements of 
industrialization necessitated, in turn, the structural presence of welfare state 
institutions in all developed countries. Kerr et al. elaborate:

There is general recognition that neither the individual nor his family should 
assume the major responsibility for the hazards involved in being a permanent 
member of the industrial working force...In the logic of industrialization, the 
responsibility for guaranteeing the minimum welfare and security of industrial 
man rests in large measure upon his managers and his government. This 
completes the severance of his dependence, both materially and emotionally, 
on kinship and family ties.

The convergence theorists argued that welfare states developed in order to 
facilitate individuals’ transition from small tight-knit communities to large impersonal 
one. They saw government social spending as a replacement for the support provided 
by kinship and family networks. But this theory should be strongly contrasted to the 
historical institutionalist account of social protection. Unlike T.H. Marshall, the 
convergence theorists did not see rising inequality as the impetus for state social 
spending. In a comparative study of capitalist and communist economies, Pryor 
showed that social expenditure levels were closely correlated to a state’s level of 
economic development, and not whether property was owned privately or

48 *Industrialism and Industrial Man: The Problems of Labor and Management in Economic Growth* 
collectively. And the logic of industrialism they hypothesized—or “technological imperative,” as Form re-conceptualized it—does not necessitate welfare state spending because of citizens’ demands for social rights, or industrial agitation by organized labor. Indeed, Kerr et al. claimed that

Labour organisations...are essentially reflections of the societies in which they develop. The universal responses of workers to industrialisation, and the nature of expressions of their protest, are increasingly moulded to conform and contribute to the strategy of the industrialising elites.

In a book published the same year, Ross and Hartman argued that economic development produced the “withering of the strike,” as organized labor gradually became a constituent group supporting a unified logic of industrialization. On the whole, the convergence theorists’ tale is a highly structural one—a single shared imperative for all industrialized nations!—but to the extent that they analyze individual agency, it is by examining the role of ‘modernizing elites,’ and particularly those of the new managerial class, in developing the labor market conditions necessary for a successful industrial society. A theory of class conflict this is not.

Though shedding some of the overarching framework of convergence, economic sociologists in the 1970s and 1980s drew upon Kerr et al.’s analysis in emphasizing welfare state spending as the consequence of economic growth. To this

insight Wilensky and Pampel and Williamson contributed their finding that the degree of public old-age pension expenditures in a given country strongly correlates with its demographic structure.\textsuperscript{54} They hypothesized this correlation as resulting from older citizens exercising the franchise, but contended that class variables have little to no statistical significance on expenditures. Wilensky also moved from the convergence theorists’ structural view towards an understanding that specific institutional context informs welfare state development. For example, “the larger the percent of the labor force who have had a taste of self-employment,” he wrote, “the greater the economic individualism and concomitant resistance to the welfare state.”\textsuperscript{55} More generally, Wilensky argued that individualist or collectivist cultural values inform a community’s response to the ‘technological imperative’ posed by industrialization. Imbued individualist values—not just among the economic elite, but the working class, as well—were found partially responsible for meager welfare state development in the United States.\textsuperscript{56}

In the subsequent decade, scholars of comparative industrial policy actively abandoned convergence theory, and combined earlier insights about the “logic of industrialism” with the understanding that successful production regimes could emerge under different institutional frameworks. Kitschelt et al. attribute this historiographical shift to growing evidence that the post-war consensus in the U.S. and Western Europe had fragmented:

\textsuperscript{55} Wilensky, \textit{The Welfare State and Equality}, 61.
\textsuperscript{56} Ibid., 28-39.
Since leaving the “golden age” of sustained economic growth in the early 1970s, no pattern of democratic capitalism appears to have found a niche in which it has come to rest around a stable set of democratic class compromises similar to the divergent but relatively stable “postwar settlements”…

To this analysis, I would add the experience of the collapse of Communism in Eastern Europe, which discredited any lingering views that the United States and Soviet Union were both highly productive societies converging upon shared pluralist industrial institutions. Regardless of the underlying cause, researchers now needed to acknowledge the substantive institutional variations between different national economies and, moreover, develop a framework that explained how they could operate in a global context simultaneously.

The explanation the industrial theorists came up with drew heavily upon the thought of classical economist David Ricardo, and they proclaimed it a theory of comparative institutional advantage. In addition to different factor endowments of land, labor, and capital, they argue, countries rely upon different systems of industrial relations, corporate finance, educational pipelines, and coordination (or lack thereof) between firms. “Competitive advantage is created and sustained through a highly localized process,” according to one influential treatment in this literature, and “differences in national economic structures, values, cultures, institutions and histories contribute profoundly to competitive success.” The evolution away from the


58 For a relatively late—but highly influential—argument that productivity growth in communist countries mirrored that of other industrialized states, see William J. Baumol, “Productivity Growth, Convergence, and Welfare: What the Long-Run Data Show,” The American Economic Review 76, no. 5 (1986). Baumol used data extending only to 1979.

convergence thesis of the 1960s is striking. Even while writing in a period of increasing labor and capital mobility, this line of scholarship explicitly rejects the idea that globalization will lessen differences in cross-national political economies. Porter doubles down on this point: “While globalization of competition might appear to make the nation less important, instead it seems to make it more so…the home nation takes on growing significance because it is the source of the skills and technology that underpin competitive advantage.” But though it rejects the idea of convergence, the comparative institutional advantage literature still conceives of institutional development as resulting from an intrinsic ‘logic of industrialism.’ It has simply come to the conclusion that there are multiple possible institutional configurations resulting from multiple different ‘logics.’ So although the implications of the literature with respect to institutional diversity are very different from that of its forbearers—it postulates multiple institutional equilibria rather than convergence—the underlying functionalist understanding of institutions is quite similar. Having traced this lineage, it is now time to explore the comparative institutional advantage literature in more depth. Doing so will reveal why this literature is often called one of ‘rational choice institutionalism,’ as well as its resultant view of welfare state development.

**Varieties of Capitalism: A Rational Choice Typology**

Within the comparative political economy literature, Peter A. Hall and David Soskice’s *Varieties of Capitalism* framework has become perhaps the most favored way

---

60 Ibid.
of examining cross-national variation. At its core, Hall and Soskice argue, theirs is a firm-centric view of national economies which sees companies as rational actors “seeking to develop and exploit core competencies or dynamic capabilities…for developing, producing, and distributing goods and services profitably.” Firms have to “resolve coordination problems” with respect to labor relations, work training, corporate governance, and “inter-firm relations,” and tend to do so through one of two different institutional configurations: those of Liberal Market Economies (LMEs) and Coordinated Market Economies (CMEs).\(^6\) Though the coordination problems speak to very different challenges of production—how to properly train workers or secure corporate financing, for example—Hall and Soskice note that countries tend to establish clustered solutions because of institutional complementarities, defined as occurring when “the presence (or efficiency) of one [institution] increases the returns from (or efficiency) of the other.”\(^6\) Hence their framework of two distinct institutional models of capitalism, rather than a menu of different solutions to a number of different coordination problems.

The reader will notice a lack of discussion of the influence of organized labor, state actors, or unique historical peculiarities in the discussion thus far. Their absence is deliberate: Hall and Soskice’s approach is firm-centric not only in seeing institutions as resulting from the need to solve corporate coordination problems (cf. the ‘logic of industrialism’), but also in seeing firms themselves as agents of

---


\(^6\) Ibid., 17.
institutional change. In fairness, they distance themselves from the work of Oliver Williamson and others who, in Hall and Soskice’s words, “assume that the core institutional structurers of the economy, whether markets, hierarchies or networks, are erected by firms seeking the most efficient institutions for performing certain tasks.” Sometimes, they argue, regulatory actions, disputes among firms, and the need to build political coalitions entail that firm “strategy follows [institutional] structure,” rather than vice versa. But with respect to how social policies develop, the processes they outline gravitate towards the idea that institutions coalesce around the productive requirements of firms. Theirs is, few would dispute, a theory of rational choice institutionalism, and it is plain in this telling who forms society’s key rational agents.

Before honing in on the welfare state subsection of the Varieties of Capitalism literature, however, it is worth outlining the “varieties” it describes in a bit more detail. The Liberal Market Economy model, identified primarily with Anglophone states such as Australia, Canada, New Zealand, the U.K., and the U.S., features equity-based corporate finance systems that urge maximization of shareholder value. Labor markets are “highly fluid,” without centralized wage bargaining, works council-based ‘codetermination,’ or strong vocational training. Inter-firm relationships, in turn, are governed by “standard market relationships and enforceable formal

---


contracts,” rather than coordination through conglomerate structures, and are often accompanied by vigorous government antitrust enforcement.65 Heuristically, it can be claimed that firms in LMEs solve coordination problems through market mechanisms. For Hall and Soskice, there are corresponding benefits to such an institutional structure:  

High rates of labor mobility mean that companies interested in developing an entire new product line can hire in personnel with the requisite expertise, knowing they can release them if the project proves unprofitable...Inter-firm relations based primarily on markets enhance the capabilities of firms to buy other companies, to poach their personnel, and to license new products—all means of acquiring new technologies, quickly.66

LMEs, in sum, position firms with comparative institutional advantage by creating the conditions for rapid innovation in production. Coordinated Market Economies, on the other hand, garner comparative institutional advantage by perfecting production processes. In contrast to the atomized corporate structure typical of the LME, CMEs solve coordination problems through dense interconnectivity. The Japanese keiretsu conglomerate system may be taken as an extreme example, wherein a wide variety of industrial firms are concentrated under a single corporate umbrella, resulting in more informal information-sharing and streamlined vertical supply chains. Rather than equity markets, corporate funding largely stems from keiretsu-

65 Hall and Soskice, “An Introduction to Varieties of Capitalism,” 30. Note that in the United States, whose political economy featured strict anti-monopoly enforcement in the first half of the twentieth century, the number of significant antitrust cases brought by federal regulators has plummeted in recent decades. As a further aside, the decline of anti-monopoly enforcement provides a fascinating case study of the role played by ideas in institutional change: in this case, the influence of a group of Chicago school theorists who argued that industrial concentration should only be regulated if it resulted in an observable increase in the price to consumers of the primary goods produced by that industry. For the seminal statement of this school, see Robert H. Bork, The Antitrust Paradox (New York: Free Press, 1978). For further summary and a critique of this theory through an analysis of Amazon’s business practices, see Lina M. Khan, “Amazon’s Antitrust Paradox,” Yale Law Journal 126 (2016).

linked banks, and conglomerates take responsibility for technical worker training and long-term employment guarantees.\textsuperscript{67} These institutions of close coordination are best suited for “incremental innovation” and gradual reduction of production costs.\textsuperscript{68} According to Hall and Soskice, Japan, the Nordic states, and much of Continental Europe are all identifiable as CMEs, with France and the Southern European states in “more ambiguous positions.”\textsuperscript{69}

The argument that these different capitalistic models advantage different kinds of industrial production has significant evidence to support it. Using European Patent Office data, Hall and Soskice show that German firms generate far more innovations in technically complex industrial sectors such as nuclear and civil engineering, while American firms are more successful in rapidly evolving sectors such as information technology and semiconductor production.\textsuperscript{70} According to their theory, systems of corporate finance and industrial organization are key to the creation of comparative institutional advantage. But perhaps equally important are the effects of social policies and, in turn, their effects on the character of national labor markets. The differing ‘logics of industrialism’ of LMEs and CMEs dictate very different varieties of welfare states.

\textsuperscript{67} Correspondingly, Japanese firms are frequently able to get loans from deposit-taking banks on highly advantageous terms. There is some evidence that excessive internalization of corporate debt by keiretsu-linked firms was a contributor to the deep recession experienced in Japan during the early 1990s. Others claim that fiscal crises allow bank executives to take over and restructure the firms within a conglomerate. See Michael R. King, “Who Triggered the Asian Financial Crisis?,” \textit{Review of International Political Economy} 8, no. 3 (2001); Erik Berglöf and Enrico Perotti, “The Governance Structure of the Japanese Financial Keiretsu,” \textit{Journal of Financial Economics} 36, no. 2 (1994).

\textsuperscript{68} Hall and Soskice, “An Introduction to Varieties of Capitalism,” 39.

\textsuperscript{69} Ibid., 21.

\textsuperscript{70} Ibid., 40-41.
Varieties of Capitalism and Welfare States

In the same volume as the “Varieties of Capitalism” statement described above, Estévez-Abe, Iversen, and Soskice describe welfare states as a critical institutional component of CME production regimes—continuing the ‘logic of industrialism’ thread—because they allow for worker skill formation necessary for certain kinds of industrial production. The authors differentiate between general skills (like university degrees) and industry- and firm-specific ones. Befitting their position as rational choice institutionalists, the authors assume that “people calculate overall return to their educational/training investment before deciding to commit themselves...[and] refrain from investing in skills that have more uncertain future returns.”

Different levels of employment and unemployment protection (the degree of job security in the former case, the level of income replacement provided by unemployment benefits in the latter) beget different kinds of skill development. High levels of employment protection naturally make investing time and money to acquire firm-specific skills a less risky endeavor. High levels of unemployment protection encourage the development of industry-specific skills, because they give workers the income security to search for related work in the event that they are laid off. Neither kind of protection encourages workers to be as flexible as possible, and thus invest in general skills. Social protection programs, it is argued, have fundamental consequences for the character of production regimes:

Where there is a large pool of workers with advanced and highly portable skills, and where social protection is low, companies enjoy considerable flexibility in attracting new workers, laying off old ones, or starting new production lines. This flexibility allows for high responsiveness to new business opportunities...[while] economies with a combination of firm- and industry-specific skills...advantage companies that seek to develop deep competencies within established technologies, and to continuously upgrade and diversify existing product lines.72

According to this theory, firms do not always resist the development of the welfare state; in fact, there exist certain institutional environments wherein social protection enhances firms’ modes of production. In Liberal Market Economies, however, employment security is simply counterproductive to the prevailing institutional paradigm: hence, Estévez-Abe, Iversen, and Soskice would argue, the lack of strong welfare state protections in countries such as the United States. In their conclusion, the three authors explicitly reject Esping-Andersen’s claim that the optimal way of understanding welfare states is by how much they ‘de-commodify’ labor.73 On the contrary, they contend, social policies are most notable in the extent to which they commit workers to labor—and for a long period of time, to boot—by incentivizing human capital development specific to a given industry or firm.

Mares offers another account of welfare state formation based on the microfoundations of firm behavior. Like the authors described above, she claims that “social policies support the investments in skills made by employers,” and are “of particular importance to employers in coordinated market economies.”74 She pursues a game-theoretic analysis of the conditions under which firms are likely to support

73 Ibid., 180.
welfare benefits as measured by two different variables: the degree to which they distribute labor market risk, and the degree of control they allow to individual employers. Firms that rely heavily upon skilled workers are hypothesized to support firm-controlled contributory social insurance schemes—which allow for tight coupling between social policy benefits and employee “wage differentials”—over universalistic programs. With respect to the scope of social insurance, Mares argues that firms operating in risker industries, as well as larger firms, will prefer to spread risk over a wider section of the economy than will low-risk firms and small artisans. She supports this claim with historical evidence of the debate surrounding disability insurance in Germany in the 1880s: large firms with relatively high worker injury rates, particularly iron and steel manufacturers, advocated for “unitary pools of risk,” whereas smaller firms, and textile manufacturers in particular, rejected the idea of risk pools spanning multiple industries. Mares makes no claim that firms alone create the welfare state for their own needs, but rather that these microfoundations determine which kinds of firms are likely to enter into coalitions with trade unions to develop different kinds of social insurance. In line with Hall and Soskice’s foundational work, the welfare states determinants she describes—firms requiring specific versus general worker skills; small firms versus conglomerates—are very much linked to firms’ productive needs.

Though also writing within the rational choice literature, Iversen and Soskice seem to suggest that the impetus for social protection arises differently: not from

---

75 Ibid., 196.
76 Ibid., 204.
firms seeking to incentivize their workers to make particular skill investments, but by agitation by workers themselves. In their paper “An Asset Theory of Social Policy,” Iversen and Soskice reinterpret the Meltzer-Richard median voter model by postulating that workers seek both to protect themselves against the possibility of unemployment and to hedge the risk posed by acquiring specific, firm-level technical skills. They likewise theorize that women are likely to support social insurance programs that enable them to more easily exit the workforce for childrearing. Iversen and Soskice support their model with survey data documenting the policy preferences of workers of varying skill levels: high-skill workers do in fact tend to support stronger wage protection and unemployment schemes. They profess to show that those same workers tend to disfavor government spending on arts and the environment, implying that their preference for social policy spending must be the result of a material interest in skill protection rather than ideological support for state intervention in civic and economic affairs more generally. Though they decline to place their theory within a particular political context, or describe its historical realization, Iversen and Soskice imply that social policies develop because highly skilled workers—whether in conjunction with organized labor or not—demand them from elected officials.

A final text worth considering in this literature is Peter Swenson’s *Capitalists Against Markets*, which offers an account of welfare state development in the U.S. and Sweden explicitly at odds with the statist and power resource schools. Swenson

---

outlines three different corporate labor market strategies that he argues motivate employers to support corresponding social policies: “cartelism,” wherein social insurance schemes with high employer contribution rates can drive low wage competitor firms out of business; “segmentalism,” wherein supplementing high efficiency wages with social benefits improves productivity and reduces the need for managerial oversight; and “solidarism,” wherein universalistic social benefits allow employers to reduce labor costs by compressing wage differentials. Swenson places these motivations in historical context by showing how firms employing such strategies—the former two in different industries in the U.S., the latter largely in Sweden—actively lobbied national governments to implement social insurance programs.

In seeking to address the perceived neglect of firms in the prior literature, Swenson does not argue that firms act alone: historically, he claims, they often did so in coordination with organized labor, especially because some of the labor market strategies he describes lend themselves to cross-class coalitions. But his corporatist argument reveals a critical axiom common to the larger rational choice literature: that welfare state development is not best understood as the product of continual struggle—‘society against markets’—but a kind of evolution of social policies to interlock with existing institutional complementarities in a given national economy. Indeed, Swenson argues that all three labor market/welfare state combinations form “self-reinforcing…equilibria,” subject to cyclical patterns and exogenous shocks but

---

not internal assault by firms or workers themselves. Even more than the emphasis on labor versus capital as agents of institutional change, this is perhaps the greatest chasm within the existing scholarship on welfare state development.

**Conclusion**

The breadth of literature described here originates with a curio of institutional diversity: all post-industrial economies have welfare states, but they vary dramatically in function and generosity. How is one to explain the apparently structural reasons that these institutions have emerged more or less concurrently alongside their very different characteristics across different nation-states? A great deal of ink has already been spilled attempting to explain this paradox. Yet the resulting scholarship poses more questions still. For one thing, it has not coalesced around anything resembling a consensus. In seeking to explicate welfare state diversity, scholars have assumed different underlying goals of social policy, proposed different understandings of actors’ behavioral motivations, and emphasized altogether different agents as the driving forces behind historical change. On a broader level, the two major schools of thought even have differing conceptions of how institutions evolve (or not) over time. The theories of historical institutionalism and rational choice institutionalism, as applied to the welfare state, appear fundamentally contradictory. A new synthesis is clearly required.

At the same time, however, resolving the disagreements within the existing literature is not sufficient to provide a convincing comparative examination of global

---

79 Ibid., 37.
welfare states. The scholarship described in this chapter, the reader may well have found, is as exhausting in detail as it seems exhaustive in scope. It is easy to get bogged down in the minutiae which render each country’s welfare state slightly different from that of its neighbor. This is a trap which must be avoided. A single-minded focus on institutional diversity—classifying different welfare state configurations into categories, for example—can miss larger macro-historical trends common to many welfare states. The goal of examining welfare states’ historical determinants, after all, is to explain their configuration in the present moment. Likewise, the theories of institutional change described in this chapter are useful, to be sure, but mostly to the extent that they explain who or what holds influence over the development of social policies. The value of a comparative approach is to uncover whether those forces are specific to a particular context or more broadly applicable. In the next chapter, I combine the two literatures’ insights as to how welfare state change occurs, while also arguing that the resulting explanation is germane to many advanced political economies.
2 Toward a New Understanding of Welfare State Change

Introduction

The previous chapter outlined the two major schools of thought seeking to characterize welfare state diversity. Reductively, they can be thought of as emphasizing either labor or capital as agents of the construction of social policies, and understanding institutions as either the consequence of dialectical struggle, or as existing in stable configurations determined by structural optimality. The differences within this scholarship—the varieties of ‘Varieties’—are summarized in table 2.1. Yet many of the scholars writing in this field have elided these obvious disagreements or even proclaimed the literatures’ ultimate compatibility.¹ One of the tasks here is to confront these incongruities head-on, synthesizing where possible and picking sides where necessary. On the question of whether the primary function of the welfare state is to de-commodify workers’ labor power, for instance, I will concur with the historical institutionalists. But I shall also endeavor to move beyond the typological approach offered by both schools of thought, identifying welfare regimes within a singular historical framework and understanding diversity as subordinate to common motivators of institutional change.

Table 2.1 Summary of Welfare State Scholarship

<table>
<thead>
<tr>
<th>Core text</th>
<th>Historical Institutionalism</th>
<th>Rational Choice Institutionalism</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ideal types</td>
<td>The Three Worlds of Welfare Capitalism</td>
<td>Varieties of Capitalism</td>
</tr>
<tr>
<td>Liberal, Conservative, Socialist welfare states</td>
<td>Liberal Market Economies, Coordinated Market Economies</td>
<td></td>
</tr>
<tr>
<td>Function of welfare state</td>
<td>De-commodifying labor; social protection from risk</td>
<td>Incentivizing skill development (further commodifying labor); risk-pooling</td>
</tr>
<tr>
<td>Basis of theory</td>
<td>Power resource theory / working class mobilization</td>
<td>Microeconomic foundations of firm behavior; institutional comparative advantage</td>
</tr>
<tr>
<td>Characteristics of ideal types</td>
<td><strong>Liberal</strong>: dualized welfare states with greater benefits for high-income earners; residual benefits often means-tested; historical lack of strength/internal division on Left</td>
<td><strong>LME</strong>: relatively little social spending; fluid labor markets; decentralized industrial relations; unstructured educational pathways; non-conglomeration of firms; equity-based finance systems; fast-paced innovation</td>
</tr>
<tr>
<td>Conservative: welfare states structured around maintaining class divisions and staving off social unrest (often non-redistributive); historically built with support from Church and/or landed elite; structured around employment and male bread-winners</td>
<td><strong>CME</strong>: greater social spending; regulated labor markets; centralized collective bargaining; vocational or state-directed educational pathways; conglomeration or close linkages between firms; bank- or state-based finance systems; gradual innovation</td>
<td></td>
</tr>
<tr>
<td>Socialist: solidaristic and significantly redistributive welfare states; built by trade unions and social democratic parties</td>
<td><strong>Socialist</strong>: solidaristic and significantly redistributive welfare states; built by trade unions and social democratic parties</td>
<td></td>
</tr>
<tr>
<td>Theoretical origins</td>
<td>Dialectical reaction of society to market encroachment on social life</td>
<td>Modernization theory; structural logic of industrialism</td>
</tr>
<tr>
<td>Institutional change</td>
<td>Fluid struggle between labor and capital</td>
<td>Multiple stable equilibria oriented around self-affirming institutional complementarities</td>
</tr>
<tr>
<td>Prospects for post-industrialism</td>
<td>Resilience of welfare state depends on political strength of Left; some states ill-positioned for transition to service economy</td>
<td>Increasing trade ties reify institutional comparative advantage; where complementary, robust welfare states can survive</td>
</tr>
</tbody>
</table>

The discussion of the historical institutionalists and rational choice institutionalists’ historical antecedents in chapter 1 offers the building blocks for constructing a new framework. Moving Karl Polanyi’s analysis into the present, welfare states are hypothesized to face retrenchment pressures—that is, efforts to reduce benefits and restrict those who have access to them—from forces attempting to ‘dis-
embed’ social protections in order to liberalize labor markets. The core cause of this trend, I hypothesize, is a structural ‘logic of post-industrialism’ that recalls the ancestral work underlying the rational choice theorists. The hypothesis also nods at their work on the microeconomic foundations of firm behavior by identifying the motives of and mechanisms by which firms have pursued retrenchment. But the vision of institutional change offered here also makes reference to the historical institutionalist scholars. The logic of post-industrialism I attempt to define not only motivates firms to pursue retrenchment, but also increases their relative political and economic bargaining power to achieve this goal. The importance of organized labor—whether through trade unions or the political Left—is understood as a countervailing power that modifies the degree to which firms can engineer retrenchment. Critically, firms’ efforts to stymie organized labor power in general—aided by the effects of structural trends such as globalization and the changing nature of work—form a crucial way in which they have pursued welfare state retrenchment in particular.

A good deal of scholarship already exists on the concept of retrenchment, and there is little need for another meandering literature review.\(^2\) But it is worth clarifying what it means for the purposes of this thesis. Cuts to social spending are perhaps the most obvious form of retrenchment: the elimination of a budget line item is a highly

---

visible form of institutional change. But as this treatment understands the welfare state primarily as it comes to affect labor markets, retrenchment need not come in the form of reduced state expenditures, nor is this the optimal way to measure the changing quality of the welfare state. Dualization of benefit levels, or the introduction of new categories of workers ineligible for social insurance, are effectively forms of retrenchment that may not emerge in longitudinal studies of aggregate government welfare expenditures. Critically, expenditure-level analysis also misses the changing character and benefit levels of *private* social spending, which is often supported through tax subsidies (an invisible form of state spending) and forms a crucial component of the welfare states in ‘Liberal’ political economies.³ Even studies purporting to analyze private expenditure levels will not uncover reduction of coverage in a particular industry or increasing inequality of benefit levels. For the average worker, however, and her or his level of protection from labor market risk, these changes definitively constitute retrenchment.

This chapter concludes with a discussion of whether or not welfare states’ retrenchment across many national political economies means that they are ‘converging’ in institutional makeup; with some important caveats, I argue that it does. The parallel nature of what seems to be occurring with respect to social policy across advanced

---

countries demands a serious inquiry into the causes and mechanisms behind this global change. A focus on the common does not render the unique unimportant; if anything, it highlights the factors that have resulted in different welfare state designs in different countries. But plenty of scholarship has already been written attempting to identify institutional varieties, and to adopt this approach—diversity qua diversity—is in some sense to miss the forest for the trees. Globalization is often thought of as synonymous with cosmopolitanism and increasing cultural heterogeneity. In the realm of social policy, however, globalization has resulted in a reduction of institutional diversity.

*Imagining a New Synthesis*

Before developing a substantive thesis of how welfare states develop over time, it is necessary to decide what form this thesis ought to take. Both the historical and rational choice institutionalist approaches have explained cross-national differences in terms of typologies: Liberal, Conservative, and Socialist ideal types in *The Three Worlds of Welfare Capitalism* schemata, and Liberal and Coordinated Market Economies in the *Varieties of Capitalism* schemata. The forces underpinning these institutional ‘models’ sharply differ between the two frameworks, of course. The former offers ideal types based on distinct historical processes, while the latter outlines institutional configurations that motivate different firm behaviors. Even still, the analytical framing of each text is similar. In this chapter, I will reject the typology approach altogether in favor of an alternative methodology. The reasons for doing so are manifold: for one, the typologies in question are lacking in their stated task of categorizing institutional diversity. But more importantly, they offer accounts of institutions that are effectively
frozen in time, even while coupling them with historical analysis of how those institutions once were not and eventually came to be. Institutions are fluid, rather than static, entities, and I aim for an approach that differentiates welfare state regimes while acknowledging this fundamental feature.

Schelkle and Jackson and Deeg offer excellent summaries of the technical discrepancies of the Worlds and Varieties typologies. Both have faced issues with institutional configurations that do not neatly fit into their predetermined categories. Southern European states like Spain and Italy, though grouped by Esping-Andersen with Austria and France, are not well described as ‘Conservative’ welfare regimes. By the same token, statist political economies like those of France and Japan are hardly ‘Coordinated Market Economies’ in the sense that Germany or the Lowland states are. The welfare regime in Japan, which is almost entirely based on occupation benefits and features lower state social spending than virtually any other rich country—even the United States—is particularly anomalous. Most of the Eastern European states, though now OECD members, also do not fit neatly into the Worlds and Varieties

---

4 This is undoubtedly a focus of the historical institutionalists, if not the rational choice institutionalists.
typologies, not to mention the welfare regimes outside of Europe and North America. Even some of the existing ideal type classifications fail to hold water: one study found that six of Esping-Andersen’s eighteen cases (a full one-third) were “in a group inconsistent with type.”

Even discounting their theoretical differences, neither of the typologies discussed thus far achieve their stated purpose in classifying institutional diversity. One could solve this problem by expanding out the number of ideal types from two and three to seven, eight, and beyond, as some have done. But this is hardly a solution at all: the more one expands a typology, the less useful it is in identifying larger-cross national trends. Conversely, further specification also voids Weber’s original definition of an ideal type: a “methodological utopia [that] cannot be found empirically anywhere in reality.” Yet the larger issue with typologies is not methodological, but substantive: they give the heuristic impression of an extant set of institutional configurations that, by the very nature of academic scholarship, continue to be descriptively useful years

---

9 Esping-Andersen has rejected the idea that there exists a (Central-)Eastern European model, while Fenger differentiates not one but three distinct welfare state subgroups in that region. McMenamin offers this description of those countries’ social policies: “Most measures point in the direction of relatively generous welfare regimes which crowd out non-state methods of provision. However, their unemployment replacement rates and overall social transfers are fairly low...By far the most unusual aspect of their welfare system is the very high contribution rate of employers to social insurance.” H.J.M. Fenger, “Welfare Regimes in Central and Eastern Europe: Incorporating Post-Communist Countries in a Welfare Regime Typology,” Contemporary Issues and Ideas in Social Sciences 3, no. 2 (August 2007); Iain McMenamin, “Varieties of Capitalist Democracy: What Difference Does East-Central Europe Make?,” Journal of Public Policy 24, no. 3 (2004): 270.


11 For one effort to expand the Varieties of Capitalism typology, see Bob Hancké, Martin Rhodes, and Mark Thatcher, eds., Beyond Varieties of Capitalism: Conflict, Contradictions, and Complementarities in the European Economy (Oxford: Oxford University Press, 2007).

after publication. Indeed, Titmuss’ original distinction between residual and institutionalist welfare regimes dates from the 1950s, and Esping-Andersen’s typology—developed more than a quarter-century ago—is still accepted as canon in a range of sociological scholarship today. The result is a schematic model that is not only ahistorical but *unhistorical*, purporting to describe the antecedents of welfare state regimes, and by extension, a theory of institutional change, while neglecting to extend that logic into the present.

Both schools of thought discussed *aim* to offer a dynamic approach, of course: Esping-Andersen, for instance, dedicates a whole chapter to “Post-industrial employment trajectories.” Hall and Soskice’s claim to dynamism is anticipating firms’ response to exogenous “shocks that unsettle equilibria on which economic actors have been coordinating…with efforts to modify their practices so as to sustain competitive advantage.”\(^{13}\) But by virtue of their Ricardian understanding of comparative advantage, these changes are not understood to unsettle the bipolar framework of Liberal and Coordinated Market Economies, as though those two models will exist—perhaps in modified form—forever thereafter. This manner of thinking bears similarity to Pierson’s work on welfare state retrenchment, which describes social policies as creating constituent groups and path-dependent political logics that ensure their long-term survival.\(^{14}\) The possibility of large-scale change, such that institutions become indistinguishable from their previous iterations (or fade away altogether) is largely absent here. But this cannot describe the future evolution of such institutions, much

---

\(^{13}\) Hall and Soskice, “An Introduction to Varieties of Capitalism,” 62-63.

\(^{14}\) Pierson, *Dismantling the Welfare State*
less the welfare state: after all, how else did those institutions emerge in the first place but by dramatically (if gradually) upending the status quo ante?

I therefore aim not to offer an updated typology of welfare states, capturing the essence of institutional diversity in 2018, but to build upon a larger model of institutional change that identifies welfare states’ orientation in the present moment. Wolfgang Streeck has offered the clearest statement of this sort of program, positing that institutional “systems” can be understood only as “merely moments in continuous processes of change,” spurred by the “entropic tendencies in capitalism that...elicit continuous efforts at social reconstruction.”

As will become clear later in this treatment, I shall part ways with Streeck on his view that welfare regimes are not in fact ‘converging.’ But Streeck’s warning of the inherent myopia of typologies is astute, and worth quoting at length:

> When the organized, nonliberal capitalism of the postwar era will finally be gone—which it likely already is—there will always be enough differences between countries, produced by time lags and tradition, for institutional theorists and policy researchers to make comparisons, suggest lesson-drawing, find path dependency and study hybridization. In fact, so many differences will remain that studying them close up will keep analysts busy enough to overlook the big commonality that lies behind the differences: the retreat in contemporary capitalism of institutions imposing and enforcing collective public obligations on economic actors, in favor of voluntary, privatized institutions of the Williamsonian kind.

---

16 Ibid., 170.
If one is to abandon the typological approach in favor of a structural historical one, then, what would such a framework look like? The next section attempts to answer this question.

The Basis for a ‘Triple Movement’

In addition to the literature on welfare state development itself, the preceding chapter attempted to catalogue the theoretical origins of the competing schools of thought. This exposed the deep roots of the conflict within the existing scholarship. (See table 2.1.) Moreover, those antecedents offer the basis upon which I will attempt to build a more dynamic thesis of how welfare states have developed over time. Polanyi’s vision of the ‘double movement’ is precisely the kind of historicized account of the conflict between the dueling demands of market expansion and social protection needed here; it merely has to be brought forward into the present. And the industrial theorists who informed the rational choice scholarship of Hall and Soskice, inter alia, provide the framework by which one might do so.

Writing in 1944, Polanyi’s description of a popular movement to shield individuals from the inequities of market capitalism—to ‘re-embed’ societies within markets—presciently predicted the post-war industrial consensus that was to follow. Though he is celebrated for his analysis of the Speenhamland system in England, the analysis is arguably better descriptive of the wage-compressing trente glorieuses experienced in Europe and the United States from the end of World War II up until the 1970s. The notion that this period of embedded social protection has faded is no repudiation of Polanyi, for he posited a dialectical struggle between markets and
societies: one wherein a given macro-historical trend necessarily begets its own successor.\textsuperscript{17} Welfare states today are in the third stage of a \emph{triple movement}, the removal of de-commodifying social protections in order to expand and liberalize labor markets.\textsuperscript{18} But though Polanyi might argue otherwise, I am not convinced that this trend towards liberalization is entirely the innate consequence of the political-economic system which preceded it: in Fichte’s terminology, that the post-war consensus endogenously generated the ‘antithesis’ through which this new ‘synthesis’ was born. Even if this were the case, demonstrating it to be true would prove a vast task far beyond the scope of this thesis. Instead, the forces underlying market liberalization can be seen as a consequence of the \emph{logic of post-industrialism}. Just as Kerr, Rostow, and others sought to define the universal pressures created by industrial production—and the corresponding institutions they would necessitate—one can analogously identify the pressures created by contemporary economic order. This is the source of the synthesis with the rational choice institutionalists: firms are the primary agents behind welfare

\textsuperscript{17} Streeck concurs on this count, arguing further, “today’s second Great Transformation of the state, which in important respects appears to be a direct reversal of Polanyi’s, would seem to amount not just to another wave of economic liberalization, but to a perhaps permanent dismantling of collective capacity to resist liberalization or bind it into and reconcile it with a nonliberal institutional context.” Ibid., 110, 251-52.

\textsuperscript{18} On this point, I side with the historical institutionalists who argue that welfare states not only de-commodify labor power, but that especially in so-called Socialist welfare states, de-commodification is their explicit purpose. In Conservative welfare states, benefits are not available to all equally but are rather targeted at male breadwinners according to their level of income. The underlying goal is preservation of social hierarchies, but a consequent effect is to de-commodify labor market participation in proportion to one’s previous standard of living (that is, for those in households with a wage earner eligible for social insurance). See the discussion of German unemployment insurance in chapter 4. De-commodification is not at all a normative goal in what Esping-Andersen deems Liberal welfare states, where ‘welfare to work’ rhetoric frequently abounds. Some social policy programs still have the practical effect of de-commodification, but their efficacy is currently being undermined through the addition of work requirements to eligibility criteria and the shifting of social insurance risk onto individual workers. Chapter 3 addresses de-commodification with respect to Liberal welfare states in more depth, as I argue that even private, employer-sponsored pensions can have an (albeit limited) de-commodifying effect.
state liberalization today, because the logic of post-industrialism dictates that liberalization is a rational course for them to pursue. The argument is less one of technological necessity—with an attendant fatalistic view of liberalization—but of a heightened motivation on the part of firms to advocate for the dismantling of de-commodifying institutions and to ease the political barriers to their removal. Capital always wishes to expand the limits of the market, and managers their relative bargaining power on the shop floor, but that is not to say that the push for each’s expansion is always uniform.19

The core of the argument is as follows. Following Polanyi and his intellectual descendants, I posit that at the most abstract level, political-economic institutions in capitalistic countries are formed through active contestation between those who wish to expand the role of markets in human social life and those who wish for protection from the social displacement this process entails. Very frequently, this struggle is mediated through attempts to harness the apparatus of the state for one project or the other. Capital-owners are usually the litigants in the former category, and while they sometimes attempt to force institutional change through their investment power alone—for example, by insisting that a sovereign state implement certain policies within its jurisdiction as a condition for purchasing its debt—they frequently do so through corporate firms in which they hold controlling investments, and whose profits form the basis of capitalistic accumulation. Workers’ ability to extract higher wages and benefits from their employers—heightened through social policies that lessen their

---

19 The discussion of financialization below will elucidate how the interests of capital-owners—the shareholders of firms—have become the key constituency motivating firm behavior.
need to work and render them less vulnerable in negotiations—limits the opportunity for accumulation. The actual agents supporting market expansion, then, are very often amalgamations of firms through industry and employer associations. In the latter camp, trade unions and allied social democratic parties have historically been the most influential forces seeking to install institutions of social protection. In some economies, bargaining between these two groups is highly choreographed through corporatism; in others, contestation is more ad hoc and pluralistic. Simplifying to the utmost, the character of welfare state institutions depends on the relative strength of these two groups—or, the distribution of ‘power resources’ between them.

The long-running conflict between these two impulses has proceeded from the ‘satanic mill’ of industrialization (to use Polanyi’s term), to widespread efforts over the course of the nineteenth and twentieth centuries to protect individuals through social insurance and public assistance, to a reactionary project of removing social protections.

It is this third moment that defines the present situation. Firms are especially motivated to pursue such changes because of the logic of post-industrialism, which not only increases their relative bargaining power but also, given increasing global competition between firms, dictates the imperative of liberalizing labor markets in order to continue the process of accumulation apace. Towards this end, firms wish to lessen both the

---

20 Consumer and civil rights groups have also played historically important roles, though often with less successful organizing models. Trade unions have the advantage of multi-level engagement with their membership, in that they can use member dues both to advocate for higher compensation and better working conditions at the firm level, and to advocate for policies advantageous to workers at the industry or national level.

21 For a rich discussion of post-industrialism and crises of accumulation, see the writings of the French Regulation school, especially Michel Aglietta, *A Theory of Capitalist Regulation: The US Experience*, trans. David Fernbach (London: Verso, 1979). Note that I am not advancing an argument that capital accumulation would altogether collapse were it not for labor market liberalization that enabled further
de-commodifying effects of the welfare state on labor market participants and their own financial contributions to social insurance schemes. Cross-national diversity—the original entry-point of this inquiry—should be conceptualized as a product of unique histories, constituencies, and institutions that differently mediate this pressure within the broader paradigm. There is now have cause to examine both the motivating logic of this trend, and the basis by which firms have exercised it.

*The Logic of Post-Industrialism*

Any definition of the ‘logic of post-industrialism’ must begin with the historical caesura of the early 1970s. In April 1971, President Richard Nixon imposed wage and price controls across the United States and unilaterally canceled the convertibility of the U.S. dollar into gold. March 1973 witnessed the formal collapse of the Bretton Woods system of fixed-rate currency convertibility, resulting in free-floating exchange rates between the world’s major currencies. When they elapsed after 90 days, the Nixon price controls resulted in spiraling commodity prices, and October 1973 brought the first of two major oil shocks following Arab countries’ announcement of a petroleum embargo. These twin developments squeezed major industrial firms, both increasing the costs of production and forcing them to hedge themselves against foreign exchange extraction of value from labor (as some in the Regulation school might). The claim is that profit-squeezing as a result of globalization and secular stagnation has rather increased the natural propensity of firms to seek an expansion of their market power in employment relations, and that the logic of post-industrialism has simultaneously sharpened their tools by which to do so. Firms’ desires to suppress wages, after all, are not absolute. They may come into conflict with preferences for incentivizing workers to develop firm-specific skills: preferences which are often realized through offering wage premiums and employment protections. My claim is that the relative importance of maximizing market power as a (the) goal of industrial relations has increased, and that spurring welfare state retrenchment has offered one vehicle to firms by which to do this.
rate instability. More generally, the 1970s bore the economic malaise of ‘stagflation,’ combining high inflation and monetary instability with high unemployment and sluggish economic growth. As the decade progressed, these forces cemented the popular perception that advanced economies needed to implement dramatic market reforms. The Reagan/Thatcher ‘revolutions’ in the U.S. and Great Britain offered one such set of solutions, largely centered around deregulation. GDP growth in advanced economies has increased in subsequent years, though still consistently underperforming the International Monetary Fund’s annual forecasts. But much as the trauma of hyperinflation still guides German monetary policy nearly a century after the Weimar crises, the specter of secular stagnation still informs the logic of post-industrialism.

Second, post-industrialism is characterized by increasing financialization of global economies, defined by Krippner as “the tendency for profit making in the economy to occur increasingly through financial channels rather than through productive activities” such as the extraction, manufacturing, and trading of physical goods. In the immediate postwar decades, financial sector profits comprised approximately 10 to 15 percent of total corporate profits in the U.S.; by 2001, they

---

23 For a representative example, see David Gordon Smith, “High Inflation Causes Societies to Disintegrate,” Der Spiegel, March 11, 2012. Though Germany no longer has its own currency, the analogy still hold: European monetary policy, for all intents and purposes, is effectively German monetary policy.
24 Greta R. Krippner, Capitalizing on Crisis: The Political Origins of the Rise of Finance (Cambridge, MA: Harvard University Press, 2011). Krippner argues that in the U.S. context, financialization arose as a result of “social, fiscal, and legitimation crises” of the resource-scarce 1970s. To ease access to credit, stabilize the economy, and pay for growing state expenditures that addressed these challenges, she argues, policymakers deregulated financial markets, switched to a ‘monetarist’ policy at the Federal Reserve, and encouraged significant foreign capital inflows. One main result of these policies, if unintentional, was the increasing importance of the financial sector to the U.S. economy.
exceeded 40 percent. This transformation has been accompanied by the ascension of ‘maximizing shareholder value’—returning wealth to the owners of a firm—as the primary organizing principle of corporate behavior. In the 1950s and 1960s, the predominating “portfolio theory of the firm” encouraged the creation of large conglomerates that diversified risk to investors by spreading production across multiple unrelated industries. General Electric is one of the few remaining American firms of this model, though it too is in the process of spinning off its many different business units. But the wave of corporate mergers and acquisitions in the 1980s, the rise of institutional investors as a major force in financial markets, and the increasing compensation of corporate executives through stock options all motivated firms to prioritize growth in equity values over risk diversification. The resulting tendency to maximize short-term profits, often to compensate shareholders through dividends, imposes a very different set of incentives on firms. One of them is to break up

25 Ibid., 28.
26 Ibid., 8.
27 The example of General Electric is a useful illustration of both the increasing concentration of corporate profits in finance and the move away from corporate conglomerates. From a company founded by Thomas Edison and still known to many as a manufacturer of lightbulbs, the company’s GE Capital unit, involved in a variety of financial activities from mortgages to commercial lending to private equity investments, grew to be larger than any of the firm’s core industrial units. Prior to the 2008 financial crisis, GE Capital accounted for 42 percent of the firm’s total revenue. In 2015, the company announced plans to spin off the vast majority of GE Capital’s assets (which were ultimately sold to financial firms such as Wells Fargo and Goldman Sachs), and refocus the unit on financing investments in its other subsidiaries, such as aviation. The move was intended to rejuvenate the company’s lagging stock price, in part because the sale of assets would allow the company to compensate shareholders to the tune of $40 billion in dividends and $50 billion in stock buybacks (increasing the value of each individual share) over a three-year period. Michael J. de la Merced and Andrew Ross Sorkin, “G.E. To Retreat from Finance in Post-Crisis Reorganization,” New York Times, April 10, 2015.
28 Krippner, Capitalizing on Crisis, 8-9.
conglomerates into more streamlined, singularly-focused entities. Another key priority is the reduction of labor costs.

Third, the logic of post-industrialism is inextricably linked with that of *globalization*. Removal of tariff barriers and technological advances with respect to containerization and information technology have resulted in greater competition among firms from all countries to find markets for their goods. By the same token, increasing capital mobility—especially since the 1990s, when the International Monetary Fund joined private investors in urging countries to liberalize their capital accounts—has given large firms the leeway to relocate productive operations across the globe in search of the most desirable political and institutional environments. Increasing labor mobility, like that required between European Union’s member states by their shared *acquis communautaire*, has likewise enabled this trend, arguably resulting in downward pressure on wages.

Fourth, the logic of post-industrialism is exemplified by the *changing nature of work* from repetitive manufacturing jobs to service-industry employment. This transition is at once technological and interlinked with the facets of post-industrialism described above, such as the increasing importance of finance in advanced economies and greater industrial competition from lower-income countries. Post-industrial service

---

29 Olivier Jeanne, “Capital Mobility and Regulation,” in *Global Economies in Extraordinary Times: Essays in Honor of John Williamson*, ed. C. Fred Bergsten and C. Randall Henning (New York: Columbia University Press, 2012). This trend is often thought of as flowing from a policy vision known as the “Washington Consensus” first articulated by economist John Williamson in 1989, and which the World Bank and U.S. Department of the Treasury also embraced. It insisted that countries reduce deficits, privatize state-owned enterprises, and generally deregulate financial markets as a condition for favorable international loan guarantees. Williamson claims that capital account liberalization was never a component of his initial recommendation.
work has received a great deal of scholarly attention; for the purposes of this treatment, its most important consequence is the resulting tendency towards labor market dualization. Indeed, service-industry work tends to cluster around bipolar levels of skill development, with some jobs, such as those in the hospitality industry, requiring little prior training and others, such as those in financial services, requiring a great deal. In 2017, the average wage of a worker with a college degree was nearly 50 percent higher than one with only a high school diploma, the highest that wage gap has ever been. The result is a large proportion of firms within a given national whose rational end is to eliminate social protections that grant workers a degree of leeway in employment negotiations: as labor is easily replaceable, low-skill employers will seek to increase the number of workers willing to take such positions at low wages, as well as to reduce their own payroll tax contributions. Indeed, the rational choice institutionalist scholars argue that under such conditions, firms will pursue social

---

31 Elise Gould, “The State of American Wages, 2017,” (Washington, DC: Economic Policy Institute (EPI), 2018), 19-26. As the report argues, the gap is not the result of a shortage of skilled workers—through a wage premium offered to college graduates—but instead changes to the global economy such as automation and de-unionization that have lowered the relative wages of unskilled workers.
32 This analysis is focused on welfare state benefits that relate to employment and have directly de-commodifying effects, such as unemployment insurance and old age pensions. Those types of benefits are the subjects of my case studies. Health insurance, which is often tied to employment in the United States, can prove an exception to this trend. Walmart, the largest low-wage employer in the U.S., for example, relies on Medicaid expenditures to supply health care to their employees, who would be otherwise unable to buy it for themselves. Walmart certainly has no direct aim to dismantle Medicaid or substantially curtail benefits. I would suggest this is because Walmart’s wages are already effectively at the zero-lower-bound and cannot be further reduced (indeed, a substantive proportion of their workers are paid the minimum legal wage), and, more importantly, because Medicaid is not funded by employer or payroll taxes.
policies of this very sort: my suggestion is merely that the underlying trend is far more universal than to the Liberal Market Economies to which they ascribe it.33

I have identified four elements of the ‘logic of post-industrialism’—secular stagnation, financialization, globalization, and the changing nature of work—that have particularly motivated firms to pursue welfare state retrenchment since the 1970s. The next task is to identify the specific mechanisms by which they do so. As will become clear, the changes underlying the logic of post-industrialism have had a reciprocal effect on firm behavior. By this, I mean that post-industrialism has simultaneously increased firms’ motivation to pursue welfare state retrenchment and increased their political and economic power to do so. It has likewise diminished the power of other groups—principally organized labor—to sustain current levels of social protection, much less expand them. In reference to the scholarship underlying rational choice institutionalism, this chapter has outlined the structural reasons why welfare state retrenchment has assumed such a prominent position on national political agendas. But I have tried hard not to import a functionalist view of retrenchment: that structural logic necessitates corresponding change. It is because of the tools that the logic of post-industrialism has granted industry, and more importantly, its success in employing them, that welfare states are undergoing retrenchment.

Firms in the Driver’s Seat

In this section, I postulate four main mechanisms by which firms have pursued welfare state change: lobbying, in its diverse forms, from campaign spending to the ‘war of ideas’; threatening capital flight; stymieing the power of organized labor and neglecting collective bargaining institutions; and constructing ‘de-democratizing edifices.’ These mechanisms are analytically distinct, but not mutually exclusive from one another: lobbying in particular serves as a kind of catch-all vehicle that firms may use in conjunction with another strategy (campaigning for a bill that would diminish labor union strength, for example). They are also means of pursuing retrenchment from different angles. While the first two mechanisms offer ways to dismantle welfare state policies head-on, the latter two are focused primarily on undercutting countervailing forces that might resist those efforts. All are material strategies that have been used in the service of retrenchment.

I. Lobbying

Obviously enough, firms seek to make their mark on public policies through deep engagement in the political process. This can take many forms. Lobbying occurs most transparently through campaign contributions, wherein donors finance a candidate’s bid for (re)election based on perceived shared policy priorities, or an implicit quid pro quo to pursue the donor’s agenda once in office.\footnote{Campaign contributions can also be non-transparent if routed through a 501(c)(4) social welfare organization to a political action committee, a transfer which enables a great deal of donor anonymity. Though those organizations (so-called ‘Super PACs’) cannot coordinate directly with candidates for office, they are often run by candidates’ associates in direct support of their electoral bids.} The nexus between campaign contributions and legislative priorities will be so familiar to U.S. readers (and likely
others) that it hardly requires elaboration. The so-called ‘revolving door’ of the lobbying industry, wherein lawmakers or regulators support their patrons’ preferred policies only to later work for them in the private sector for very high levels of compensation, offers an even more material incentive for government agents to pursue business’ agenda. In addition to cash, firms (especially employer associations) also mobilize people for the task of lobbying, by flying in lawmakers’ constituents to press them on an issue or flooding regulators with comments on proposed regulations. These tactics, as the case studies will suggest, have undoubtedly been used for the cause of welfare state retrenchment.

Another way that firms have sought to reduce social protections is by funding a ‘war of ideas’ through intellectual work challenging the welfare state, usually on grounds of fiscal cost or inherent inefficacy. Charles Murray’s book Losing Ground (written while a fellow at the Manhattan Institute) is the best known of these efforts, but by no means the only case.\(^{35}\) Mark Blyth has shown that more than 40 percent of the Hoover Institution’s funding came from business foundations between 1979 and 1982, during which time the think tank produced work by Martin Andersen arguing “that not only was the welfare system a net drain on the economy, but also that the amount spent on welfare, if left in private hands, would have produced economic growth sufficient to obliterate the poverty that the welfare institutions were designed to alleviate.”\(^{36}\) Martin Feldstein, the director of the National Bureau of Economic

---


Research (NBER)—which received nearly half of its 1983 funding from Fortune 500 Companies—applied similar analysis to unemployment insurance, arguing that benefits “increase[d] the real wage artificially and hence lower[ed] productivity.”37

In 1987, the American Enterprise Institute (AEI) convened a “Working Seminar on Family and American Welfare Policy,” which culminated in the publication of a report entitled A Community of Self-Reliance. It argued that alleviation of poverty in the United States would require work requirements for welfare recipients, limits to how long individuals could receive benefits, and the devolution of welfare program administration to state governments. The report was influential in part because the panel convened not only conservative intellectuals like Murray but also established Washington liberals like Robert Reischauer and Alice Rivlin (the first director of the Congressional Budget Office, and a fierce critic of Ronald Reagan’s economic policies during his administration), all of whom unanimously agreed to the final document. Indeed, all three of those policy recommendations were ultimately incorporated into the welfare legislation signed by President Clinton in 1996, and according to a key Republican staffer behind the bill’s drafting, this was no mere coincidence.38 AEI’s success in marshalling a nonpartisan ‘consensus’ around welfare reform speaks to how industry-aligned groups have pursued policy change through

37 Ibid., 158.
“cultural capture.”\textsuperscript{39} The war of ideas is fought not merely on the merits of policy proposals, but by the level of prestige those proposals confer. Lobbying (around the federal government, at least) involves political strategies centered around a very particular set of individuals and institutions within Washington, D.C. But firms also have tools for retrenchment involving the entirety of the global economy.

\textit{II. Capital Flight}

By virtue of the globalized logic of post-industrialism, firms are most incentivized to pursue welfare state retrenchment when they face the greatest trade competition from abroad. By the same measure, they are likewise best equipped to force policy changes in environments most open to international trade. Where capital mobility is highest—exemplified by outward foreign direct investment (FDI) flows in Sweden in the 1980s, and in Germany in the 1990s—investment capital seeks profit abroad, and domestic policymakers are forced to create the conditions to re-route investments back to local industries.\textsuperscript{40} Rodrik, for example, has shown that taxes are lower on capital and higher on labor in more ‘trade-open’ countries.\textsuperscript{41}

Swank addresses the question of capital flight explicitly, and agrees in principle that international capital mobility (especially when coupled with fiscal stress) places

\textsuperscript{39} For an exegesis of that concept, see James Kwak, “Cultural Capture and the Financial Crisis,” in \textit{Preventing Regulatory Capture: Special Interest Influence and How to Limit It}, ed. Daniel Carpenter and David A. Moss (New York: Cambridge University Press, 2014), as well as that volume more generally.
\textsuperscript{41} Dani Rodrik, \textit{Has Globalization Gone Too Far?} (Washington, DC: Peterson Institute for International Economics, 1997). Note that Rodrik also claims that trade-openness is associated with \textit{higher} levels of government expenditure on social protections, as measured by social insurance spending. See my critique of expenditure-level analysis above.
strong pressure on welfare state regimes. The core of his argument “is that political institutions determine the degree to which the economic and political logics of globalization contribute to welfare state retrenchment.” Unique domestic veto points, bicameralism, proportional versus majoritarian legislative bodies, and varying institutional capacities on the part of constituent groups like organized labor all modify this universal pressure in different countries. On this basis, Swank rejects a “systematic” connection between capital mobility and retrenchment, but this portrayal is somewhat hasty. After all, the ability of some institutional configurations to resist the threat of capital flight does not mean that it is not present. Nor can those institutions be expected to stem the pressure for liberalization indefinitely. Whether in evaluating their country’s evolving capital account or in responding to a large firm’s explicit demands, policymakers continually seek to shape an institutional environment that will encourage investment within their jurisdiction. Trimming the welfare state is one way that they have sought to do so.

III. Changing Labor Relations

Efforts to weaken de-commodifying social protections need not come through a direct assault on the welfare state. Indeed, one of the primary ways firms have pursued this goal is through a proxy struggle with labor unions that were historically integral to welfare state development. As John Kenneth Galbraith argued, “private economic power is held in check by the countervailing power of those who are subject to it”: in

42 Swank, Global Capital, Political Institutions, and Policy Change in Developed Welfare States, 8.
43 Ibid., 277.
44 Ibid., 36.
the case of labor markets, workers and their representative associations.\textsuperscript{45} By undercutting unions’ strength as a countervailing power, firms increase their own monopoly bargaining power to unilaterally dictate wage and benefit levels. This market power extends both to labor negotiations specific to individual companies, and to pluralist negotiations between interest groups to determine public policies at the governmental level. Firms can pursue this strategy through advocacy for anti-union legislation; vociferous opposition to union organizing, elections, and contract demands; and collective bargaining tactics that devolve labor-management relations. This final path demands greater elaboration: by bargaining for ‘opt-out’ clauses to sectoral-wide agreements that allow for modifications at the firm level, or leveraging union seniority rules to introduce new categories of workers ineligible for certain kinds of benefits, firms can not only undermine trade union strength (in membership or financial resources), but unravel systems of industrial relations upon which some social insurance programs depend. Whether in bargaining over benefits on shop floors, or in debating policies on the floors of national legislatures, weaker trade unions translate to less worker voice, and quite often a lower level of social protection through the welfare state.

Firms’ efforts to lessen labor union power are greatly aided by the inherent logic of post-industrialism. Firms in the service sector, which accounts for an increasing proportion of employment in industrialized countries, tend to be more difficult for labor unions to organize than those in the manufacturing sector. Employment in those sectors is more transitory—in part because low-wage service sector work requires

relatively little job training—and workers therefore have little bargaining power to make demands of their employers. Advances in organizational management have also given firms the tools to outsource low-skill work from their core businesses through subcontractors, franchises, and temporary employment agencies. And weakened labor protections in industrialized countries have resulted in a downward spiral in union power: the fewer workers join unions, the more limited the unions’ resources are, and the less they are able to resist labor market liberalizations that further diminish their ranks. It is no accident that this process has frequently occurred concurrently with welfare state retrenchment.

IV. De-Democratization

Given that the logic of post-industrialism also exposes individuals to deleterious economic conditions—whether through outsourcing, automation, obsolesce of acquired skills, or the like—it could well be expected to result in a renewed popular push for social protection. Reactionary forces have stemmed this pressure in part through the construction of institutions that skirt or re-route democratic pressures. The archetypical example of this phenomenon is the European Union (EU), often described in popular commentary as facing a “democratic deficit.” This term is usually used in reference to the relative unaccountability of the rule-making European Commission to voters in the Union’s national polities. But perhaps even more significant is the degree to which the EU reflexively restricts domestic policy in its member states, and the

---

members of the European Monetary Union (Eurozone) in particular. The 1992 Treaty of Maastricht requires states to limit budget deficits to 3 percent of GDP per annum, and a later agreement further requires them to reduce structural deficits by a minimum of 0.5 percent per annum. Such rules plainly restrict the ability of national governments to implement counter-cyclical social policies: claims on unemployment benefits, for example, are likely to rise in economic downturns just as tax revenues are declining. In Europe, the generosity of national welfare states is in direct tension with supranational obligations.

The tendency to reduce social spending is not just a side effect of European efforts to create the structural conditions for a common currency, but indeed central to those efforts. In a highly prescient 1939 essay, “The Economic Conditions of Interstate Federalism,” F. A. Hayek concluded that “in a federation, certain economic powers, which are now generally wielded by the national states, could be exercised neither by the federation nor by the individual states…there would have to be less government all round if federation is to be practicable.”48 Because the creation of an interstate “single market” would necessitate the fiscal integration of a large number of heterogeneous communities,

Even where it is not simply a question of “regulating” (i.e., curbing) the progress of one group in order to protect another group from competition, the diversity of conditions and the different stages of economic development reached by the various parts of the federation will raise serious obstacles to federal legislation. Many forms of state interference, welcome in one stage of economic progress,

are regarded in another as a great impediment. *Even such legislation as the limitation of working hours or compulsory unemployment insurance,* or the protection of amenities, will be viewed in a different light in poor and in rich regions and may in the former actually harm and rouse violent opposition from the kind of people who in the richer regions demand it and profit from it. *Such legislation will, on the whole, have to be confined to the extent to which it can be applied locally without at the same time imposing any restrictions on mobility,* such as a law of settlements. 

In other words, to the extent that welfare state institutions de-commodify labor in a given jurisdiction, supra-national bodies will tend to reduce these protections in an effort to standardize labor market conditions across a single market. For Hayek, this was a desirable outcome and a reason to support interstate federalism: “the abrogation of national sovereignties and the creation of an effective international order of law,” he wrote, “is a necessary complement [to] and the logical consummation of the liberal program.”

Harmonization of European political economies around a diminished vision of the welfare state is more than a theoretical requirement of a supranational federation. It is an active project in which European firms have been intimately involved. In a 1991 essay, Streeck and Schmitter maintained that European Community-wide ‘peak organizations’ lobbying on behalf of large firms held outsized power in the supranational system—precluding the formation of a genuine ‘Euro-Corporatism’—as some 471 of the 654 lobbying organizations registered to the European Commission by 1985 represented industry or commerce. Those groups held “privileged access to

---

49 Hayek, “The Economic Conditions of Interstate Federalism,” 263.
50 Ibid., 269.
deliberations” held by the Commission and were integral to the establishment of “negative integration’ [of the Union] through preemption of national regulatory regimes without a simultaneous supranational restoration of regulatory capacity.”52 Streeck and Schmitter identify social rights as a key locus of this diminution, and a fundamental incongruity between the “modern European welfare state” and the European Community. They predict the former’s replacement with something resembling “a pre-New Deal liberal state.”53

The establishment of supra-national bodies like the European Union is just one manner by which popular pressures for social protection can be diverted. Domestic policy-making institutions—like the U.S. Federal Reserve, in the case of monetary policy—can be spun off as independent entities unbound by political constraints. Likewise, legislatures can tie their own hands through budgetary rules that restrict future decision-making.54 The U.S. Budget Control Act of 2011, for example, imposed automatic budget “sequestration” upon federal expenditures for the next several years, resulting in the defunding of long-term emergency unemployment benefits. The argument I offer here is that these ‘democracy-reducing’ institutions are the product of firms’ political advocacy, and form a way to put pressure on welfare states through budgetary obligations in place of a full-frontal assault. The underlying motive to dis-embed social protections remains the same.

52 Ibid., 137, 49.
53 Ibid., 152.
54 These efforts have intellectual roots in the ‘public choice theory’ of economists like James M. Buchanan.
V. Fiscal Pressures?

To review, the working hypothesis features four main vehicles by which firms are theorized to pursue welfare state retrenchment: lobbying, the threat of capital flight, an assault on labor unions and collective bargaining institutions, and the construction of ‘de-democratizing’ institutions. Conspicuously absent from this list is the notion that welfare states have faced retrenchment pressures because of rising fiscal costs associated with social programs. Indeed, a substantive proportion of the existing literature sees retrenchment as a consequence of budgetary considerations, rather than a desire on the part of firms to liberalize labor markets. This thesis is not mutually exclusive from the one offered here. The conditions fueling the budgetary ‘crises,’ for example, such as demographic shifts and higher claim levels on welfare benefits due to job dislocation, are in large part a consequence of the logic of post-industrialism outlined above. But to the extent that there is human agency in this explanation, it is assumed to be on the part of fiscally-minded bureaucrats rather than managers and capital-owners.

I might simply gesture at this alternative thesis with the understanding that social policy changes are complex and multi-causal, necessarily involving different constituent groups with different ultimate ends. But without endeavoring to disprove the budgetary explanation altogether, it is worth considering the extent to which fiscal challenges are used instrumentally in pursuit of ulterior aims of business groups.

55 See Hugh Heclo, Modern Social Politics in Britain and Sweden: From Relief to Income Maintenance, Yale Studies in Political Science (New Haven, CT: Yale University Press, 1974). Streeck argues that this took place in Germany as the state absorbed the costs of compensating surplus labor, rendered obsolete by globalization and technological change, until the point of fiscal ‘exhaustion’ in the 1990s. Streeck, Re-Forming Capitalism: Institutional Change in the German Political Economy, 64.
Around the same time as this chapter was written, for example, the U.S. Congress enacted a major piece of tax legislation whose central feature was the reduction of the corporate tax rate from 35 to 21 percent. The Congressional Budget Office estimated that the legislation will add $1.5 trillion to federal deficits over a ten-year period, or $1.8 trillion with additional debt service factored in.\(^{56}\) Yet just as the final details of the legislation were being hammered out by a conference committee, House Speaker Paul Ryan (R-WI) insisted in a radio talk show interview:

> We’re going to have to get back next year at entitlement reform, which is how you tackle the debt and the deficit...Frankly, it’s the health care entitlements that are the big drivers of our debt, so we spend more time on the health care entitlements—because that’s really where the problem lies, fiscally speaking.\(^ {57}\)

Fiscal stress does present a real challenge to the viability of welfare states, but it can just as easily appear as a Trojan horse.

**Divergent Views of Convergence**

In place of the typological descriptions of welfare state diversity described in chapter 1, this work understands different social policy regimes as anchored within a larger macro-historical movement. I have hypothesized widespread structural conditions motivating firms to support welfare state retrenchment—affirming the historical institutionalists’ view of welfare states as de-commodifying institutions in the process—and the tangible policy instruments they use to pursue such goals. This focus

\(^{56}\) Congressional Budget Office (CBO), “Estimated Deficits and Debt under the Conference Agreement of H.R. 1, a Bill to Provide for Reconciliation Pursuant to Titles II and V of the Concurrent Resolution on the Budget for Fiscal Year 2018, as Filed by the Conferees to H.R. 1 on December 15, 2017,” (Washington, DC, 2018).

on individual (or rather, corporate) agency is necessary to my attempt to provide a realistic vision of political contestation over social policy. By the same token, it also seeks to avoid the trap of attributing historical changes to vague ‘forces of capital.’ Even still, the essence of the argument is one of a singular underlying force identifiable across multiple countries, and it is thus still vulnerable to the accusation that this is but an over-simplified ‘grand theory’ of the nineteenth-century variety.58

The response, as suggested above, is that identifying a historical trend common to many national political economies is not tantamount to claiming that they are all the same. Indeed, the great volume of scholarship seeking to unpack the disparate policy results of political institutions and historical legacies in different countries is for the most part well-taken. My quibble is that a focus on the comparative alone displaces the identification of the common, and that institutional diversity is the consequence of unique contingent factors that differently route systemic pressures. By the same measure, the hypothesis is not a teleological one, as Streeck seems to offer, for example, in his discussion of liberalization resulting from a ‘crisis of capitalism.’59 The underlying ‘logic of post-industrialism’ postulated here may well be an intrinsic consequence of late-stage economic development, but I am intentionally agnostic as to whether this is the case. It is not necessary to offer a comprehensive theory of economic progress, or

58 C.f. Michel Foucault: “Marxism exists in nineteenth-century thought like a fish in water: that is, it is unable to breathe anywhere else.” Michel Foucault, The Order of Things: An Archaeology of the Human Sciences (New York: Vintage, 1973), 261.
59 Streeck, Re-Forming Capitalism: Institutional Change in the German Political Economy, 10-11. “In this perspective, ‘globalization’ is not an accident, but just another stage in a long, more or less continuous process of capitalist progress, one that is not in any way derailed by single political-historical events, even if they are as major as, for example in our case, national unification.” See also, more generally, Streeck, Buying Time: The Delayed Crisis of Democratic Capitalism; How Will Capitalism End?: Essays on a Failing System (London: Verso, 2016).
uncover the existential origins of welfare states, to identify their clear trajectory over the last several decades.

If the hypothesis is borne out, and it becomes clear that firm-led welfare state retrenchment in multiple advanced political economies is the consequence of common systemic pressures, the question naturally arises as to whether social policy institutions are converging upon one another. This topic has received a great deal of scholarly attention with respect to other branches of political economy. Baccaro and Howell, for example, argue that advanced nations are converging in a neoliberal direction with respect to industrial policy. Jackson and Deeg challenge the Varieties of Capitalism authors’ idea that Coordinated Market Economies rest at stable equilibria, finding, “Looking across the cases two common patterns we find are a growing liberalization in relation to the role of the state and a growing segmentation (dualization) in terms of employment conditions and social protection.” Conversely, scholars such as Berger, Wade, and Guillén have explicitly disputed the idea that national political economies are converging, while Streeck has argued that convergence may take place in some “spheres” alongside simultaneous divergence in others. Yamamura and Streeck’s

---

second edited volume on ‘nonliberal capitalism,’ *The End of Diversity?*, it should be noted, makes virtually no mention of social policy transformation at all.\(^6^3\) The task here, then, is to re-cast the broader convergence debate and anchor the evolution of the welfare state within it.

To some extent, this dispute underlies a definitional one about what it means for two or more political economies to converge. Convergence does not require similar speeds of institutional change, nor the eventual realization of a shared institutional programme. Rather, it refers to a common *trajectory of change in a parallel direction*. As Baccaro and Howell maintain, “convergence does not require the same institutional form…different starting points and different mobilization capacities on the part of class actors makes it unlikely that institutional forms will converge” completely.\(^6^4\) In the case of welfare state development, the parallel direction of change is the reorientation of social policies around the goal of expanding the limits of labor markets, either as an explicit normative aim or implicitly through those policies’ ultimate effects.

Though this trend is hypothesized to be widespread, nowhere is its progression fully complete. Should the structural conditions motivating convergence continue unabated into the indefinite future, one might expect the forces countervailing retrenchment—trade unions, proportional legislatures, legacies of solidarism—to wholly degrade over time. But I have also built upon Polanyi’s work by suggesting a ‘third movement’ of labor re-commodification after the macro-historical trend of social

---


protection against markets; that same logic requires the possibility of another, differently oriented macro-historical trend yet to come. If welfare states are converging upon a singular model, it is one that will surely never be actually reached. But searching for perfect institutional symmetry obscures the common nature of the change occurring. In this sense, social policy regimes are, in fact, converging.

Some scholars, while noting that market liberalization seems to be occurring across many different advanced economies, differentiate ‘varieties’ of liberalization into distinct subgroups. Kathleen Thelen distinguishes the deregulatory approach to labor markets (as well as vocational training) that has taken hold in Esping-Andersen’s Liberal countries with the dualization of labor markets in Conservative ones.65 Still other political economies have undergone what she calls “embedded flexibilization,” wherein labor market liberalization has occurred “within the context of a continued strong and encompassing framework than collectivizes risk.”66 This challenges the idea that all advanced countries are converging upon a single model based upon their shared unraveling of social benefits. It is difficult to do justice to Thelen’s argument in the context of this thesis, which has little room for a case study on Denmark or the Netherlands, the two countries she where argues liberalization has not coincided with

65 The categorization of these processes alongside Esping-Andersen’s typology is Thelen’s. Her contention is that employment protections and welfare benefits in Conservative countries have been well-preserved for workers in the industrial ‘core,’ even amidst increasing inequality and declining coverage among other segments of the workforce. For a response to this argument, and a comment on the precarious bargaining position of workers even in Conservative countries’ industrial core, see chapter 4.

a retrenchment of risk protection. But even were its inclusion to disprove the convergence hypothesis as I have outlined it (and I am not convinced it would), the particularities of the situations in those countries correspond quite neatly to the hypothesis of institutional change I have offered here. As Thelen argues, social protections have been preserved in those cases because of the strength of organized labor, the persistence of cross-class coalitions, and the state’s capacity to force labor and industry groups into collective agreements. Put otherwise, where firms were unable to exercise the kinds of strategies outlined above, welfare state retrenchment has not significantly taken place. That there exist post-industrial countries where the retrenchment trend appears not to hold does not invalidate the trend, nor demonstrate that its simultaneous occurrence in very different political economies is incidental. And given the prominence of the two countries selected as case studies—not merely paradigmatic example of different models of capitalism, but the two largest economies of Europe and North America—those examples may well be the exception, rather than the rule.

Conclusion

Chapter 1 offered a critical analysis of the existing literature on welfare state diversity; this chapter attempted to develop a new comparative understanding of welfare state regimes. On its face, this framework bears little resemblance to that of either the historical institutionalists or the rational choice institutionalists. But I have

---

67 Were this a doctoral dissertation or monograph-length project, the first addition would undoubtedly have been a case study on one of the Nordic countries.
68 I thank Professor Jacob Hacker for this point.
not scorned them entirely. The preceding scholarship has significant utility in unmasking the particular peculiarities of each state’s welfare regime, as well as their historical sources, be they trade union strength, conservative landed elites, or interlocking ‘institutional complementarities’ with other parts of a production regime. Where the scholarship has fallen short is in positing a coherent vision of institutional change; indeed, this is the primary area of dispute between the two schools of thought. The solution is to put institutional change front and center: to subsume cross-national diversity within a broader understanding of common macro-historical development. I use the term macro-historical—and not, say, ‘world-historical’—because systemic structural forces are not felt equally in all places, nor addressed in the same manner; they certainly do not command identical institutional results. But the very fact that an array of phenomena is described as ‘diverse’ implies that those phenomena share some fundamental characteristics, such that they might be compared at all. Post-industrial welfare states are common, I posit, not simply ontologically—that they all exist simultaneously—but in the way that they have changed over time.

Even while advocating a more wide-angled view of comparative social policy, my own scope of inquiry is necessarily narrow. It is limited to the identification of a structural pressure on welfare states in the present moment—what I have deemed the logic of post-industrialism—and the specific mechanisms by which it forces change. Moving forward, the inquiry will narrow further still, examining specific aspects of social insurance in two countries over a limited period of time. To provide a sweeping study of welfare state changes in every country would be both infeasible and unreadable, sacrificing nuance before the false god of comprehensiveness. Nor shall I attempt to
test every element of the hypothesis, or every mechanism by which firms are posited to force welfare state retrenchment. Instead, the focus will be on the main thrust of the argument: that across very different national contexts, welfare state change is proceeding in a parallel direction, spurred by ultimately similar forces. The selection as case studies of the United States and Germany reflects the fact that they are very different political economies with distinct social policy legacies; the fact that they are ‘diverse’—and may well continue to be—is accepted a priori. But identification of a common sort of institutional change in both countries would provide a strong indication that its basis is systemic.
3 U.S. Old Age Pensions and Guided Institutional Drift

Introduction

The U.S. welfare state is currently undergoing retrenchment, and has been for the last several decades. The small improvements made in social insurance coverage during this period have been consistently undermined: the Children’s Health Insurance Program (CHIP), enacted after the failure to pass a universal healthcare law in 1997, spent four months in limbo without Congressional reauthorization at the end of 2017. While the Affordable Care Act of 2010 increased the number of Americans eligible for Medicaid, the administration of President Donald Trump has allowed states to impose work requirements on recipients as a precondition for receiving benefits. All the while, U.S. residents have seen the rollback of social policies from long-term unemployment benefits to income support for single mothers. In the latter case, the open-ended Aid to Families with Dependent Children (AFDC) program was replaced in 1997 with the more stringent Temporary Assistance for Needy Families (TANF).

---

1 Arguably the largest increase in the size of the welfare state in recent years has come in the form of repeated expansion of the Earned Income Tax Credit (EITC), most recently in 2009. But the EITC expansion is worth qualifying in two ways. For one thing, it is means-tested, offering benefits proportional to a low- or middle-income worker’s labor income. The program is designed to incentivize labor market participation, rather than offer social protection. And the fact that the credit is distributed as a tax benefit, rather than through active government appropriations, is also significant. A great number of potential recipients fail to collect the credit for this reason, because of the complexity of federal tax preparations. Moreover, that the EITC is designed as a tax credit changes its long-term political status: see below for a longer discussion of the ‘submerged state.’

2 Robert Pear, “Trump Administration Says States May Impose Work Requirements for Medicaid,” New York Times, January 11, 2018. At the time of publication, three states—Kentucky, Indiana, and Arkansas—have already received federal approval to introduce work requirements to Medicaid. At least seven other states have petitioned to do the same.
That reform reduced benefits, imposed work requirements on beneficiaries, and placed a lifetime cap of 60 months on the length of time for which they can receive assistance. States have the discretion to lower this lifetime cap even further: Arizona has reduced it to a mere 12 months.\(^3\) Though there remains fierce debate about the ultimate effects of the 1997 welfare reform, there is significant evidence that it has increased the incidence of extreme poverty among American children.\(^4\) The overall effect of these changes has been to reduce social protection for the most indigent members of society in favor of pushing them onto the labor market. Welfare assistance has continuously devolved from a right of citizenship to an earned privilege, offered only on the condition of one’s willingness to accept employment of virtually any kind.

In these examples, welfare state retrenchment has come in the form of cuts to federal appropriations or the end to long-term ‘entitlements’ to benefits. Change of this sort is the most common understanding of retrenchment in the popular U.S. imagination: hence President Bill Clinton’s (in)famous pledge to “end welfare as we know it.” But this chapter examines retrenchment of a different sort, and not one that has come in the form of a reduction in state spending: the changing character of private old age pensions sponsored by U.S. employers. The purpose of this focus is two-fold: to contribute to a larger scholarly project redefining what constitutes retrenchment, and to examine a facet of U.S. social policy that typifies its classification as a ‘Liberal’

\(^3\) Nathan Smith, “State Welfare Reforms: TANF Time Limits by the Numbers,” The Council of State Governments, http://knowledgecenter.csg.org/kc/content/state-welfare-reforms-tanf-time-limits-numbers. Though Arizona’s enrollment limit is the lowest in the country, 12 other states have caps of 24 months or less.

political economy (and by extension, a facet that would be most atypical in the German context). More importantly, this selection serves as a case study for appraising the hypothesis of the causes and agents of welfare state change offered in the previous chapter. Along with chapter 4, it will also examine the hypothesis of the parallel nature of welfare state change in diverse political economies.

The overall story I recount in this case study is the large-scale shift from defined benefit (DB) to defined contribution (DC) private pensions—especially so-called ‘401(k)s’—since the 1970s. This trend has resulted in significant stratification of retirement assets, and, because of the way DC plans are managed, a relocation of investment risk from employers to their employees. The consequence is that private pension plans—already fairly limited in their capacity as a social safety net, by virtue of being tied to employment—have become even less ‘de-commodifying.’Workers can expect fewer contributions to such plans from their employers, have to make technical investment decisions themselves, and, perhaps most importantly, have to individually bear the risk that their retirement assets will shrink due to negative capital market movement. Though private benefits (by their very nature) are not disbursed by the federal or state governments, I will argue that they constitute a key component of the U.S. welfare state, and this trend therefore a form of welfare state retrenchment.

In dialogue with theorists of institutional ‘drift,’ who argue that private pensions have changed because of growing incompatibility between the old DB plans and new political-economic environmental conditions, I contend that this development was a much more intentional one than has been previously described. It was large firms, and particularly their representatives through employer associations such as the U.S.
Chamber of Commerce and National Association of Manufactures (NAM), who sought to reduce the de-commodifying power of private pensions and restrict them to tools of human resource management. In the historical narrative offered here, firms motivate institutional change by lobbying and exercising legislative influence, by mobilizing their members to petition agencies, and by funding think tank research. Above all else, however, firms motivate change by curtailing the power of organized labor unions—the very historical actors that forced firms to install private pensions in the first place—as a ‘countervailing force’ to retrenchment. There was no grand, multi-decade plan to restructure private pensions in the U.S. But employer associations were instrumental to the changes that caused such restructuring, and expressed motivations consistent with its ultimate result. By their own actions, firms hold the keys to a now-shrinking kingdom.

Surveying the Landscape

Support for elderly residents in the United States is unique among other developed nations, even that in other ‘Liberal’ political economies with which the country is often clustered. It is often described as a ‘three-legged stool’ (a metaphor sometimes attributed to President Franklin D. Roosevelt) comprised of federal social insurance, employer-provided pensions, and employees’ personal savings. Public old age spending in the U.S. is distributed primarily through earned pension systems, rather than means-tested or flat-rate assistance programs funded through general revenue.⁵

⁵ A notable exception to this overall story is Medicaid, a means-tested medical assistance program jointly administered by individual states and the federal government. It does rely on general revenue appropriations, and benefits many seniors who rely on it for coverage of supplementary medical services not covered under Medicare—the primary old age health insurance program—such as elder
The marquee social insurance program in the United States, Social Security, was established in 1935 as a pay-as-you-go (PAYGO) trust fund funded through payroll taxes. Beneficiaries are eligible to receive full benefits, calculated in relation to their past contributions, at age 67, or a smaller proportion thereof as early as age 62. The conservative character of the program’s funding and pay-out structure limits its redistributive effects, but it still forms the backbone of old age support in the U.S.: in 2016, it distributed $769 billion to 44 million retirees and 6 million of their survivors.

In 2013, the most recent year for which data is available, public old age spending in the U.S. totaled 6.3 percent of GDP, compared to an OECD-wide average of 7.7 percent. Social Security also represents the greatest success story of the U.S. welfare state. The year before its enactment, approximately half of all elderly U.S. residents were thought to live in poverty. As Social Security expenditures per capita increased dramatically during the postwar era, the elderly poverty rate dropped from 35 percent in 1960 to 10 percent by 1995.

care facilities. However, as Medicaid assistance comes in the form of medical subsidies rather than cash payments, it is outside the scope my analysis here.

6 The Social Security system actually encompasses two trust funds: the Old-Age and Survivors Insurance (OASI) trust fund and the Disability Insurance (DI) trust fund. The former is much larger, with roughly $2.8 trillion in asset reserves at the end of 2016, compared to $46 billion in the latter. In recent years, benefit claims on the DI program have increased more rapidly than those of the OASI program, requiring re-allocation of Social Security payroll taxes to bolster the DI fund. The discussion here refers exclusively to the OASI program. Social Security Administration (SSA), “The 2017 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds,” (Washington, DC, 2017), 7.

7 Ibid., 2, 7.


In addition to Social Security, occupational pensions also play a fundamental role as the second leg of old age support in the United States. Private old age spending in 2013 amounted to a full 5.0 percent of GDP, well above the OECD average of 1.3 percent and the second-highest level of spending in the group.\textsuperscript{10} In 2015, nearly 135 million Americans—more than half of those over the age of 18—participated in private old age pensions.\textsuperscript{11} Though such programs are not directly administered by the federal or state governments, it is fitting to call them part of the ‘welfare state.’ For one thing, private pensions are so widespread that it is impossible to imagine their disappearance without the state stepping in to patch the hole in the safety net. Nor have private pensions developed in a vacuum, absent state intervention: since the late 1930s, private old age pensions have enjoyed tax-subsidized status because employers can generally deduct their contributions to them from corporate taxes, thereby rendering pensions an attractive form of non-wage compensation.\textsuperscript{12} In this manner, taxpayers fund private pensions to an extraordinary degree, simply through automatic exemptions rather than active appropriations. This distinction is the basis of what is often referred to as the ‘submerged state’: like an iceberg, government spending is divided between what is visible above sea level and a great chunk of invisible spending through forgone revenue, hidden through subsidies below the surface. Congress’ Joint Committee on Taxation

\textsuperscript{10} Organisation for Economic Co-Operation and Development (OECD), “Social Expenditure—Aggregated Data.” The United Kingdom had slightly greater private spending, at 5.1 percent of GDP.


\textsuperscript{12} Jacob S. Hacker, \textit{The Divided Welfare State: The Battle over Public and Private Social Benefits in the United States} (New York: Cambridge University Press, 2002), 86. Individuals are only taxed on their compensation through those funds upon withdrawing pension assets. More recently, employee contributions to certain employer-sponsored funds have also enjoyed tax-exempt status, as will be discussed in detail later in this chapter.
(JCT) estimates that over the five years from 2016 to 2020, tax subsidies of private pensions will result in a net loss to the Treasury of over $1 trillion.\footnote{Joint Committee on Taxation (JCT), “Estimates of Federal Tax Expenditures for Fiscal Years 2016-2020 (JCX-3-17),” (Washington, DC, January 30, 2017), 38. Defined benefit (DB) pension exemptions will cost $424.3 billion over the period, and defined contribution (DC) exemptions $583.6 billion. This figure does not include the cost of individual retirement accounts (IRAs), whose exemptions will result in a net loss of $130.4 billion.}

In the 1970s, through passage of the Employment Retirement Income Security Act (ERISA), the federal government gave private pensions official sanction by imposing stricter requirements as to their actuarial soundness and how long employees had to work in order to receive benefits. It also established a Pension Benefit Guaranty Corporation (PBGC) to pool risk across private pensions, offering a public endorsement of participation not unlike the FDIC did for deposit-taking banks. Not incidentally, as I will discuss later in the chapter, the PBGC also played an important role in the large-scale shift from DB to DC pensions. Though private old age pensions rest upon non-government spending, they are regulated, insured, and even significantly subsidized by the U.S. government. Any useful definition of the U.S. welfare state ought to include them. As one AFL-CIO official testified as early as the 1940s, private pensions “are a form of social insurance in the United States of America….The labor movement would have preferred some other approach to these matters, but this is what has grown up in our society.”\footnote{Hacker, \textit{The Divided Welfare State}, 140.}

A longstanding debate within U.S. social policy circles has been what relationship private plans should have to Social Security. The program’s administrators and labor activists historically saw public benefits as the core of old age insurance, to be
supplemented by private plans only at the margins, whereas business leaders such as Ira Mosher, the president of the National Association of Manufacturers (NAM), described Social Security as a “basic minimum layer of protection…to provide merely the bare necessities.” What has actually unfolded is something roughly between the two positions. In 1975, old age and survivors’ benefits distributed through the Social Security amounted to $58.5 billion, 75 percent of the $77.6 billion in old age benefits distributed in total. By 2014, the figure declined to a slimmer majority of 52 percent: that year, some $650 billion were withdrawn from defined benefit and defined contribution private pensions. (See figure 3.1.) The first private plans in the U.S. were established in 1875 by the American Express Company, and their growth accelerated after the favorable tax status granted to them during the Roosevelt administration. In 1965, General Electric’s manager of employee benefits testified before Congress, “We believe that present attitudes, if allowed to stand, will ensure the rapid extension of private plans to all employees who desire coverage.” That trend continued into the late 1970s, by which point 45 percent of American workers were covered by some sort of private plan. But though the proportion of old age benefits paid through private pensions has risen significantly over the last 40 years, the proportion of workers receiving them has remained effectively the same.

---

15 Ibid., 138.
Figure 3.1  Public and Private U.S. Pension Spending, 1975-2014

Though a full-scale analysis of the reasons private plans emerged is not necessary here, it is worth remarking upon the crucial role of organized labor in the larger story.

Trade unions strongly advocated for generous defined benefit pensions for their members, and their ability to press for benefits was institutionalized in 1948 when the National Labor Relations Board ruled that employers were legally obligated

---


to collectively bargain on the subject of pension benefits. In a conference organized by the U.S. Chamber of Commerce the previous year, one attendant asked, “Do you not think that there is an increasing trend towards unions attempting to force corporations to install retirement plans?” a statement with which the speaker, a vice-president of Wachovia Bank, agreed. The National Association of Manufacturer’s Labor-Management Relations Committee unanimously decided:

Management should not surrender its initiative in this matter to the union....Unless management takes the initiative in satisfying this desire [for employee benefit programs], union sponsorship of these programs is inevitable, with resulting loss of employee confidence and faith in their management.

Old age pensions were also established by firms like Eastman Kodak in efforts to prevent unionization of their workforce. Trade union agitation, or the specter thereof, strongly contributed to the extent to which private pensions took hold. This historical fact is worth keeping in mind while discussing how such pensions have changed over the last several decades.

It may seem strange to use de-commodification of labor as the variable by which to measure the strength of the welfare state in the case of private pensions. Benefits of that sort, after all, are conditional on long-term employment, designed as non-wage compensation for high-value employees or to incentivize workers to stay at a particular firm for a significant length of time. But private pensions still have a de-commodifying

---

23 Hacker, The Divided Welfare State, 89, 128.
effect, for at least three reasons. First, the extent of pension assets a worker has accumulated will influence the point in life at which she can retire. Private pension benefits may also determine the ability of other household members to stay home to care for an elderly family member. Finally, pension disbursements also influence their recipient’s need to work even after reaching retirement age. The mean senior over the age of 65 in the United States is not only employed, but still relies on labor income for nearly one-third of her annual income.\textsuperscript{24} Private pension benefits account for a smaller percentage (Social Security is by far the most important source of income), but the more generous they are, the less that individual presumably needs to work to make ends meet. Even though they are conditional upon employment, private pensions can still offer social protection through a de-commodifying effect on labor. But not all private pensions are created equally.

Despite their (increasingly) central role in the U.S. pension landscape, private plans do not distribute benefits uniformly across the working population. That the share of all old age benefits disbursed through private plans has gone up, while their coverage rate stays the same (around 45 percent) necessitates that a minority of the population must be benefitting more than others. And among those workers and their bereaved lucky enough to have private pension coverage, benefits are further stratified. Under the initial tax code provisions granting employer-sponsored plans subsidized status, firms were obligated to offer benefits on a relatively equitable basis, not simply to higher-paid workers, else pension funds simply become a way to defer bonus wages

and save on taxes in the process. But accompanying rules authorized firms to include lower-income workers’ Social Security benefits in an ‘integrated’ calculation of retirement benefits, thereby allowing significant disparities in benefits. In 1966, when the U.S. Treasury Department drafted regulations to tighten this loophole and equalize private pensions, industry lobbyists quickly mobilized against the proposed rule. Of 1,800 individual comments submitted on the proposal that year, all but one opposed it, and the Treasury Department eventually watered down the rule to the point that it was “virtually meaningless.” The inequitable character of private pensions—even in the era when defined benefit plans dominated the landscape—should thus be seen as a direct consequence of firm advocacy.

A focus on the increasing dominance of private pensions alone belies an equally tectonic shift that has occurred over the past several decades: the mass substitution of defined benefit (DB) pension plans for defined contribution (DC) ones, especially among private sector workers. (See figure 3.2.) DB pensions are based upon a guaranteed monthly benefit: once an employee has worked in a firm long enough and otherwise meet the requirements to become ‘vested’ in a plan, she or he can expect to receive regular benefit payments according to a set formula. How the pension fund’s assets are invested—whether in U.S. Treasuries, bonds, equities, or even the firm’s own stock—is of concern to the worker only to the extent that the fund remains solvent and is able to pay out benefits. DC pensions, on the other hand, are based upon initial

---

26 Hacker, The Divided Welfare State, 146–47.
27 Of course, individuals may wish for their pension assets to be invested in ‘high road’ or local firms, and to the extent that other investments, such as outward FDI, may promote outsourcing of jobs, such
payments to an investment fund and disburse benefits according to the market performance of that fund. Individual recipients are frequently able to make investment decisions on behalf of their own pension dollars, structuring their asset allocation according to their ‘risk profile.’ Though such plans were initially marginal compared to defined benefit pensions—in 1979, 83 percent of workers with a private pension plan primarily relied on a DB plan—they have grown to significantly overshadow them.28

(See figure 3.3.) Moreover, within the larger category of DC plans, one type of pension has grown to outsized prominence: the so-called ‘401(k).’ The reasons for its emergence, and its effect on the welfare state’s de-commodification of labor, are the main subjects of inquiry here.

---

Figure 3.2  Number of Pension Plans by Type, 1975-2014

![Graph showing the number of pension plans by type from 1975 to 2014. The graph indicates a steady increase in the number of Defined Benefit (DB) plans and a peak in 1987, followed by a decline. The number of Defined Contribution (DC) plans shows a steady increase throughout the period.](image)

Figure 3.3  Private Benefit Disbursements by Type, 1975-2014

![Graph showing the percentage of private benefit disbursements by type from 1975 to 2014. The graph indicates a decrease in the percentage of Defined Benefit (DB) disbursements and an increase in Defined Contribution (DC) disbursements over time.](image)


30 Data source: “Pension Plan Benefits Disbursed by Type of Plan, 1975-2014.”
401(k) Society

The actual creation of the 401(k), it is fair to say, was in essence an accident. But as will become clear, the mere accidental status of an event does not mean that it was unforeseeable, or contravened a larger historical trend. The story originates with the Revenue Act of 1978, signed during the administration of President Jimmy Carter, whose central features were lowering individual income, corporate, and capital gains taxes. Section 135 of the law, which added section 401(k) to the Internal Revenue Code (hence the name), was intended to clarify the tax treatment of a particular variety of employee profit-sharing programs. The aim, according to the Joint Committee on Taxation’s report, was to ensure that “a participant in a qualified cash or deferred arrangement will not have to include in income any employer contribution to the plan merely because he could have elected to receive such amount in cash instead.” Assuming this to be a technical correction, the report added, “This provision will have a negligible effect upon budget receipts.”31 But in 1980-81, an enterprising benefits consultant named Ted Benna saw that the provision could be read to grant tax-exempt status to employees’ contributions to employer-sponsored pension funds—in essence, to defer taxes on wages until they had already accrued years’ worth of capital gains. With the help of a friend serving in Ronald Reagan’s cabinet, Benna persuaded the IRS to issue regulations cementing this interpretation, and the 401(k) revolution began.32

congressional report’s claim that the provision would have ‘negligible impact’ turned out to be less than accurate.

401(k) retirement plans serve to de-commodify an individual’s labor market participation far less than a traditional defined benefit pension. Under the mantle of increased flexibility, such plans shift the risk of market failure onto employees, requiring them to individually calculate how much income they must set aside for retirement and how to invest those assets in the interim.33 Given a multitude of allocation choices, workers frequently lack the technical guidance necessary to make sound investment decisions. And because pension assets are disaggregated, they lose the ability to pool risk offered by large DB plans. Moreover, whereas DB plans had to hew to at least some degree of benefit equity among workers within an individual firm, 401(k)s eliminate such considerations entirely.34 Employer contributions to such funds are usually offered in the form of ‘matching’ of employee contributions. An employee earning close to a subsistence wage may not be able to divert any spare income to a retirement account, and because their employer is not otherwise contributing to the plan, the alleged ‘benefit’ of a 401(k) offers no practical value. One survey found that 43 percent of full-time workers eligible for such plans did not participate for reasons of affordability.35 Indeed, the median value of all 401(k) accounts is $22,000—hardly

33 This is not to say that DB pensions are riskless, of course: individuals usually have to work at a firm for a given period of time before becoming ‘vested’ in its retirement plan and guaranteed benefits, and face the possibility of being laid off before reaching this threshold. And there is always the risk of pension fund insolvency or the firm going bankrupt, which may result in pensioners taking a significant haircut on their retirement assets. (See the discussion of the PBGC below.) Nonetheless, the risk to the average worker of participation in a DC plan is still greater than that of a DB one.
enough for a comfortable retirement—and 40 percent of workers with such plans have saved less than the average annual Social Security benefit. Conversely, high-income earners who are able to divert money from their paychecks to a 401(k) greatly benefit from their tax-subsidized status. While workers in the top quintile of families age 32-61 earn 63 percent of wage income, they hold 74 percent of all retirement account savings; workers in the bottom three quintiles, though earning 17 percent of income, hold only 6 percent of such assets. Thus while the coverage rate of all private pensions may have stayed essentially constant over the past forty years, at 45 percent, the share of workers significantly benefiting from such plans has actually shrunk.

Drawing upon the framework of endogenous institutional change proposed by Streeck and Thelen, Hacker has referred to the shift from DB to DC plans as welfare state change through institutional “layering.” Though not abandoning DB plans wholesale, the creation of an alternative type of pension adjacent to them allowed firms to gradually shrink their importance. More generally, pension reform is understood less as an explicit challenge to the U.S. welfare state than a kind of institutional “drift.” Drift occurs when institutions diverge from the political and economic conditions where they can function successfully, thereby subject to “erosion or atrophy” without

---

36 Ibid., 10.
37 Morrissey, “The State of American Retirement: How 401(k)s Have Failed Most American Workers,” 26. That the disparity of earned income between the quintiles is also so large merits mention, but it lies outside of the scope of this chapter’s discussion.
active efforts to maintain them. As Hacker argues, drift is not always accidental, but “can also be promoted by political cultivation.”\(^{39}\) He goes on:

It was employers, after all, who constructed the extensive private systems of risk socialization that they are now so busy dismantling. Their abandonment of the old order appears to reflect not just the rising cost of past approaches and economic changes that have undermined the value of private benefits for corporate strategies, but also the absence of effective ideological or political counterweights in either the halls of government or the private sector.\(^ {40}\)

Hacker notes in particular GOP efforts to expand 401(k) plans—as well as private individual retirement accounts (IRAs)—since the Regan administration as a primary way that drift has occurred. But the causal roots of the underlying change stem far before the creation of the 401(k). Indeed, even if its emergence was wholly accidental, the conditions under which the 401(k) would flourish (for some, at least) were a product of firms’ conscious efforts. To understand them, one must travel even further back in time, to what is often thought of as the heyday of corporate liberalism.

“\textit{That New Labor Law}”\(^ {41}\)

At the close of World War II, the end to military conflict in Europe and East Asia coincided with a rash of domestic strife within the United States. The country’s industrial capacity increased dramatically over the course of the war, and workers who had accepted low wages as their contribution to a patriotic struggle—nearly every major industry was intimately involved in the production of war materials—were no longer willing to do so. In the year and a half following Victory over Japan Day, seven million

---


\(^{41}\) Title of pamphlet published by the National Association of Manufacturers (NAM), 1947.

By February 1946, a full quarter of the entire Congress of Industrial Organizations (CIO), which comprised over six million automobile, steel, electrical and other industrial workers, was on strike.\footnote{Philip Yale Nicholson, \textit{Labor’s Story in the United States}, ed. Stanley Aronowitz, Labor in Crisis (Philadelphia: Temple University Press, 2004), 245.} It was in this context that some of organized labor’s greatest victories were forged. The United Auto Workers (UAW) members at General Motors, led by Walter Reuther, struck for 113 days in 1945-46, demanding a 30 percent increase in wages. Though that strike was largely unsuccessful (Reuther’s demands were too ambitious, and his bargaining strategy undercut by less generous pacts agreed to by other unions), the 1948 UAW-GM contract include a Cost of Living Adjustment (COLA) clause that guaranteed wages would rise alongside increases in the cost of goods. A five-year contract agreed to in 1950 cemented this provision, wage increases tied to improvements in productivity, and guaranteed pensions and health insurance.\footnote{Nelson Lichtenstein, \textit{State of the Union: A Century of American Labor} (Princeton, NJ: Princeton University Press, 2002), 122-23. The COLA was updated quarterly in reference to the Consumer Price Index (CPI) calculated by the federal Bureau of Labor Statistics (BLS). Reuther initially opposed the COLA clause and came to view it as a stopgap measure, contending that indexing wages to inflation was insufficient to the union’s larger goal of shifting the balance of industrial power (and the share of industrial profits) towards workers. Productivity wage increases marked a step in this direction.} At the time it was announced, the labor economist Frederick H. Harbison (not incidentally, one of the authors, alongside Clark Kerr, of \textit{Industrialism and Industrial Man}) called the contract “the most significant development in collective bargaining” in more than a decade.\footnote{Frederick H. Harbison, “The General Motors–United Auto Workers Agreement of 1950,” \textit{Journal of Political Economy} 58, no. 5 (Oct. 1950): 397. See chapter 1 for a discussion of \textit{Industrialism and Industrial Man}. Harbison and his co-authors saw centralized collective bargaining and profit-sharing...}
emulated among other industrial unions; in a little over a decade, “the COLA principle had been incorporated into more than 50 percent of all major union contracts.” Those agreements became the basis for significant wage gains among middle-income workers during the postwar era, and the historically low rate of income inequality observed during that period.

The strike wave of 1945-46 also catalyzed a wave of resistance to organized labor as a political and economic force. Work stoppages resulted in 144 million work hours lost, and the aggressive bargaining tactics of unions like the UAW struck fear in the hearts of employers. Southern businesses in particular were ardently opposed to the CIO, with its racially integrated ranks and advocacy for equality in the workplace. In the wake of the strikes and the continuation of wartime price controls, President Harry Truman had become deeply unpopular, and Republicans swept both houses of Congress in the 1946 midterm elections. Senator Robert A. Taft (R-OH), the incoming chairman of the Labor and Public Welfare Committee, planned to table labor law reforms in the new legislative session. The National Labor Relations Board (NLRB), Taft later maintained, seemed driven by “a public mission to place a union of the Congress of Industrial Organizations in every plant in America.” Taft, and his allies in the business community, were determined to ensure that this would not occur.

---

agreements, installing an equal balance of power between capital and labor, as key components of a ‘pluralist’ industrial society.


In 1947, the National Association of Manufacturers (NAM) and U.S. Chamber of Commerce worked with Republican leadership in both houses of Congress—and quite a few Democrats, as well—to pass the Labor Management Relations Act, commonly known by the names of its sponsors, Taft and Representative Fred A. Hartley (R-NJ). Amending the National Labor Relations (Wagner) Act of 1935, which its proponents saw as too tilted in favor of trade unions, Taft-Hartley imposed a host of requirements that restricted union negotiation tactics and tightened collective bargaining. It prohibited wildcat strikes and secondary boycotts of goods; authorized the President to call off strikes under conditions of “national emergency”; barred union contributions to candidates for federal office; and, perhaps most importantly, outlawed so-called ‘closed shops’—where firms are contractually bound to hire only union members—and allowed states to pass ‘right-to-work’ laws that effectively required unions to bargain on behalf of non-union employees out of union coffers.49 According to one contemporaneous scholar, NAM and the Chamber “campaigned to repeal the Wagner Act from the time of its passage,” and NAM had been distributing literature to local antiunion groups for a full decade before Taft-Hartley was passed.50 NAM’s Law Department drafted much of the bill text that would eventually become law, and

49 ‘Union shops,’ in which workers can be required to join a union (though they not need be one already) as a condition of employment, are still allowed in the United States. ‘Right-to-work’ laws function by prohibiting employers from mandating that employees pay ‘agency fees’ to unions that represent them in negotiations with employers. As it is not feasible to negotiate for wages, working conditions, and benefits for certain union workers, but not others, in a large firm, agency fees are designed to circumvent the free rider problem which incentivizes workers to decline to pay union dues while enjoying the benefits gained through collective bargaining. ‘Right-to-work’ laws are currently on the books in 28 states, and have been strongly lobbied for by business associations such as the U.S. Chamber of Commerce.

the Association spent more than $3.6 million—almost $50 million in 2017 dollars—lobbying on behalf of the bill.\textsuperscript{51} It is fair to say that Taft-Hartley was the creation of American industry, and, given that it passed both houses of Congress over President Truman’s veto, a highly impressive one at that.

Despite industry’s claims that it merely leveled the playing field of collective bargaining, Taft-Hartley proved to be extremely effective in reducing labor union strength in the United States. Though the proportion of private sector workers in unions (or union ‘density’) continued to grow in the years immediately following 1947, reaching its peak in 1954, empirical work suggests that the ‘right-to-work’ laws authorized by Taft-Hartley diminished union election success among new organizing efforts and the average size of bargaining units.\textsuperscript{52} The proportion of U.S. workers in unions in 2017 was just 10.7 percent, compared to 31.2 percent in 1948.\textsuperscript{53} Almost half of those workers are government employees who are members of public sector unions; in the private sector, union density is a mere 6.5 percent. Not only has income inequality risen dramatically during this period, the share of economic output going to compensating labor more generally—from executive salaries to janitorial wages, union and non-union workers—perceptively dropped from 65.8 percent to 58.4 percent.\textsuperscript{54}

\textsuperscript{51} McCarthy, Dismantling Solidarity, 97.
\textsuperscript{54} Michael D. Giandrea and Shawn A. Sprague, “Estimating the U.S. Labor Share,” \textit{Monthly Labor Review}, U.S. Bureau of Labor Statistics (February 2017). Though this may not seem like a major change, put otherwise, it means that the share of total output going to compensating capital owners increased by more than a fifth. For a seminal treatment of U.S. wage inequality, see Thomas Piketty.
Obviously, not all of the decline in density (and simultaneous drop in the relative value of middle-class incomes) is attributable to Taft-Hartley. Over a similar timespan, the proportion of U.S. GDP stemming from manufacturing dropped from a high of 28.1 percent in 1953 to 11.7 percent in 2016. But the proportion of manufacturing workers represented by unions is now not much higher than the private sector average, at 9.1 percent. And the continual efforts of industry representatives to institute ‘right-to-work’ laws—as recently as 2017 in Kentucky—speaks to their long-term efficacy in curbing the power of organized labor.

Disrupting labor power has had a significant impact on increasing income inequality in general, and the decreasing generosity of private pensions in particular. By limiting union membership, firms limit union dues and thus labor’s ability to mobilize for political goals on the national scale. Moreover, decreasing union representation limits workers’ abilities to press for better pensions within their own workplaces. Ippolito has found that nearly half of the shift from DB to DC pensions can be attributed to declining union membership. The majority of new pension plans in non-unionized firms are 401(k)s, and among existing plans, unionized firms are far more likely to continue to offer generous DB pensions. In 1979, at the precipice of the 401(k) revolution, workers represented by unions were 12 percent more likely to participate in


56 For efforts of groups like the American Legislative Exchange Council (ALEC) and the Heritage Foundation—both substantially funded by large U.S. firms—to implement ‘right-to-work’ in Kentucky, see Shaila Dewan, “Foes of Unions Try Their Luck in County Laws,” New York Times December 18, 2014.
DB pensions than their non-union counterparts; just nine years later, by 1988, the “incremental effect of this variable [was] almost three times as high.” 57 The current gap in pension coverage between unionized and non-unionized workplaces is enormous. A full 66 percent of workers in the private sector who are members of unions have DB pensions; for their non-union counterparts, the figure is 9 percent. 58 Right-to-work laws introduced through Taft-Hartley thus came to have a dramatic effect on the character of old age pensions. By virtue of a general attack on organized labor, firms simultaneously paved the way to switch out their private old age pensions for more inequitable and less de-commodifying versions.

A disproportionate share of remaining DB pension assets is held in trust for workers in the public sector, where union density is much higher than the rest of the economy. While 74 percent of state and local government workers participated in DB plans in 2017, only 15 percent of private sector workers did the same. 59 This is in part a testament to the successful organizing tactics of public sector unions, but moreover the very different set of constraints upon government bureaucrats as opposed to private shopfloor managers. Federal and state governments agencies have predetermined budgets and do not have to answer to shareholders. Nor do they face competition from domestic or international rivals, as they hold a monopoly on the completion of

59 Ibid. For a detailed look at the disparity in DB pension coverage between public and private sector workers, highlighting the importance of unionization, differing employer motivations, and lack of ERISA requirements on public sector plans, see Alicia H. Munnell, Kelly Haverstick, and Mauricio Soto, “Why Have Defined Benefit Plans Survived in the Public Sector?,” (Center for Retirement Research at Boston College, December 2007).
particular services. Government officials may even have an *incentive* to respond positively to public sector union demands if the president or governor (or her or his party) relies upon trade unions for political support. Therefore, the incentive for public sector bureaucrats to engage in ‘union-busting’ tactics to strengthen their bargaining position and reduce pension expenditures is quite low. This is not the case for private sector managers, however, who have sought to undercut labor unions not only within their individual firms, but also through policies that affect industrial relations across the United States.

Though Taft-Hartley impacted old age pensions in the broad sense I have described, it also addressed it specifically in a little-remarked-upon section of the act. In 1946, bituminous coal miners of the United Mine Workers (UMW) union staged a high-profile nationwide strike led by union leader John L. Lewis demanding mine operators contribute to a “health and wealth fund” to be used for employee benefits, ultimately settling at the rate of five cents per ton mined. In response, Senator Harry F. Byrd (D-VA) tacked an amendment onto the Case bill (a forerunner to Taft-Hartley), stating:

> I am endeavoring to strike against the attempt of representatives of labor to use such payments in establishing funds over which no one but the labor representative would have any control. I assert that if such a condition were allowed to take place, labor unions would become so powerful that no organized government would be able to deal with them.

---

In a dramatic coda, Byrd added that union control of health and welfare funds would lead to “the complete destruction of the private enterprise system in the U.S.” Though the Case bill failed as a result of Truman’s veto, a very similar provision ultimately passed as section 302 of the Taft-Hartley Act. Its effect was to outlaw any employer contribution to a union-controlled welfare fund unless the fund was jointly administered by the firm. The prohibition extended to funds established for the purposes of old age pensions. Violators were subject to up to $10,000 in fines and the prospect of a year in prison.

Rather than proactive policymaking aiming to guide the development of private pensions in the U.S., section 302 was a reactive measure whose aim was to limit union influence over such pensions. In his floor statement on the Senate bill, sponsor Robert Taft described the welfare fund restriction as a “stopgap provision until a further study can be made, in order that abuses may not arise.” But the initial version of the bill passed in the House of Representatives went further still, prohibiting employer contributions to union health and welfare funds even under conditions of joint administration. The provision was grouped with another prohibiting firms from assisting unions in collection of dues by deducting them from workers’ paychecks, a common practice at the time. The language used in the committee report makes clear that the aim was not simply preventing “abuses,” but curbing union efforts to bargain for private pensions: “Certainly, it is not in the national interest for union leaders to

---

61 McCarthy, *Dismantling Solidarity*, 96.
control these great, unregulated, untaxable funds *derived from extractions upon employers.* By giving employers the keys to pension funds—either through joint management or outright control—lawmakers ensured that employers could use them for purposes of human resource management. And employers’ use for private pensions, quite naturally, does not necessarily dovetail with workers’ desire for de-commodification of their need to work in old age.

Because this statutory change took place relatively early in the development of private pensions, it has received relatively little scholarly attention as an antecedent of welfare state retrenchment. But section 302 clearly upended the landscape in the 1940s, and private pensions would look very different today were it not for the provision. In 1945, slightly less than one-third of private pensions were administered by unions, with the rest closely split between jointly managed plans and those delegated by employers to an insurance company. Put otherwise, some two-thirds of private pensions were either directly or jointly controlled by labor unions. Shortly after 1948, given the prohibition of union-sponsored funds, the number of participants in jointly managed plans jumped dramatically alongside increasing union density. But by 2014, the number of participants in multiemployer plans (the primary way such jointly managed plans have been constructed) was 14 million, just 11 percent of the total number of participants in private pension plans; such plans also held only 8.5 percent of all private

---

pension assets.\textsuperscript{65} Indeed, the proportion of pension assets held through \textit{all} plans established through collective bargaining, whether jointly administered or not, made up one-quarter of the total.\textsuperscript{66} Though the more hardline version of Taft-Hartley passed by the House ultimately did not become law, its legislative aim—to kick unions out of the private pension landscape—has come relatively close to fruition.

Just as employer groups were pushing to move union health and welfare funds under the auspices of joint management, they simultaneously resisted any efforts to formally bargain over pension plans with unions. The same year that Taft-Hartley was passed, NAM’s Labor-Management Relations Committee agreed upon “the sincere desire of industry to establish programs to protect and safeguard the welfare of its employees.” It went on to note, however:

In connection with the collective bargaining aspect of this subject, the Committee agreed...that employers must do everything possible to avoid bargaining regarding such programs, while at the same time engaging in such informal discussions with employees and their representatives as would not lead to or imply contractual obligations.\textsuperscript{67}

Though industry was to position private old age pensions as a form of social protection sufficient to eliminate the need for public intervention—an early draft of a 1965 policy statement entitled “Industry Believes,” for example, claimed “federal benefits are only a substitute for gainful employment or a supplement to private provisions,” and that the federal government “has no place in an old age assistance program”—it also sought

\textsuperscript{65} Multiemployer plans have also become less attractive to employers because of innumerable fiscal and regulatory challenges those plans have faced in the intervening years. As I contend below, however, the causal chain that created the need for ERISA (1974) and the Multiemployer Pension Plan Amendments Act of 1980 arguably began with this shift of control over pension assets to employers.


\textsuperscript{67} “NAM Labor-Management Relations Committee Minutes.”
to ensure that private pensions would be a conditional tool of management rather than a guarantee.68 “There was unequivocal agreement,” according to the Committee’s minutes, “that management should have the final decision both as to the establishment and operation of employee benefit plans.”69 Joint administration was hardly the end goal, but a waystation towards the ultimate elimination of trade union influence over private pension plans.

In 1948, the U.S. Court of Appeals for the Second Circuit ruled in *Inland Steel Co. v. NLRB* that firms were required to bargain over health and welfare funds, including old age pensions: essentially, that which they had tried to avoid doing under any circumstances. The response was swift, with the Chamber of Commerce claiming that the decision would “seem likely to be an encouragement of union demands for pension systems in coming contract negotiations...Such demands seem likely of widespread adoption by the unions as business conditions make further wage increases totally unrealistic.”70 NAM’s *Law Digest*, written by the same department that drafted much of Taft-Hartley, expressed surprise that the decision contravened their (err—Congressional) legislative intent: “The policy and theory was not novel under prior Wagner Act decisions...It would not seem, however, to be the policy of the Labor Management Relations Act [Taft-Hartley] to frustrate the bargaining process by

---

68 “Proposed Amendments and Additions to the Employee Health and Benefits Section of ‘Industry Believes,’ as Approved by the Public and Private Benefits Subcommittee,” 1963. National Association of Manufacturers Papers, Series I, Box 23, Hagley Museum & Library, Wilmington, DE. This assertion was scraped prior to the document’s finalization.
69 “NAM Labor-Management Relations Committee Minutes.”
70 *Labor Relations Letter* no. 47,” May 1948. U.S. Chamber of Commerce Papers, Series IV, Box 71, Hagley Museum & Library, Wilmington, DE. The Chamber was reacting to the initial 4-1 decision by the National Labor Relations Board, later upheld by the Second Circuit.
denying to either party the effectuation of rights stated in freely negotiated contracts.”\(^{71}\) Five years later, in 1953, NAM’s Law Department submitted testimony before the House Education and Labor Committee urging legislation that would place health and welfare funds outside the scope of mandatory collective bargaining.\(^{72}\) Though NAM proclaimed the potential universality of private benefits in sweeping terms—recall the statement of the General Electric executive: “we believe that present attitudes, if allowed to stand, will ensure the rapid extension of private plans to all employees who desire coverage”—the notion of allowing employees or their representatives to be involved in decision-making over those plans was to be avoided at all costs.\(^{73}\)

The efforts of firms’ representatives, such as NAM and the Chamber of Commerce, to eliminate the role of unions in private pension administration was focused, prolonged, and, most of all, effective. As I have shown, there is substantial empirical evidence indicating a connection between union representation and more generous pension benefits; by eliminating that ‘countervailing power,’ firms likewise eliminated a potential obstacle to the large-scale shift to defined contribution pensions. It seems quite likely that if unions controlled the bulk of private pension plans today, the distribution of assets would be less skewed towards high-income earners. But section 302 of Taft-Hartley also set in motion a causal chain that especially motivated firms to switch to DC pensions like 401(k)s, through passage of the Employee

---

\(^{71}\) “NAM Law Digest 10, No. 4,” September 1948. National Association of Manufacturers Papers, Series V, Box 57, Hagley Museum & Library, Wilmington, DE.

\(^{72}\) “Statement of Law Department, National Association of Manufacturers, before House Committee on Education and Labor,” May 8, 1953. National Association of Manufacturers Papers, Series V, Box 59, Hagley Museum & Library, Wilmington, DE.

\(^{73}\) “Statement on Private Pension Coverage before the Senate Subcommittee on Employment and Retirement Incomes.”
Retirement Income Security Act (ERISA). That excruciatingly complex law is partially summarized above, but for the purpose of this thesis, its primary result was forcing firms to accept stronger fiduciary responsibility for the management of private pension funds for their employees, and to satisfy a bevy of regulatory tests to demonstrate as much. While some scholars have pointed to ERISA’s requirements as a key ‘push’ factor for firms in their move to DC pensions, the legislation would not have developed in the way it did were it not for Taft-Hartley.\textsuperscript{74}

Unlike was the case for Taft-Hartley, employer groups were not strong advocates for passage of ERISA; on the contrary, according to the \textit{New York Times}, they fought it with “fierce opposition.”\textsuperscript{75} Throughout the 1960s and 1970s, Congressional efforts to further regulate private pension plans were met with pamphlets published by NAM and the Chamber with titles like “A New Straightjacket for Employers” and “Will There Be a Private Pension in Your Future?,” ominously warning of firms eliminating their plans.\textsuperscript{76} But in some sense, greater federal intervention in private plans was a necessary—or at least predictable—consequence of moving pension management under employer control. Employers had good reason to resist new vesting requirements (prescribing how long employees had to work at a firm


in order to begin receiving benefits), but the proliferation of private plans was bound to produce calls for standardization between firms. And given that NAM’s Employee Health and Benefits Committee decided that pension assets ought to be held as “general assets of [a] company,” rather than “in trust,” stricter federal standards with respect to plans’ financing could hardly come as a surprise.\(^{77}\) Indeed, the years preceding ERISA’s enactment in 1974 were marked by a series of ineffective stopgap measures attempting to impose discipline on private pensions, most notably the Welfare and Pension Plans Disclosure Act (WPPDA) of 1959. The crux of employer groups’ argument against new legislation was the dubious claim that there was already an effective “voluntary, self-policing method of preventing abuse” in pension management.\(^{78}\) ERISA may have been passed under unusual circumstances—especially given firms’ strident opposition to it—but its core feature was a long time in the making.

In sum, while the creation of the 401(k) was an accident of history, the conditions that allowed for its proliferation were not. By removing labor unions from pension administration except under special jointly managed plans, and by undercutting union power more generally, firms weakened a key constituency that would have resisted the move to DC pensions. From intellectual conception to the drafting of bill text to the lobbying muscle necessary to secure passage (over President Truman’s veto, no less), employer groups were active at every step involved in Taft-


Hartley. And when faced with developments at odds with their goal of controlling private pensions, such as a court decision forcing firms to collectively bargain over them, employer groups reacted strongly in urging a legislative fix. To the extent that firms switched to 401(k)s because of increasing regulatory costs of DB plans introduced by ERISA—rather than their inherent preference for pensions which grant a lesser degree of labor market protection and allow for greater stratification of benefits toward high-income earners—that change was in no small part a consequence of their previous efforts to concentrate private plans under employers’ control. If the sea change in private pensions was a form of institutional ‘drift,’ it was also one guided by firms.

Guided Institutional Drift

I have described the way that decreasing union density paved the way for the switch from defined benefit to defined contribution pensions, and argued that employer associations played an integral role in creating this institutional environment. Still, the perceptive reader will no doubt point out that I have not proved any larger intentionality on the part of firms; even if they wished to consolidate power over private pension management, this chapter has not yet shown explicitly that they did so to reduce labor market protections, limit old age insurance to high-income earners as ‘fringe’ tax-advantaged benefits, or generally reduce payroll costs. But well before the genesis of the 401(k) in the early 1980s, employer groups discussed the future of private old age pensions in terms that strikingly foreshadow what would come to dominate the pension landscape. In this sense, the 401(k) was an innovation only in the strictly legal sense,
opening the doors to a more ‘flexible’ variety of private pensions that firms had already imagined implementing for quite some time.

As early as 1949, the U.S. Chamber of Commerce was publically advocating for contributory old age pensions that sounded very much like the 401(k)s they would later become key proponents of. The Chamber’s *Labor Relations Letter* from October of that year included an entire section entitled “Should The Worker Contribute?,” rhetorically asking, “Should welfare benefits be earned, at least in part, or should they be put up on a something-for-nothing basis, as advocates of the welfare state would like to set them up”? Industry’s position, it maintained, was “clear identification of the individual’s benefit with the contribution he has made.” The newsletter went on: “In addition to the matter of individual independence and dignity, there is the fact, in dollar and cents, that if worker contributions are added, more generous benefit payments become possible.”79 The paean to encouraging individual responsibility would become a crucial argument in favor of 401(k)s—and in opposition to ‘the welfare state’ more generally—in the late 1980s. And the Chamber’s messaging was not an aberration, but evidently the beginning of a longer campaign; the following *Labor Relations Letter*, published in December 1949, noted, “it should be pointed out the present national policy of Congress, some unions, and the policy of many employers favor a contributory [pension] plan.”80 Even before changes to tax law made defined contributions plans

79 “*Labor Relations Letter* no. 64,” October 1949. U.S. Chamber of Commerce Papers, Series IV, Box 71, Hagley Museum & Library, Wilmington, DE.
especially attractive to firms, employer associations were already strongly advocating for
their instatement in place of defined benefit plans.

The National Association of Manufacturers echoed the Chamber’s stance on DC pensions in the 1950s. A 1958 report entitled *A Fresh Look on Retirement Security* offered a rosy vision of “worker capitalists”:

> In the future years as workers become well informed in personal security matters generally, and even better able to fend for themselves, may not the company and industry (and perhaps government) group insurance programs assume a subordinate place or even a voluntary status?…These measures…would create a host of new capitalists, able for the first time to put substantial sums to work at their own discretion.\(^81\)

An internal report written by NAM that year framed the proposition more starkly, as a way of shedding employer pension obligations: “utmost consideration,” it wrote, “should be given to incentives for individuals to provide for their own security in old age.”\(^82\)

In the 1960s, NAM argued that pensions should be developed so as to bind workers to labor market participation, through “reliance on expansion and improvement of the private enterprise economy to minimize the number of aged who become dependent.”\(^83\)

An earlier draft of that policy statement—scrapped by committee for being too harsh—opposed proposals to expand Social Security because they might offer “inducements not to save and work.”\(^84\) DC private pensions, administered by employers but supported by employee savings, were in the minds of business leaders well before the 401(k) revolution.

---

\(^81\) McCarthy, *Dismantling Solidarity*, 90.
\(^82\) Ibid., 133. Emphasis added.
\(^84\) “Proposed Amendments and Additions to the Employee Health and Benefits Section of ‘Industry Believes,’ as Approved by the Public and Private Benefits Subcommittee.” See supra note 68.
As noted above, ERISA is generally considered to be a ‘push’ force that motivated firms to switch to DC pensions because of the increasing costs it imposed on administering DB pensions. But the Chamber of Commerce’s rhetoric in opposition to the legislation suggests that this change was already in the making. Warning that “excessive new legislation could put private pensions into a straightjacket of costly and unnecessary controls,” one pamphlet offered “two great ideas” as alternatives. The first was to “increase the present tax deferral for pensions for the self-employed.” A second was to grant tax-advantaged status to employees who worked for firms without private pensions and saved for their own retirement. Both aimed for “the Federal Government [to] encourage people to save for retirement” themselves, without the expectation of an employer-provided safety net.85 In short, the twin legal developments of ERISA and the 401(k) loophole made the switch to DC pensions possible. But it was a longstanding desire on the part of employers to move to plans based on employee contributions—and the simultaneous muzzling of organized labor as a countervailing force—that made the DC switch probable.

Additionally, while ERISA’s regulatory requirements increased the costs of maintaining DB pension plans, its other provisions actually made it easier for firms to abandon them in favor of 401(k)s. Title IV of the statute created a federal Pension Benefit Guaranty Corporation (PBGC), which insures DB pensioners against the risk of pension fund insolvency. The Corporation is funded by mandatory annual insurance premiums on DB plans, paid at a rate set by Congress, as well as income from pension

85 “Will There Be a Private Pension in Your Future?”
assets under the Corporation’s trusteeship. Though not supported by general revenues, the PBGC is often believed to have the U.S. government’s implicit backing in the event of a major default. This scenario is no mere hypothetical, as the PBGC’s current liabilities exceed its total assets by over $75 billion. The Corporation’s shortfall is largely due to the way employer-run pension plans have taken advantage of it since the passage of ERISA. For one thing, the PBGC is structured in such a way so as to create a moral hazard dilemma that incentivizes employers to underfund DB pensions. And ERISA’s arcane rules about measuring a fund’s actuarial value allows its manager to significantly underestimate potential liabilities. More importantly, firms have also used the PBGC as a way to ‘dump’ unwanted DB plans, shifting massive unfunded liabilities onto a public corporation and creating an opportunity to switch to more desirable 401(k) plans. This strategy was employed repeatedly by the airline industry after the terrorist attacks of September 11th, 2001, when Delta, TWA, United, and U.S. Airways all entered bankruptcy proceedings and spun off major pension liabilities to the PBGC. In the case of United, the company’s four pension plans were

---

88 Brown, “Guaranteed Trouble,” 189-90. These rules allowed Bethlehem Steel’s pension fund—the second largest the PBGC has ever bailed out, with $3.6 billion in claims—to “report a funding status of 84 percent, despite having a market value of assets that, upon termination, equaled only 45 percent of the market value of the plan’s liabilities.” Legislation passed in 2006 partially addressed some of these concerns. Ippolito theorizes that a firm may deliberately underfund its DB pension fund, despite the tax advantages of increasing contributions, to establish a ‘bondholder’ relationship between the firm and its employees that establishes them as stakeholders in the long-term success of the firm. See Richard A. Ippolito, “The Economic Function of Underfunded Pension Plans,” *The Journal of Law & Economics* 28, no. 3 (October 1985).
89 C.f. Tobias Fünke: “Well, I don’t want to blame it all on 9/11, but it certainly didn’t help.” Large steel and aluminum manufacturers have also adopted a similar strategy. The PBGC had a consistently positive net position until 2002, at which point its liabilities began to skyrocket.
underfunded by $9.8 billion, of which the PBGC guaranteed $6.6 billion.90 The remaining liabilities were passed onto United’s pilots, flight attendants, and ground employees, who lost significant retirement assets. Almost all of United’s employees, if they have pensions, now participate in 401(k) plans.

Finally, while the legislation that created 401(k)s had unforeseen consequences (to the Joint Committee on Taxation, at least), Congressional efforts to expand those accounts in recent years have been explicit in their goals. As part of the tax cuts signed by President George W. Bush in 2001, for example, Congressional Republicans increased contributory limits to 401(k) accounts and indexed those caps to inflation for the future.91 In its 2017 legislative plan on retirement security, the Chamber of Commerce advocated for eliminating rules that restrict ‘top-heavy’ 401(k) plans, named because they disproportionately benefit a small number of highly-compensated workers in a given firm.92 And in the discussion of how to address 401(k) contribution limits in the most recent iteration of GOP tax cuts, House Committee on Ways and Means Chairman Kevin Brady (R-TX) described the most important focus as “help[ing] people save more.”93 It is notable that incentives aiming to increase employer contributions to DC plans, encourage uptake for those who do not currently participate, or expand access for low-income earners are wholly absent from the agenda. (For the sake of clarity: an increased contribution cap to a tax-advantaged plan is only

a benefit to someone who already contributes the maximum allowable amount: it does nothing to help the ‘average’ individual save for retirement.) Instead, the aim is to further transform private pension plans from a form of social insurance to a means of offering extra tax-advantaged compensation to high-income earners. Such changes do not involve a budget cut to the welfare state, but because of their (intended) effects, they are indeed a form of retrenchment.

Conclusion

Institutional changes to private old age pensions are far from the only way that the United States has witnessed welfare state retrenchment over the past several decades. This chapter has barely touched upon the evolving character of unemployment insurance and workers’ compensation; the elimination of Aid to Families with Dependent Children (AFDC) and subsequent restrictions on Temporary Assistance for Needy Families (TANF) benefits; the expansion of the Earned Income Tax Credit (EITC) as a way to route social assistance through the tax code; or efforts to couple Medicaid benefits with work requirements (a development that has occurred within days of the authorship of this chapter). Nor has it discussed firms’ efforts to retrench public old age spending, such as through proposals to partially privatize Social Security, raise the minimum retirement age, or means-test benefits. The introduction of individual retirement accounts (IRAs) has functioned similarly to that of the 401(k) in creating an alternative, individually-managed tax-advantaged savings account that
disproportionately benefits high-income earners. Moreover, both types of plans have been used as a means to undercut more equitable and de-commodifying public pensions: Hacker has unearthed a journal article by Heritage Foundation analysts published in 1983 by the Cato Institute (both think tanks funded by many prominent industrialists) advocating a “Leninist strategy” for dismantling Social Security through the expansion of IRAs. The story told here is far from unique, and but one example of U.S. welfare state retrenchment.

The significance of focusing on the development of private old age pensions is that it highlights that the kinds of features typifying a so-called ‘Liberal’ welfare state—dualized benefits, a significant private presence, insurance assets invested in market securities—have become even more stratified in benefit and coverage levels in recent years. Given that industry captains, federal legislators, and even representatives of organized labor have historically offered statements describing the centrality of private pensions to the broader pension landscape, retrenchment of private pension is ipso facto retrenchment of the U.S. welfare state more generally. Critically, this change has not come in the form of a reduction in overall disbursements, but instead an overwhelming switch to a form of retirement accounts that benefit certain high-income workers far

---
94 The creation in 1997 of ‘Roth IRAs,’ named for Senator William Roth (R-DE), offered an even more lucrative retirement savings vehicle for high-income earners: though initial contributions to those accounts are not tax-deductible, they are not subject to capital gains taxes and can be withdrawn at any time without penalty. There is an upper income limit in order to be eligible for Roth IRA contributions, but for a married couple it is $189,000 in combined annual income; Hacker estimates that Roth IRAs generally benefit only the top three deciles of wage earners. In 2006, Congress created a so-called ‘Roth 401(k),’ an employer-sponsored retirement plan with the same tax structure as the Roth IRA. Unlike for Roth IRAs, there is no upper income limit for eligibility to participate in those plans. Hacker, The Divided Welfare State, 164.
95 Ibid., 170; Stuart Butler and Peter Germanis, “Achieving a ‘Leninist’ Strategy,” Cato Journal 3, no. 2 (Fall 1983).
more than others, and require workers to make individual decisions about how much to save, how to invest those savings, and when to begin withdrawing them. The tendency of pensions to offer social-protection—to de-commodify the necessity of one’s participation in the labor market—has thereby been greatly reduced.

Despite the literature describing the creation of 401(k) accounts—in which the great majority of defined contribution pensions are invested—as a historical accident, I have argued that their widespread adoption was far from unforeseeable. Through passage of the Taft-Hartley Act in 1947, in which they were intimately involved, firms sidelined labor unions from pension plan management and weakened their political and bargaining power more generally. This move successful routed a key countervailing power to the widespread adoption of 401(k)s. Though it was not their desire to do so, wholesale control over pension management created the conditions wherein firms were forced into costly fiduciary obligations and other regulatory burdens in operating DB plans, further incentivizing the move to 401(k)s. The legislation that introduced those requirements also offered an inexpensive way for firms to make the switch by dumping pension liabilities onto a federal insurance corporation. Moreover, I have shown that while the legal instrument of the 401(k) was a genuine innovation, the goal of encouraging worker retirement savings in place of firm-guaranteed benefits was a long-term priority of employer associations well before that ‘accident’ of history. There was no singular moment, no piece of legislation or rulemaking, which codified the 401(k) as a replacement for the DB pension plans of yore. But even though private pension changes occurred through a kind of institutional ‘drift,’ it was one intentionally guided by firms.
A notable consequence of this case study, if one is convinced by the narrative I have offered, is that while the individual agency in welfare state retrenchment is clearly sourced to firms, the origins of their involvement in retrenchment are traced to the 1940s. This clearly precedes the temporal period of the ‘logic of post-industrialism’ described in chapter 2, as well as the unique structural conditions that characterize it.\textsuperscript{96} Indeed, that period is not one ordinarily associated with increasing globalization or mass movement from industrial to service work. One therefore might reconsider the working hypothesis: either U.S. firms’ motivation to weaken de-commodifying welfare state institutions is a consequence of endogenous change, or very different exogenous forces than the ones previously offered. Alternatively, perhaps firms’ motivation to reduce the de-commodifying character of private pensions—though they themselves were instrumental in establishing them—was essentially constant over time, merely surfacing when firms had the political power to implement such changes. Regardless of how one resolves this question—the underlying basis of institutional change—it is evident that firms are central to the ongoing evolution of the American welfare state. And it is equally clear which direction this evolution has taken.

\textsuperscript{96} This finding echoes previous work I have done tracing the roots of neoliberal policies in a very different sphere of political economy—urban planning—to an earlier period than usually considered. See Joel Michaels, “Hollowing the City: Federal Policy and Urban Space in Washington, D.C.,” (unpublished manuscript in the author’s possession, 2016).
4 Unemployment Insurance and the Erosion of the German Model

Introduction

In the comparative political economy literature, the case of post-war Germany receives an unusual degree of attention. Not only is the country the largest economy in Europe, a dividing line between ‘East’ and ‘West,’ and the most important political force within the European Union, it is also seen (along with Japan) as a prototypical example of ‘non-liberal capitalism’ in action. In contrast to the diffuse markets for worker skills and investment capital in countries such as the United States, German vocational training and corporate finance systems were historically marked by a high degree of coordination. Relations between labor and capital more broadly were mediated through corporatist bargaining, with wage levels largely decided through high-level binding agreements covering entire industries. The welfare state in Germany follows a similar pattern. Though social insurance programs are administered by the state, they were historically funded through payroll tax contributions paid in equal measure by workers and employers. Industrial relations are at the core of the German welfare state: wage levels negotiated through corporatist bargaining determine not only how much individuals contribute to social insurance funds, but also how much they can expect to receive from them in the event of hardship.

Over the past several decades, the German industrial relations model has significantly eroded, and the strength of the welfare state along with it. This can be
especially observed through the declining generosity of unemployment insurance benefits and the proportion of workers eligible to receive them. To some extent, these changes are natural consequences of an increasingly post-industrial economy and the challenges brought by re-unification with the former Communist German Democratic Republic (GDR). Those developments have resulted in an increasingly dualized labor market—characterized by a large segment of low-wage, low-skill workers—and strengthened employers’ bargaining power in negotiations. But the retrenchment of unemployment insurance has also been codified through German federal law, especially the Hartz reform legislation of 2002-3 enacted during the Chancellorship of Gerhard Schröder. Those laws reduced the amount of time a worker can stay on unemployment insurance, limited the conditions under which a worker can refuse undesirable employment, reformed social assistance to make it more means-tested, and expanded a category of ‘marginal employment’ job contracts without rights to unemployment insurance. They were accompanied by a shift in the overarching normative goal of the German welfare state, moving from policies with an (albeit conservative) understanding of social protection to ones aimed at pushing individuals onto the labor market.

With an eye toward the rational choice institutionalists who argue that German firms play a pivotal role in supporting a stable institutional configuration in that country—the welfare state included—this treatment highlights the ways that firms have instead supported welfare state retrenchment and a move towards a more ‘Liberal’ institutional model. They have done so directly, through public relations campaigns and political muscle-flexing in favor of the Hartz reforms. They have also done so indirectly, in their preferences for decentralized collective bargaining agreements and
highly flexible job contracts that limit access to benefits and curtail the power of trade
unions as a countervailing force to resist welfare state retrenchment. Though not the
exclusive agents of German welfare state change, firms and their representative
associations have been critically important ones, without which social policy in that
country would look very different.

Unemployment insurance holds a particular significance relative to other facets
of the German welfare state, which merits its discussion here. According to the rational
choice institutionalists, the wage protection unemployment insurance grants workers
incentivizes them to develop skills specific to particular industries, thereby sustaining
Germany’s specialized manufacturing sector. Should a worker be laid off from a highly
specialized job, this theory maintains, she or he could draw upon many months of
insurance benefits at a relatively high wage replacement level in the time it takes to find
similar employment.¹ Yet the effective value of unemployment insurance benefits has
dropped significantly, and therefore presumably the incentive for workers to develop
specific skills. Critically, this change has occurred in no small part due to the conscious
efforts of firms in that very specialized manufacturing sector. Their actions have not
only sped the dualization of the German labor market but resulted in growing job
precarity even for those workers in the economy’s industrial core.

The last chapter focused on privately distributed social benefits meant to
support individuals in old age; in this chapter, I look at publically distributed ones

¹ Margarita Estévez-Abe, Torben Iversen, and David Soskice, “Social Protection and the Formation of
of Comparative Advantage, ed. Peter A. Hall and David Soskice (Oxford: Oxford University Press,
2001).
meant to support individuals in while they are still in the labor market. While running the risk of disorienting the reader, this choice of case studies is intentional. It is meant to demonstrate how very different segments of welfare states have all undergone a kind of retrenchment. Moreover, the case studies are intended to explore changes to forms of social policy considered archetypical of multiple ‘diverse’ political economies. By its conclusion, this chapter will attempt to show how a key example of the ‘Coordinated’ or ‘Conservative’ welfare state model (depending on which typology one draws upon) is not only in the midst of retrenchment but drawing closer to the institutional configuration of a ‘Liberal’ welfare state.

Surveying the Landscape

The German welfare state is arguably the oldest in the industrialized world. After the unification of Germany under Prussian hegemony in 1871, Chancellor Otto von Bismarck began a campaign to introduce worker protections that would quell social unrest and reduce emigration to countries like the United States. Bismarck forced through the Reichstag sickness insurance legislation, in 1883; accident insurance, in 1884; and old age insurance, in 1889. His aim, as described in chapter 1, was to establish a social safety net without significantly redistributing resources or destabilizing class hierarchies: hence the classical description of Continental welfare states as ‘Conservative.’ Consequently, all three insurance programs paid benefits in relationship to past wage earnings. The former two were funded exclusively by firms

---

2 Bismarck also aimed to deprive his socialist political rivals of a key issue with which to contest his authority.
and their employees, without any supplemental government revenues. Unemployment insurance, established in Germany during the Weimar period, was constituted along similar lines. The German social safety net also centers upon the protection of male breadwinners within a tight single-family structure, a tradition that contrasts with the support for single mothers and needy children (however limited) typical of the U.S. and British welfare states. In sum, German social insurance is inextricably linked to the character of the German labor market: a nexus that will greatly inform the analysis later in this chapter.

Though confined to a subsection of the overall population, long-term unemployment insurance (Arbeitslosengeld) in Germany has historically been extremely generous to its beneficiaries. At its heyday in the mid-1970s, unemployed Germans were entitled to monthly benefits of up to 68 percent of their previous wages, plus assistance in finding a new job and funding for relevant training.\(^3\) Despite some changes to benefit calculations in the intervening years, insurance benefits have remained relatively high. And prior to recent reforms, unemployed Germans were entitled to a constant level of unemployment benefits pegged to their past wages for up to three years. In 2002, a 40-year-old worker newly entering the unemployment rolls could expect a monthly benefit totaling 61 percent of his previous wage, and the same benefit in his 32\(^{nd}\) month of unemployment.\(^4\) Though many other countries offered their


\(^4\) I have generally attempted to use gender-neutral language when describing hypothetical workers, but the usage of male pronouns in this chapter is intentional, aiming to reflect the patriarchal structure of the German welfare state.
unemployed higher initial benefits, no other OECD country provided as large a benefit for such a prolonged period. At that time, workers who had exhausted their time on the unemployment rolls were entitled to unemployment assistance (*Arbeitslosenhilfe*), an intermediate-level benefit of potentially unlimited duration that was partially means-tested but still closely pegged to past earnings. At the bottom of the hierarchy, those ineligible for unemployment insurance due to lack of previous contributions could apply for social assistance (*Sozialhilfe*), an entirely means-tested benefit administered by and funded through local municipalities. In short, German unemployment benefits have always been dualized and strongly tied to employees’ past wages (or lack thereof). But the degree of dualization, in contrast, has not remained constant.

Because German unemployment insurance payouts can be so generous, the program has been used as a way to soften the blow of job losses due to globalization and technological change. (See figure 4.1.) The long duration of monthly unemployment benefits offers workers the time to retrain for work in a different industry, or even a way to simply stay afloat until they are eligible to begin collecting old age pensions. Not incidentally, the way that German firms have capitalized upon government-subsidized early retirement programs as a way to shave their workforce in response to cyclical downturns reflects a similar usage of the welfare state to compensate

---


surplus labor. The reliance on unemployment benefits has come at significant cost, however. By 2003—the year of major systemic reforms—federal contributions to the unemployment assistance program totaled €16.5 billion, nearly one-third of that program’s total expenditures; federal subsidies to the unemployment insurance program, initially intended to be funded solely through payroll contributions, came to 11.7 percent of its expenditures. The state has also employed budgetary workarounds, such as diverting resources from the old age pension funds to the unemployment insurance ones, and vice versa, to shore up gaps in funding.

If the German federal government has had to shuffle money around to fulfill claims on unemployment insurance benefits, the lion’s share of the burden has fallen on firms and their employees who jointly fund the programs through payroll tax contributions. Throughout the 1960s and early 1970s, unemployment insurance contributions never rose above 2 percent of the wage bill, and total social insurance contributions stayed below 30 percent of labor costs. By 2003, the unemployment contribution rate more than trebled to 6.5 percent of wages, and total contributions reached more than 40 percent. The steadily increasing contribution rate squeezed firms twice-over, as they were not only responsible for paying half of the insurance tax outright, but also had to address trade union demands to increase wages so as to keep real take-home pay constant. One way for firms to reduce payroll taxes was to seek a

---

10 Ibid., 177.
reduction in the value of claims to the unemployment insurance funds. Of course, as I will show, this policy goal had the additional effect of weakening the bargaining position of organized labor, and further imperiling the labor market position of those not represented by unions.

### Figure 4.1 Unemployment in Germany, 1975-2016

![Graph showing unemployment rates in Germany from 1975 to 2016.](image)

Despite the many veto points to institutional reform in Germany, such as the historic strength of trade unions in tripartite negotiations and the federalist character of its national government (where representatives appointed by each of the sixteen Länder states make up the Bundesrat, or upper legislative house), the generosity of the German welfare state began to deteriorate around the turn of the century. In 1997, the

---

Bundestag passed the Labour Promotion Reform Law, which tightened the criteria under which an unemployed individual could refuse a job offer and still continue to receive long-term benefits: any job offering at least 70 to 80 percent of his previous wage (depending on how long the worker had been unemployed) was sufficient to cut off benefit disbursements.\textsuperscript{12} Even stricter ‘workfare’ requirements were also widely introduced at the municipal level. While the average net replacement rate of unemployment insurance had been declining since the 1970s—alongside that of old pensions—the federal government froze unemployment benefits from 2000 to 2002 so that they were no longer pegged to increases in real wages.\textsuperscript{13} Streeck attributes these changes to fiscal “exhaustion” of the federal government, no longer able to use social policy to compensate those whose jobs had been rendered obsolete.\textsuperscript{14} But as I will demonstrate, firms also played a crucial role in limiting the guaranteed right to unemployment compensation, seeking both to reduce their payroll costs and flood the labor market with relatively low-wage workers.

Changes to German industrial relations, while technically outside the scope of social policy, will also be a component of this case study. They have not only resulted in the weakening of labor unions as a political force to contest welfare state retrenchment, but have also threatened the solvency of the unemployment insurance funds and shrunk the number of workers who can claim benefits from them. The

\textsuperscript{13} Streeck and Trampusch, “Economic Reform and the Political Economy of the German Welfare State,” 184.
\textsuperscript{14} Wolfgang Streeck, Re-Forming Capitalism: Institutional Change in the German Political Economy (Oxford: Oxford University Press, 2009).
German collective bargaining ‘model’ has declined gradually rather than in punctuated bursts, and there is no analogous piece of anti-labor legislation to the Taft-Hartley law in the United States. But the trend is nonetheless unmistakable. Industrial relations in the German manufacturing sector, historically a trend-setter for that of the rest of the economy, rested upon sectoral collective agreements with major trade unions, combined with smaller ‘works councils’ comprised of employees at the firm level. Because high-level negotiations set standards for wages and benefits, works council representatives generally had non-adversarial relationships with firm managers, working in tandem to coordinate industrial production. Yet while this bargaining structure may still be considered the German ‘model’, it no longer describes how industrial relations are actually constituted in the majority of German firms.

In 1980, a full 80 percent of workers in West Germany were covered by sectoral collective bargaining agreements. Moreover, such agreements were frequently renewed, with 608 accords (a record high) certified as binding that year. By 2013, however, only 49 percent of workers were covered by sectoral agreements. The proportion of workers covered by the full gamut of collective representation—sectoral collective bargaining agreement plus firm-based works council—has declined even more precipitously,

---

dropping below 15 percent by 1997. Critically, even those workers covered by sectoral agreements are not necessarily entitled to the benefits enumerated therein, because an increasing number of agreements contain “opening clauses” that allow for significant modifications of agreements at the firm level. While it was once an uncommon practice, in 2004–2005, fully three-quarters of all German workplaces invoked such clauses. One 2003 study found that an additional 15 percent of firms violate sectoral agreements illegally. The push for increasing flexibility at the firm level has eroded the notion of works councils as removed from basic wage bargaining (where they still exist, that is: the share of workers represented by works councils has declined even more rapidly than that of sectoral agreements). The last quarter of the twentieth century also witnessed a significant decline in trade union density, which is not unrelated to the erosion of traditional collective bargaining agreements. Indeed, the two phenomena have a reciprocal effect on one another: reductions in union power (through lowered membership dues and organizing strength) hamper labor’s ability to bargain for strong sectoral agreements, while the disintegration of works councils cuts off a critical source of union recruitment. In this sense, the German industrial relations ‘model’ is caught within a vicious cycle that seems to compel its further erosion.

17 Anke Hassel, “The Erosion of the German System of Industrial Relations,” British Journal of Industrial Relations 37, no. 3 (September 1999): 487.
20 “The Erosion of the German System of Industrial Relations,” 488.
The Root Causes of German Institutional Change

The rising cost of unemployment insurance claims and the erosion of the Germany industrial relations model are in part the consequence of the unique circumstances of German reunification in 1990. The demise of the former German Democratic Republic (GDR) meant an end to that government’s industrial subsidies and a great deal of resulting joblessness in the eastern region of the country; the spike in the unemployment rate in the early 1990s is visible in figure 4.1. Indeed, the proportion of unemployment recipients in the former East remains much greater than that of the overall population to this very day. After reunification, many newly unemployed workers were entitled to unemployment benefits from the unified German government, paid through social insurance funds which those workers—by virtue of residing in the GDR—had not initially contributed to. Monthly benefits were calculated in relation to past wages, just as for West German workers, but notably, those wages had been paid in the East German currency. For purposes of international trade accounting, the GDR government valued its Ostmark at a rate of 4.4 per 1 Deutschmark, and black-market exchange rates prior to unification often valued the Ostmark even lower. But in part to limit internal migration after reunification, Helmut Köhl’s government made the currencies convertible at par (one to one).21 Thus, not only were the social insurance funds newly responsible for paying benefits to a large number of claimants, the monthly value of their claims was greatly artificially inflated.

That millstone upon the insurance funds motivated the federal government’s budgetary workarounds discussed above. It also necessitated increasing payroll taxes on workers and employers, which heightened the latter’s incentive to pursue welfare state retrenchment.

Reunification is also responsible in part for the erosion of the German industrial relations model. Collective bargaining coverage is even lower in the former East than in the West, and small- and medium-sized enterprises in that region who can less afford union wage demands have been key advocates for decentralization within German employer associations. The fact that wages are generally lower in that part of the country has also contributed to the growing dualization of the German market, as firms can relocate elements of their production requiring fewer specialized skills to the cheaper East. But the unusual situation Germany faced following reunification should not distract from larger structural conditions motivating welfare state reform and employers’ role within it. Indeed, many of its causes are descriptive of changes to the global economy more generally.

The consequences of financialization of the German economy, globalization, and the changing nature of work have all incentivized German employer associations to reduce pursue welfare state retrenchment so as to reduce their social insurance contributions and liberalize labor markets. In addition to changing industrial relations, for instance, the end of the twentieth century witnessed a substantive challenge to the established model of German corporate governance. Whereas banks were once a key

---

source of capital and institutional stability for large German firms, protecting them from hostile takeovers, a shift in focus towards investment banking meant that firms were rendered more accountable to international shareholders. In 1992, 44 percent of the supervisory board chairs at 40 large manufacturing firms were bank representatives, whereas by 1999 the figure had halved to 23 percent.23 While financial firms like Deutsche Bank were committed to long-term stewardship of the German manufacturing sector (offering so-called ‘patient capital’), equity investors are far more concerned with maximizing short-term returns. The financialization of the German economy therefore gave firms even more reason to suppress labor costs, which they could achieve through welfare state reforms that reduced levels of social protection, forced low-wage workers onto their labor market, and weakened workers’ wage bargaining position.24

The 1990s also witnessed a surge of international competition as a result of globalization, which similarly incentivized firms to pursue welfare state reforms. Outward foreign direct investment (FDI) peaked in 1997 at DM 47.3 billion, representing 1.3 percent of Germany’s GDP. Those investments abroad also tended to be concentrated in the same manufacturing sectors which supported the German export

24 The move from operating firms according to the principle of codetermination (Mitbestimmung) to maximizing shareholder value represents another way in which German political economy has moved to what Hall and Soskice call the Liberal Market Economy (LME) model. For more on the link between corporate governance and the welfare state, see Gregory Jackson and Sigurt Vitols, “Between Financial Commitment, Market Liquidity and Corporate Governance: Occupational Pensions in Britain, Germany, Japan and the USA,” in Comparing Welfare Capitalism: Social Policy and Political Economy in Europe, Japan and the USA, ed. Bernhard Ebbinghaus and Philip Manow (London: Routledge, 2001). See chapter 2 for a definition and further explanation of financialization.
engine at home.\textsuperscript{25} Consequently, the business community and its political allies became fixated on the necessity of addressing the so-called \textit{Standortdebatte}: in essence, ensuring Germany’s competitiveness as a hub of international commerce.\textsuperscript{26} By the same token, globalization has also increased German firms’ market power to dictate the terms of that country’s industrial relations. The relative ease with which German firms can move parts of their supply chain into lower-income countries within the larger European Union (not merely the former East) have forced unions to make bargaining concessions at the margins—such as agreeing to opening clauses—in order to protect benefits for their core membership.\textsuperscript{27} And as Hassel and Williamson note, “unions are concentrated in declining industries and are hardly present in the growing service sector,” which accounts for the majority of labor market growth over the last several years.\textsuperscript{28} The service sector—in no small part because of the dearth of union representation there—has also seen the proliferation of alternative employment contracts with limited social insurance coverage. Those jobs fail to protect workers from the risk of unemployment, endanger the solvency of social insurance funds, and encroach upon the priviledged position of workers in the industrial core who \textit{do} have stronger employment protections—at least for the time being. Contrary to the assumptions of some scholars

\textsuperscript{25} Ian Bruff, \textit{Culture and Consensus in European Varieties of Capitalism: A “Common Sense” Analysis} (Basingstoke, England: Palgrave Macmillan, 2008), 124. This focus dovetailed with the concurrent efforts of politicians and capital-owners in Germany to build up Frankfurt as a center of international finance, which was perceived as requiring significant liberalizations (both of capital accounts and labor markets) in order to attract foreign investors.

\textsuperscript{26} Ibid., 125.

\textsuperscript{27} Germany’s exporting success, it must be noted, has come in no small part because it shares a currency with 18 other European countries with a lower average purchasing power, thereby artificially decreasing the price of German exports. Regulatory harmonization within the European Union has also created a large and streamlined market for German goods. For the reason described above, however, EU rules have also enabled labor market dualization within Germany.

\textsuperscript{28} Hassel and Williamson, “The Evolution of the German Model,” 11.
within the Varieties of Capitalism literature, firms have not resisted this erosion of German industrial relations (and by extension, the welfare state). Rather, just as with the retrenchment of unemployment insurance itself, they have actively spurred it.

The Hartz Reforms

In October 1998, Gerhard Schröder entered the German Chancellor’s office supported by a ‘Red-Green’ coalition of his own Social Democratic Party (SPD) and the environmentally-focused Alliance 90/The Greens. Seeking to reduce high long-term unemployment and corresponding levels of social spending, the government’s initial economic program centered upon an “Alliance for Jobs” (Bündnis für Arbeit). This tripartite body comprised representatives of the Federal government, employer associations, and trade unions, and was tasked with developing policies to promote (among other goals) “a permanent reduction of non-wage labour costs and a structural reform of the social security system, [and] an employment-promoting distribution of work and flexible working time arrangements.”

The talks concluded with relatively little progress, in part because the Schröder government was worried about forcing through reforms that would anger key elements of its political base, such as the trade unions and left wing of the SPD. However, in February 2002, a scandal implicated

---


30 Hassel and Williamson, “The Evolution of the German Model,” 10. The authors elaborate: “Unions had essentially a veto right during the first term of the Schröder government. The government even extended union rights at the workplace. Immediately after Mr. Schröder’s re-election in September 2002, union pressure was seen as the main reason why the ruling coalition’s policy programme contained so few reform ideas.”
the Public Employment Service (PES) in falsification of statistics concerning its record of finding jobs for unemployed individuals.\textsuperscript{31} This gave the Schröder administration political cover to organize a 21 member reform commission well outside the traditional tripartite model, chaired by Volkswagen’s director of human resources, Peter Hartz.\textsuperscript{32} The Hartz Commission’s final report contained 13 recommendations to alter labor market and social insurance rules. With support from its rival party, the Christian Democratic Union (CDU), which controlled the indirectly elected upper house of the legislature, the Schröder administration passed many of these proposal into law under the banner of its new economic program: “Agenda 2010.”

<table>
<thead>
<tr>
<th>Legislation</th>
<th>Date Passed</th>
<th>Date Implemented</th>
<th>Function</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hartz I</td>
<td>December 2002</td>
<td>January 2003</td>
<td>Created temporary work agency; funded vocational training</td>
</tr>
<tr>
<td>Hartz II</td>
<td>December 2002</td>
<td>January-April 2003</td>
<td>Changed definition of ‘Mini-job’ marginal employment category; created ‘Midi-job’ category</td>
</tr>
<tr>
<td>Hartz III</td>
<td>December 2003</td>
<td>January 2004</td>
<td>Reorganized Public Employment Service (PES)</td>
</tr>
<tr>
<td>Hartz IV</td>
<td>December 2003</td>
<td>January 2005</td>
<td>Eliminated unemployment assistance; created unemployment benefit II resembling social assistance; imposed new definitions of acceptable work and sanctions on non-compliance; reduced maximum duration for receiving unemployment insurance*</td>
</tr>
<tr>
<td></td>
<td>September 2003*</td>
<td>February 2006*</td>
<td></td>
</tr>
</tbody>
</table>

\textsuperscript{31} Streeck and Trampusch, “Economic Reform and the Political Economy of the German Welfare State,” 184. According to Streeck and Trampusch, it “had long been widely known among insiders that the statistics of the public employment service...were largely fictional.”

\textsuperscript{32} Ibid. See the next section of this chapter for further discussion of the Hartz Commission’s composition.

The most consequential of these actions was the “Hartz IV” law, passed in 2003, which directly affected the character of unemployment insurance. It reduced the maximum amount of time a worker could stay on that program from 32 to 12 months, and eliminated the middle category of unemployment assistance which offered longer-term benefits proportional to past wages: workers who surpass the 12-month limit are now pushed onto fully means-tested social assistance. For a single-person household in 2014, this Unemployment Benefit II (Arbeitslosengeld (ALG) II) amounted to a monthly lump-sum payment of €391, plus the cost of housing. For reference’s sake, the average monthly wage across Germany that year was approximately €3,025. In addition, the legislation further tightened the criteria for the kinds of jobs an unemployment insurance recipient could refuse for reasons of geography, reduction in wages, or change in profession, and imposed new financial sanctions on those who refused them. This change also contributes to the continual erosion of the German industrial relations model, by compelling unemployed workers to take jobs paying up to 30 percent less than collectively bargained wages. Alongside these ‘sticks’ to push the long-term unemployed onto the labor market, the Hartz reforms contained ‘carrots’ such as funding for wage subsidies and increased job training. At the same time, however, the PES, which administers those programs,

34 Individuals over the age of 55 may continue to receive benefits for up to 18 months.
37 Ochel, “Hartz IV—Welfare to Work in Germany,” 21. The first violation of these rules results in a loss of 30 percent of the unemployment benefit for three months; repeated violations can result in the elimination of the benefit entirely.
was modernized [through the “Hartz III” legislation] to initiate the transformation from a public bureaucracy to a public company, with management structures comparable to private companies. Accordingly, the tripartite management board and the presidency were replaced with a corporate-like board of three managers nominated by the government.38

The old management board, which the civil servant who ran the PES directly reported to, included representatives of German social partners such as the trade unions. After the Hartz reforms, those partners were given “informational rights” as to the PES’s activities but limited executive authority.39 The balance of power within the agency thus shifted away from organized labor and towards the appointees of a government working (as will soon become clear) in close collaboration with German employer associations.

Ultimately, the goal of Hartz IV was to reduce unemployment—and, correspondingly, the high payroll taxes needed to sustain the unemployment insurance funds—by strongly incentivizing unemployed workers to find a job, even if a significantly less desirable one than their previous employment. The policy thus represents an important move away from the Bismarckian origins of German social insurance, not only in its material benefits, but also in the rejection of the principle that social insurance should be used to protect individuals’ social status. Seeleib-Kaiser describes this governmental commitment as “the key normative principle of the German welfare state in the post-war era.”40 That normative stance has indeed eroded, because the relocation of the long-term unemployed onto means-tested social

39 Kemmerling and Bruttel, “New Politics‘ in German Labour Market Policy?,” 4
assistance programs reinforces the notion that those workers are in fact a societal burden. As Promberger argues:

‘Hartz IV’ has turned into a catchword to describe persons and social settings where negatively perceived immigration, educational disadvantages, inherited labour market remoteness and delinquency problems among youth concentrate in urban problem areas. Thus, the public debate on poverty in Germany keeps swinging from mercy for the poor and unemployed towards blaming the supposedly idle and back again in terms of sometimes just a few months, again reproducing medieval distinctions between the deserving and the undeserving poor.\(^{41}\)

In sum, German unemployment insurance reforms mark a substantive shift in the general character of the welfare state in that country. Not only have social policies moved away from their historical origins and corresponding normative goals, they have also moved towards a more ‘Liberal’ institutional configuration, with a high degree of benefit dualization and means-tested assistance (rather than insurance) for the most downtrodden.

The “Hartz II” law passed in 2002 also addressed labor market rules by modifying alternative kinds of employment contracts; the implications of these reforms for the welfare state are well worth considering. The most important change was to the statutory definition of the so-called ‘Mini-job,’ a technical type of marginal employment that has existed in some form or another since 1977. Mini-jobs were initially intended to provide a motivation to enter the labor force for individuals such as students, homemakers, and the elderly, who might not otherwise do so because of the high social insurance contribution in the German wage bill.\(^{42}\) While employers who

\(^{41}\) Promberger, “Nine Years of Hartz IV—a Welfare Reform under Scrutiny,” 43.

hire Mini-jobbers pay a total of 30 percent of labor costs in payroll taxes, employees’ take-home wages are fully tax-free, including a waiver on income tax.\textsuperscript{43} This enables employers to pay lower wages than they would otherwise be able to, thereby pocketing some of the tax subsidy themselves. And though the tax burden on employers is relatively high compared to normal employment contracts, in which they pay 21 percent of wages (half of the total payroll tax bill), total social insurance contributions are still lower than they would otherwise be, because the employer payment excludes unemployment insurance. Employers are also frequently able to reduce labor costs through Mini-job contracts by denying those part-time workers holiday and sick pay, though they are legally entitled to them.\textsuperscript{44} Already a common type of employment contract before the twenty-first century, the Hartz reforms took this welfare-state-adjacent category and expanded it dramatically.

Prior to 2003, an employment contract could only receive the tax-advantaged status of a Mini-job if the employee earned less than €325 per month and worked fewer than 15 hours per week. The Hartz II law raised this threshold to €400 (it has since increased to €450) and, more importantly, eliminated the working hours requirement.\textsuperscript{45} The legislation also introduced an intermediary category of a ‘Midi-job’; rather than levying the full social insurance tax upon a worker earning just over the €400 threshold, workers pay a gradually increasing proportion of their wages, beginning at just 4

\textsuperscript{43} Claudia Weinkopf, “Germany: Precarious Employment and the Rise of Mini-jobs,” in Gender and the Contours of Precarious Employment, ed. Leah F. Vosko, Martha MacDonald, and Iain Campbell (London: Routledge, 2009), 182. The 30 percent figure breaks down to 15 percent for old-age pensions, 13 percent for health insurance, and a 2 percent flat tax.

\textsuperscript{44} Ibid.

percent, for wages up to €800 per month. The Hartz II reform resulted in a dramatic spike in the number of Mini-job contracts, and a more modest number of registered Midi-job contracts. This occurred not only because the legal definition of a Mini-job was expanded, but because the Hartz IV law required those receiving the new social assistance benefit to take up marginal employment, including Mini-jobs, or face a reduction in assistance. Alongside simultaneous relaxation of rules concerning fixed-term contracts, temporary jobs, and work assigned through private employment agencies, the Mini-job reform marked a significant erosion of the German industrial model, and by extension the kinds of social protections to which workers are entitled.

The technical term for a Mini-job is ‘marginal employment,’ so named because it does not provide the range of social insurance coverage offered to an ordinary German worker. Because neither Mini-jobbers nor their employers pay unemployment insurance taxes, they are ineligible for occupational coverage based on past wages, and thus must rely on more meager social assistance in the event that they are out of a job. On the other side of the coin, increasing utilization of Mini-jobbers necessitates reduced contributions to the unemployment insurance funds from both workers and employers, threatening the funds’ long-term solvency. The Hartz reforms were not coupled with any provision to shore up the funds through general revenue or tax increases. Finally, the expansion of Mini-job contracts provokes welfare state retrenchment by further squeezing the German industrial relations model, since the

---


47 Eichhorst and Marx, “Reforming German Labour Market Institutions: A Dual Path to Flexibility.”
German welfare state traditionally offers occupational benefits in proportion to past wages. As Mini-job workers can be paid relatively low wages (subsidized by federal tax exemptions) below those guaranteed in collectively bargained contracts, they have the potential to undercut wage demands and force concessions by workers in the industrial core. Mini-jobbers not only lack strong social benefits themselves, but also jeopardize the availability of benefits for all.

It is important to note that Mini-jobs were an important part of the German labor market as early as the 1980s, well before the Hartz legislation of 2002-3. In this sense, the Hartz reforms should be seen as codifying and accelerating a larger trend in the German political economy, rather than turning it on its head.48 But the change was nonetheless a significant one: within the first three months after Hartz II went into effect, an additional 900,000 Mini-job contracts were registered, and one study attributes over 1.8 million such jobs to the impact of the new law.49 As of November 2017, 7.5 million individuals in Germany have Mini-jobs, representing over one-fifth of the entire labor force. Some 4.7 million of those workers have no other job providing them with social insurance, which prompts them to rely upon multiple Mini-jobs to make ends meet.50 Approximately three-quarters of Mini-jobbers are women—frequently those who would otherwise be homemakers—and the positions are concentrated in service sector work. Industries which rely upon flexible scheduling,

---

48 For more on this point, see Joachim Möller, “Did the German Model Survive the Labor Market Reforms?,” *Journal for Labour Market Research* 48, no. 2 (August 2015).
such as restaurant and hospitality firms and construction contractors, rely particularly on Mini-jobbers, and some 40 percent of cleaners work under such contracts. But the impact of Mini-job growth is far from limited to one sector of the economy. For one thing, the German service sector has produced the great majority of new employment opportunities in that country. And in response to international competition, German industrial firms have sought to outsource or contract out less productive components of their manufacturing processes, the erosion of the collective bargaining model, and increasing management flexibility at the firm level, means that firms can replace such work with Mini-jobbers. Indeed, just as for the retrenchment of unemployment benefits per se, firms have also been key advocates for the expansion of Mini-job contracts excluded from unemployment insurance coverage. The next section of this chapter highlights these efforts.

The Role of German Firms in Welfare State Retrenchment

German employer associations representing many of the country’s largest and most important industrial firms were instrumental in the conception and passage of the Hartz reforms describe above. As Daniel Kinderman has convincingly shown, they did so through the funding of public policy advocacy groups like the New Social Market Initiative (Initiative Neue Soziale Marktwirtschaft), or INSM. He argues that the 1996

---


federal debate over reforming sick pay rules, and an influential 1999 poll showing popular support for the welfare state among Germans—as well as “skepticism” and “fear” about potential cuts—convinced employers of the need to fund a strong public relations campaign in favor of economic reforms.53 In 2000, the federation of regional metal and electrical employer associations, Gesamtmetall, established the INSM with an annual budget of €10 million, much of which was used to hire the advertising firm Scholz & Friends.54 In 2002, the INSM coined the slogan that became Minister of Economics and Labour Wolfgang Clement’s rallying call for Agenda 2010: “Sozial ist, was Arbeit schafft,” or “Just’ is whatever creates work.”55 (More on Clement, and his ministry, in a moment.) A 2003 slogan offered: “Less welfare state means more jobs,” and

In 2004, the INSM placed a sign that read: “It’s high time for reforms: GERMANY” at a prominent place in the Spree river in Berlin. The sign was hung so that GERMANY was half submerged under the water, to symbolize the gravity of Germany’s situation.56

INSM-associated figures also blanketed German talk shows and newspaper opinion pages. As Max Höfer, a former director of the INSM, has stated, “We did Schröder’s

---


56 Ibid., 136.
Höfer also claimed that around the time of the Hartz reforms, the INSM “had public opinion leadership,” and major German political commentators agree: the Heidelberg political scientist Manfred G. Schmidt describes the INSM as “the most influential lobby that market-liberals ever had in Germany.”

It used this muscle for the task of pushing through welfare state reforms. 

_Gesamtmetall’s_ motivation for advocating reforms through the INSM was a desire to reduce social insurance costs and push large numbers of low-wage workers onto the labor market. As Ulrich Brocker, a former managing director of _Gesamtmetall_ and the founder of the INSM, offered in an interview with Kinderman, “contributions to unemployment insurance became more expensive, competition was growing and the pressure became harder…Eventually the advantages that Germany enjoyed were used up.”

According to the prominent newsmagazine _Der Spiegel_ (roughly analogous in importance to the _New Yorker_ in the United States), _Gesamtmetall’s_ efforts were joined by at least 24 other advocacy groups lobbying in support of labor market and welfare state reform. These efforts were not limited to reforming policies peripheral to the German ‘model.’ In fact, the INSM published an article in the major national broadsheet newspaper _Die Welt_ criticizing the principle of codetermination. This runs contrary to Thelen’s claim that German employers wish to preserve the institutions of corporatist wage bargaining on the sectoral level and works councils oriented to

---

57 Ibid., 139.
58 “Challenging Varieties of Capitalism’s Account of Business Interests,” 4, 12.
59 Ibid., 8.
61 Thelen, “Why German Employers Cannot Bring Themselves to Dismantle the German Model”; Kinderman, “Challenging Varieties of Capitalism’s Account of Business Interests,” 12.
codetermination of production at the firm level. By 2005, the INSM was focused on defending the Hartz reforms from popular pushback, and even argued that “Germany needs a comprehensive program of market-oriented reforms that goes considerably beyond Agenda 2010.”\footnote{“Challenging Varieties of Capitalism’s Account of Business Interests,” 14.} That these efforts stemmed from an agent of firms in the metal and electrical industries, the paradigmatic sector of the German economic model, indicates the keen focus of German firms on welfare state retrenchment.

The public officials who spearheaded reform efforts were also closely tied to business interests. As the Schröder government took office in 2002, it dissolved the Federal Ministry of Labour and Social Affairs—which, according to Pühringer and Griesser, was “was traditionally closely affiliated to representatives of the employees in both of the major parties”—and merged it with the Federal Ministry of Economics and Technology.\footnote{Stephan Pühringer and Markus Griesser, “Has Economics Returned to Being the ‘Dismal Science’?: The Changing Role of Economic Thought in German Labour Market Reforms,” Institute for Comprehensive Analysis of the Economy (ICAE) Working Paper Series, no. 49 (2016), 7.} The politician appointed to run the new ‘super-ministry,’ Wolfgang Clement, strongly contrasted the left-wing of the SPD (such as Minister of Finance Oskar Lafontaine) in his sympathy for private industry. While he served Minister-President of the Länder of North-Rhine-Westphalia prior to joining the Federal government, Clement earned a reputation for “his willingness to accommodate business interests on issues such as the loosening of dismissal regulations, and acceptability criteria for jobs.”\footnote{Sabina Stiller, Ideational Leadership in German Welfare State Reform: How Politicians and Policy Ideas Transform Resilient Institutions (Amsterdam: Amsterdam University Press, 2010), 169.} After leaving the Federal government, Clement joined the supervisory board of DIS AG, a private temporary employment agency that enables the
further erosion of standard employment contracts with rights to social insurance benefits.65 (Not to mention the fact that Clement had previously been charged with regulating firms like DIS AG.) Most strikingly of all, in 2012, Clement was appointed chair of the Board of Trustees of INSM, the advocacy group who ran the public relations campaign for the Hartz reforms he shepherded through the Bundestag.66 As of early 2018, he remains its chair. Though the Schröder administration took the lead in implementing the recommendations of the Hartz Commission, it did so in clear collaboration with business groups.

In contrast, the declining institutional power of German trade unions limited both their role in influencing the reforms advocated by the Hartz Commission, and their ability to prevent the reforms’ passage through the German legislature. The reorganization of the Ministry of Labour, cutting off a key way in which unions had influenced ruling governments, is one institutional manifestation of this trend. The composition of the Hartz Commission is another. As alluded to earlier, the Hartz Commission’s structure broke from the traditional tripartite model of the previous Alliance for Jobs. Of its 21 members, only two were representatives of trade unions, while prominent firms like Daimler-Chrysler, BASF, Deutsche Bank, Roland Berger, and McKinsey & Company (the latter two management consultant firms) were each represented individually.67 The influence of the ‘social partners’ within the Commission was therefore extremely limited, and the Commission’s ultimate proposal was much

less favorable to workers than any that would have been produced by the Alliance for Jobs.

Though highly controversial among the broader public, the four Hartz bills sailed through the German legislature with relative ease. That they were passed by the upper Bundesrat, controlled by the then-opposition Christian Democratic Union (CDU) party, is attributable to “pressure from business” on the CDU’s leaders and the declining importance of the party’s social wing, which historically had strong ties to Christian trade unions. The waning influence of German trade unions also explains the Hartz reforms’ relatively strong support within the SPD. While Schröder had been reticent to displease the party’s trade union constituencies early in his tenure (even increasing social insurance coverage for Mini-jobbers in 1999), the 2002 PES scandal changed his political calculus, and the Chancellor ran for reelection that year on a platform to implement all of the Hartz Commission’s recommendations. When the SPD-Green coalition won an unexpected majority, Schröder largely followed through on this commitment; major protests organized by the German Trade Union Confederation (Deutscher Gewerkschaftsbund, or DGB), objecting in particular to Hartz IV, were “all but ignored.” Other observers contend that the majority of the over

70 Stiller, Ideational Leadership in German Welfare State Reform, 156.
100,000 individuals who protested the passage of Hartz IV—most of them in the high-unemployment areas of the former East—were mobilized by grassroots action rather than trade unions. Of course, declining union power is inextricably linked to the changing character of German industrial relations, a shift in which firms also played a critical role.

The idea that German firms have actively sought to disassemble their country’s prototypical employment ‘model’—by moving to decentralized negotiations with works councils rather than trade unions, and relying on low-wage, low-skill labor—has been fiercely contested in the existing literature. Indeed, were it true, this observation would challenge the rational choice institutionalist account of how Coordinated Market Economies (CMEs) function according to their own differentiated logic. But while they may not have sought to do so during the halcyon days of the Wirtschaftswunder, the post-war ‘economic miracle,’ German firms are primary agents of this shift today, resulting in both labor market dualization and welfare state retrenchment. As Eichhorst and Marx argue, while marginal employment contracts have been part of the German legal code in some form or another since 1945, “in the 1980s and 1990s employers increasingly perceived such contracts as a strategic option to circumvent social insurance contributions and establish a low-wage segment of the labour market.” In the 2000s, this perception morphed into a concerted push for policy action.

71 Kemmerling and Bruttel, “‘New Politics’ in German Labour Market Policy?,” 104-5.
72 Eichhorst and Marx, “Reforming German Labour Market Institutions: A Dual Path to Flexibility,” 77.
The loudest voices advocating for labor market segmentation are those at the periphery of the German export machine. Service sector employers such as those in hospitals and retail establishments have been among the strongest proponents of the expansion of Mini-jobs, as has the ‘classical liberal’ Free Democratic Party (FDP), which represents many small- and medium-sized business owners. Firms in the former East, which tend to be smaller and less profitable than their counterparts in the former West, have been especially fierce proponents of decentralization of collective bargaining, because they lack the large workforces and human resource departments required to take advantage of the work-sharing and flexibility provisions built into sectoral agreements. As Czada notes, these firms have particularly “privileged access” to state governments in the eastern Länder, and have pushed for collective bargaining decentralization at that level. Disputes within trade associations over whether or how strongly to support decentralization has resulted in the exodus of some smaller firms from organizations like Gesamtmetall. This trend has prompted some scholars to describe ‘disorganization of business,’ rather than declining trade union power, as an underlying cause of the erosion of German industrial relations. But as noted above, it was Gesamtmetall that funded the INSM’s public relations campaign in favor of the expansion of Mini-jobs. The Initiative even argued against the supposed core pillar of the German industrial ‘model,’ codetermination. Since social policy benefits in

---

74 “Why German Employers Cannot Bring Themselves to Dismantle the German Model,” 143.
76 See, especially, Thelen, “Why German Employers Cannot Bring Themselves to Dismantle the German Model.”
Germany are so closely tied to a worker’s wage bill and occupational status, expanding the low-wage segment of the labor market—at the expense of standard employment contracts—necessitates retrenchment of the welfare state.

**Conclusion**

The German welfare state is distinct from those in Anglo-American or Nordic countries; it should even be distinguished from those in other Continental countries, like France and the Netherlands, with which it is often grouped. Its core normative principle is that German workers should be protected from the risk of destitution by insurance, in proportion to their past wage earnings. In this sense, the German welfare state was never particularly ‘de-commodifying’: individuals only earn generous benefits if they previously commanded high wages in the labor market. But this state of affairs still left plenty of room for retrenchment. Not only is the proportion of workers eligible for such benefits declining, through the expansion of marginal employment contracts, the very normative principle underlying the German welfare state is now in question. The core motivation of the Hartz reforms was not to protect German workers from the social ill of unemployment, but to figure out how to get them to re-enter the labor market, even at a much lower social position. Shortening the duration that workers can receive unemployment insurance benefits is just one manifestation of this newfound focus.

It is clear that for workers at the periphery of the German labor market, the availability of social benefits is quite limited (and increasingly so). Moreover, as the service sector expands as a proportion of the German economy, workers with multiple
Mini-jobs or other marginal employment contracts with limited social insurance coverage will become an ever-increasing proportion of the overall population. This alone is enough to show how strikingly the German ‘model’ has changed. Numerous scholars writing within the Varieties of Capitalism framework point to the situation of the archetypical worker at the industrial core of the German economy—a high-skilled, high-income employee of a large net export firm like Siemens, who learned his trade through a vocational apprenticeship at that firm—and suggest that the old model is still intact. This line of thinking is myopic. For one, it describes the position of workers whose segment of the labor market is shrinking, soon to become the exception rather than the rule. And moreover, as firms strive to contract out less skill-intensive components of their production processes to Mini-jobbers and other marginal workers, they will simultaneously be able to employ the threat of employment marginalization in contract negotiations with trade unions. Concurrently, the proliferation of marginal employment contracts contributes to the hollowing out of trade union membership, dues, and organizing power. The looming threat of the ‘reserve army of labor,’ to use Karl Marx’s term, may well force trade union concessions on key bargaining items like wage demands. German welfare benefits, of course, are calculated in proportion to that very wage bill: the logical circle of retrenchment is completed, with firms at its very center.

All this is not to say that German welfare state retrenchment is a unilateral project, conceived and executed by industry associations. The constraints upon state actors should not be underestimated, and others have written extensively on the
perceived fiscal exhaustion of German social insurance funds in the 1990s.\textsuperscript{77} Still more have argued that the Hartz reforms represent a form of ‘policy learning’ by political leaders, who gathered insights from a pilot program set up in 2000 to explore potential reforms to the PES, as well as an expert forum on the welfare state run simultaneously by the Bertelsmann Foundation.\textsuperscript{78} Political leaders are likewise governed by concerns of international competitiveness, and the reformist wing of the SPD in particular was fixated on the idea that Germany’s welfare spending was a drag on labor market performance and economic growth. But the Hartz reforms would not have had the intellectual firepower, the political support, or the underlying sense of urgency that they drew upon were it not for the collective advocacy of firms through industry associations. That they charted this course with such vigor—reversing their prior role in building a corporatist German political economy—should be attributed to the unique structural conditions of the post-industrial era.

I have discussed the retrenchment of unemployment insurance benefits in Germany, as well as the central role of firms in motivating this shift. But the chapter’s scope of inquiry, by virtue of this being a comparative case study, is actually broader than that. For the German welfare state has not merely shrunk to a lesser version of its former self: it has also developed a different set of underlying principles. In both theoretical and practical respects, the German welfare state now appears more like its

\textsuperscript{77} Streeck, \textit{Re-Forming Capitalism: Institutional Change in the German Political Economy}.

\textsuperscript{78} Fleckenstein, “Learning to Depart from a Policy Path: Institutional Change and the Reform of German Labour Market Policy”; Seeleib-Kaiser and Fleckenstein, “Discourse, Learning and Welfare State Change: The Case of German Labour Market Reforms.” The pilot program was entitled ‘Mozart.’
counterpart in the United States. This is visible in the ever-increasing dualization of benefits, in the public stigma newly attached to social assistance recipients, and in the government’s role in subsidizing low-wage (and low-benefit) Mini-jobbers through the ‘submerged state’ of tax exemptions. Both the U.S. and German welfare states are in the throes of profound institutional change. And to a striking extent, the changes in these two countries are proceeding in a parallel direction.
“I have constructed in my mind a model city from which all possible cities can be deduced,' Kublai said. ‘It contains everything corresponding to the norm. Since the cities that exist diverge in varying degree from the norm, I need only foresee the exceptions to the norm and calculate the most probable combinations.

‘I have also thought of a model city from which I deduce all the others,' Marco answered. ‘It is a city made only of exceptions, exclusions, incongruities, contradictions. If such a city is the most improbable, by reducing the number of abnormal elements, we increase the probability that the city really exists. So I have only to subtract exceptions from my model, and in whatever direction I proceed, I will arrive at one of the cities which, always as an exception, exist. But I cannot force my operation beyond a certain limit: I would achieve cities too probable to be real.’”

— Italo Calvino, *Invisible Cities* (1972)

Is there a unifying model, or even a discrete number of models, of the welfare state? Generations of scholars working on what is now called comparative political economy have endeavored to address this question. Moreover, why have policies encompassing what we think of as the welfare state developed in every industrialized country, yet with highly distinct institutional characteristics? This thesis is but a minor contribution to the vast literature on the subject. But it finds a toehold in part by redefining the question for the present epoch (after all, what else is the baby-faced undergraduate good for?). A comparative approach to the welfare state requires an explanation of why purportedly diverse phenomena—*Worlds* or *Varieties* of welfare states—actually appear to be becoming more similar. One central goal of this thesis is

---

to demonstrate the merit of this framing. Doing this alone is no small task, since it requires recognition of the idea that social policy regimes are in fact evolving in a parallel direction. But the thesis also meditates on the causes and agents of this institutional change. That these matters cannot be easily explained is frustrating, to be sure, but also makes them all the more interesting to consider.

In the first pages of this thesis, I offered a critical literature review of two different schools of thought purporting to explain welfare state diversity. The historical institutionalist school draws upon a wide range of unique contingencies, but chiefly emphasizes a ‘power resource theory’ of welfare states built through the strength of a mobilized working class, whether via trade unions or the political Left. Rational choice institutionalists, in contrast, offer an essentially functionalist and business-centered account of welfare regimes fitting within a larger system of institutional complementarities. They claim that firms support social policies in contexts where they create the labor market conditions advantageous to firms’ production processes (by incentivizing specific skill development, for instance). Tracing upwards the intellectual roots of these literatures reveals even more existential disagreements, relating to their understandings of how institutions change over time. Thinkers in the former school are indebted to Karl Polanyi’s work, positing that institutions form as the consequence of dialectical struggle between forces of market expansion and forces agitating for social protection; those in the latter school owe much to the work of mid-twentieth century labor economists who posited the structural conditions necessary for modern industrial capitalism to flourish. In spite of the gaps between these schools of thought, each one
offers a typology of different welfare regimes as a tool for understanding institutional diversity.

As I have argued, however, the typological approach to comparing advanced welfare states fails to grasp the key insight that many are undergoing change in a parallel direction. They are ‘retrenching’ in the sense that they are becoming less effective in offering individuals social protection from the risks of destitution in old age, unemployment, or other such hardships. But welfare states are not simply fading away; rather, they have transmogrified into altogether different institutions than the ones that characterized social policy in the postwar *trente glorieuses*. They are being re-oriented to the task of pushing individuals onto national labor markets, and to strengthening employers’ market power to dictate wages, benefits, and employment conditions. In explaining *why* this change has occurred, and across such different contexts, I built upon the rational choice institutionalist literature and defined a systemic logic of post-industrialism, common in varying degrees to many of the world’s advanced economies, that motivates economic actors’ behavior. But in explaining *how* its has occurred, I drew heavily upon power resource theory, arguing that retrenchment has been an active project of corporate firms and their representative associations, which have not only capitalized on the intrinsic political and economic bargaining advantages granted to them by the logic of post-industrialism, but have also sought to weaken labor unions and unravel collective bargaining coverage as a means of achieving their goals.

The two case studies in the second half of the thesis examined the evolution of private old age insurance and unemployment insurance in the United States and Germany, respectively. Though the reader will be the ultimate judge, I suggest that
they offer clear evidence of welfare state retrenchment, supported—which, even spearheaded—by firms in very different political-economic contexts. In both cases, social benefits have seen a reduction in their generosity, a dualization of their beneficiaries, and a shifting of risk from communal insurance pools to individual workers. Yet the nuances of the working hypothesis, with respect to the structural causes of welfare state convergence, are less obviously confirmed or denied by the case studies. It is always a challenge to match observed data with their structural causes, but the temporal narrative offered by the U.S. case study traces firms’ involvement in the shift from defined benefit to defined contribution pensions to the mid-1940s, well before the onset of the logic of post-industrialism. If one concludes that firms were

---

2 Two data points, it should be noted, make a line, but not necessarily a trend. One challenge that can be leveled at this thesis is that I posit the existence of a particular phenomenon across many post-industrial contexts—indeed, one motivated by their very status as post-industrial economies—without examining a large number of those cases. That I was not able to do so is a consequence of both methodology and resources (time resources, that is, not power ones). With respect to methodology: as I have discussed at length, expenditure-level analysis provides an incomplete picture of the character of a given welfare state. Lyle Scruggs, Detlef Jahn, and Kati Kuitto have done admirable work in their assembly of a “Comparative Welfare Entitlements Dataset,” which is undoubtedly the quantitative data par excellence on global welfare states available today. It offers a variety of household data on different facets of the welfare states in 33 countries, with the salient measurement being income replacement rates. But even this metric fails to capture the ways that welfare state retrenchment has been used to strengthen employers’ market power to dictate wages—narrowing the conditions under which a worker can refuse undesirable employment in order to continue receiving unemployment insurance benefits, for example—a key contention of my thesis. Due to these challenges, my methodology centered upon examining a working hypothesis in light of qualitative case studies. And given the temporal restrictions of an undergraduate thesis, my options were limited to offering evidence through many cursory historical narratives or through a few thorough ones, of which I obviously chose the latter. That this thesis examined the United States and Germany—rather than, say, Australia and Belgium—is in part a response to this conundrum, in that both political economies are often thought to be paradigmatic examples of larger institutional families. By demonstrating a commonality between those two countries, I hope to have shown the strong likelihood of a similar occurrence in the countries with which they are often grouped. But to some extent, this assertion falls into the realm of the speculative. The greatest intellectual success my thesis could achieve would be to spur similar research on other welfare states using the framework I have laid out. A single contradictory example would not disprove the convergence hypothesis—per Calvino, there are no models without exceptions—but a collection of other case studies would go a long way toward settling the matter.
indeed integral to that institutional change, it seems likely that their policy preferences were forged not by exogenous shocks, but by intrinsic inclinations.

In Germany, in contrast, firms’ involvement in welfare state retrenchment is more recent. It is linked clearly both to the changing nature of German industrial relations and the increasing payroll tax costs of social insurance as a proportion of the wage bill. Both of these trends, in turn, are linked to the particular conditions of post-industrialism, through greater international competitive pressure on German manufacturing firms, the growth of the service sector, and a larger number of claimants to social benefits due to structural unemployment. In the German case, then, perhaps changes to the welfare state are symptomatic of larger changes to the institutional environment in which firms in that country operate. But to consider this observation in a vacuum—the erosion of the German model, and nothing more—is to miss another key inference. If the typologies discussed in the literature review reveal nothing else, it is that welfare states like the U.S. and Germany are not merely located at different magnitudes on a singular spectrum of risk redistribution, but historically operated according to their own institutional logics with different underlying normative principles. Over the past 40 years, the German welfare state has undergone retrenchment by reneging on some of those normative principles, replacing them with ones quite similar to those expressed by U.S. employer associations with respect to the shift to defined contribution pensions. Rather than protecting social status, the welfare state increasingly seeks to encourage individuals to achieve self-sufficiency. Adoption of this principle is not the only way to respond to the exogenous shocks Germany’s economy has faced, nor, for that matter, the only way to reduce welfare state
expenditures. That the two case studies discussed appear to be converging therefore merits greater scrutiny.

This thesis opened with a wide-ranging survey of historical research on welfare state development. Contingent factors from legacies of political authoritarianism to religious conflict, and from constitutional design to the success of trade union movements, are all analyzed as impacting the character of welfare state formation across different political economies. Given that body of knowledge, Esping-Andersen’s attempt to differentiate welfare states through a typology (even if misguided) was based on an understanding of their construction through genuinely different historical processes. But much as the modernization theorists foreshadowed, globalization has yoked industrialized countries to shared structural conditions. This is borne out not only through increasing mobility of workers, goods, and capital, but in the increasing financialization of the global economy; the decreasing share of GDP compensating labor; and the supplanting of popular sovereignty by binding international agreements and technocratic domestic governance. It is trite to suggest that globalization has brought the world closer together—though, in an interpersonal sense, it certainly has—but it has undoubtedly brought the world’s post-industrial countries closer in their institutional configurations. They have clustered not around some synthetic

---

3 It is striking, to the present author at least, how one can visit cafés and bars in New York and Berlin, Budapest and Warsaw, Havana and Tel Aviv, and encounter settings that appear substantively the same, frequented by international clientele who all speak fluently the global language of commerce: English. Never has it been easier to meet individuals from around the world and remain instantly connected with them upon returning home (wherever that may be). It is a joy for those lucky enough to be part of it. The trouble with cosmopolitanism—in its present iteration—is that it is limited to an elite segment of the global population, resulting in vast inequality that is not only arguably unjustifiable on moral grounds, but also breeds a parochial response that threatens cosmopolitanism’s very viability.
political economy, incorporating all of the industrialized world’s traditions, but quite clearly around an even more *laissez-faire* vision of the Anglo-American model. Given American dominance over global affairs—particularly economic ones—in the latter half of the twentieth century, this is not altogether surprising. But a more detailed explanation of this observation is clearly required, and the subject beckons for further research.

So where does this leave us? In searching for a more dynamic way to compare different welfare states, this thesis has emphasized the direction of social policy change in place of an attempt to categorize different policies within a limited historical snapshot. Likewise, there is no indication that the welfare states analyzed in the two case studies rest at static equilibria; indeed, they are still very much in flux. Are welfare states simply in a race to the bottom, each reducing its potential to de-commodify individuals’ need to work? Given the current trend-lines, a cynic might say just that. But the working hypothesis outlined here is built upon a Polanyian understanding of dialectical change, which allows for (even necessitates) the possibility that when expanding markets result in social dislocation, society may in turn bite back. The last several years have seen populist reactions to existing political order in France, in Germany, in Italy, and not least in the United States. Though their leaders have been overwhelmingly ineffective in serving their constituents, their voters are very often those whom weakened social policies have left behind. Perhaps the reinvigoration of global welfare states is yet to come.
Bibliography


Congressional Budget Office (CBO). “Estimated Deficits and Debt under the Conference Agreement of H.R. 1, a Bill to Provide for Reconciliation Pursuant to Titles II and V of the Concurrent Resolution on the Budget for Fiscal Year 2018, as Filed by the Conferees to H.R. 1 on December 15, 2017.” Washington, DC, 2018.


Konczal, Mike. “‘Neoliberalism’ Isn’t an Empty Epithet. It’s a Real, Powerful Set of Ideas.” *Vox,* December 20, 2017.


Möller, Joachim. “Did the German Model Survive the Labor Market Reforms?” *Journal for Labour Market Research* 48, no. 2 (August 2015): 151-68.


