ESSAY

A RACE TO THE TOP, MIDDLE OR BOTTOM?
THE CONSEQUENCES OF DECENTRALISATION IN GERMANY

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IDEAS to CHANGE OPINIONS
Introduction
The upsurge in interest in decentralisation in recent years is by no means unique to the UK: there has been an international trend towards greater decentralisation from the level of the nation state in recent decades. Marks et al (2008), in a major study of constitutional reforms since 1950 across 42 countries, found that some 342 of those reforms strengthened regional authority, compared to just 42 that weakened it. Decentralisation is sometimes considered a potential means of, in Alfred Stepan’s phrase, ‘holding together’ states that might otherwise drift apart (Stepan 1999) – Ukraine being a topical example of this. Another earlier example from closer to home is the creation of the Scottish parliament in the 1990s, the rationale for which was to reduce pressure for independence – a flawed rationale, as it turned out. However, in other scenarios – as with the current cross-party consensus in favour of stronger city-regions in England – pressure for decentralisation instead stems from the belief that it can lead to better policy outcomes. Recent work by IPPR North suggests that there could be substantial economic gains from such decentralisation, as well as improvements in the quality of public services, as greater local and regional autonomy could allow innovation to flourish (Cox et al 2014).

Nonetheless, such transfers of power away from the national level are by no means uncontroversial. Advocates of decentralisation claim that it makes possible policies that are better tailored to their contexts (whether in terms of local circumstances or public opinion); greater capacity for experimentation, innovation and lesson-drawing; and also (more controversially) the limiting of state activity and a check on central power. Opponents of decentralisation, by contrast, are fearful either of policy incoherence or – more problematically still – downward pressure on levels of service provision or entitlement, regulation and taxation, as a result of states competing with each other in order to remain competitive. It therefore seems worthwhile to examine specific cases in which power has been passed downwards from the national level.

This paper looks at the impact of Germany’s 2006 federalism reforms, which did indeed transfer certain competencies from the level of the nation state to the regions, or Länder (singular: Land). It starts by briefly examining the literature on the possible impacts of a decision to decentralise, and then sketches the German context and the nature of these 2006 reforms. It then examines the changes that have occurred since power was transferred in three areas of policy: prisons, the regulation of care homes, and pay and conditions for Beamte, an employment category including most public servants. It finds only limited evidence of ‘races to the bottom’, and rather more evidence of upward pressure on standards. It also uncovers some support for cooperation between regions, even where this is no longer legally required. Together, these findings give cause for scepticism about grand claims that decentralisation will lead to a ‘race to the bottom’. Among other factors, the likely policy response to decentralisation depends to a large extent on the policy area in question, and on what the budgetary impact of policy variation would be.

The decentralisation debate: What impact does decentralisation have on policy?
In attempting to summarise the rather substantial academic literature on the possible policy consequences of passing power downwards in a political system, we can discern six distinct scenarios, some of which can may overlap.

1. **The race to the bottom scenario**, in which territories will reduce levels of taxation or regulation in order to gain a competitive advantage, particularly in terms of companies relocating to the region because of the advantages they would enjoy, or attracting citizens with low taxation (Oates 1972: 142; Wilson
This, in turn, will prompt other territories to follow suit, thus inspiring a ‘race to the bottom’, or downward spiral. Similarly, under this scenario territories will reduce welfare entitlements to a lower level than their neighbours, to avoid becoming ‘welfare magnets’ (Peterson 1995). The view that one takes of such a ‘race to the bottom’ would depend on one’s normative standpoint: advocates of a ‘small state’ might welcome the efficiency it brings, while social democrats may be concerned about the under-provision of public goods and damage caused to the poor and vulnerable by shrinking state provision.

2. **The race to the top scenario.** There are two ways in which a race to the top could occur. First, territories would compete to offer the best, or most comprehensive, level of public service provision, prompting other territories to match or exceed them – thereby driving up levels of provision. This is, in essence, the ‘race to the bottom’ in reverse, driven by the popularity of more being provided to the population of one area relative to those in comparable areas. It may be heightened by a greater feeling of solidarity among the population of smaller territories (for instance, in Scotland rather than the UK), which may yield greater support for the provision of welfare services (Keating 2009). Upward pressure on levels of regulation might also occur, whereby a producer in a large territory with higher standards lobbies for other, smaller territories to adopt that standard in order to gain an advantage in the market vis-à-vis domestic producers – this is sometimes known as the ‘California effect’ (Vogel and Kagan 2004: 4).

3. **The race to the middle scenario**, in which territories will try to avoid becoming ‘outliers’ and use other territories as a benchmark, even where there is no legal requirement for them to do so (Green and Harrison 2006). This is more likely to occur in areas where voters are sympathetic to the need for trade-offs between different policy objectives (Rabe 2010).

4. **The laboratories of democracy scenario.** In this case, territories will use their new freedom to determine policy to experiment, and then learn from each other’s experiments – drawing upon practices that have proved successful elsewhere, while avoiding those that failed.

5. **The political parties flexing muscles scenario**, under which policies will begin to vary according to which political party controls the territory in question. If territories were to gain powers over taxing and spending, for instance, those controlled by parties of the left would be expected to tax and spend more, while those controlled by the right would tax and spend less (Schmidt 1980). Variations might also occur in other areas of policy (for instance, in terms of comprehensive versus selective education) where the views of political parties differ (Turner 2011).

6. **The nothing happens scenario**, in which territories simply don’t use their new powers. Existing trajectories of policy may continue if they enjoy public support or backing from institutions that are able to influence policy, and so the costs of change may outweigh the potential benefits (this is sometimes known as ‘path dependence’ [see Pierson 2000]). Equally, it may be that policymakers see benefits to maintaining common policies nationally, and the potential for harm to be caused by variation. For instance, German’s Länder have retained broadly similar educational qualifications by voluntary agreement, to avoid problems with comparability or non-recognition. Alternatively, it could be that, regardless of what the constitution allows for, there is continued normative commitment to avoiding differences within a nation.

It is worth noting that these effects may vary depending on the nature of the policy area in question. For instance, while a ‘race to the top’ driven by public opinion might seem likely when it comes to, say, the entitlement of pensioners to free bus travel, it is rather less likely in the case of, for instance, access to housing for prison leavers.
Races to the bottom would be more likely to occur in areas of policy where there is a substantial fiscal reward or other benefit to be derived from downward variation.

Passing power downwards: the German federalism reforms of 2006

The present system of federalism in Germany (officially the Federal Republic of Germany) was created following the second world war in West Germany, when an explicit aim of the allied occupying powers was to constrain the centre following the experience of the Third Reich. There are multiple levels of government – principally national, regional (at the level of the Länder) and local. Over time, this evolved into a system of ‘interlocking’ policymaking: policies are often set by one level, and implemented by a lower-down level, with some potential for variation. For instance, naturalisation law is set nationally, but implemented by local authorities; schools policy is a jealously guarded competence of the Länder, though local authorities may have some role in issues concerning premises and maintenance. Furthermore, the Länder are represented in the upper house of the national parliament, the Bundesrat, and laws that have an effect on them (for instance, those that the Länder are required to implement) require the assent not only of the lower house (Bundestag) but also the Bundesrat.

Such a system of interlocking policymaking, which places a premium on negotiation between different tiers of government, might be welcomed as one that fosters compromise. However, by the 2000s it was coming under substantial criticism for blurring lines of accountability, stifling the innovation and autonomy of the Länder and, particularly, leading to legislative gridlock, wherein a majority in the Bundesrat would veto proposals made by its political opponents in the federal government and the Bundestag. A cross-party reform commission was therefore established in 2002, which brought together representatives of national government and the Länder. It proposed a disentangling of policymaking, with both the federal government and the Länder gaining more exclusive competencies, and fewer laws needing approval from the Bundesrat. While the final recommendations were rejected by the Länder as they did not go far enough, they were quickly picked up and, for the most part, implemented by the newly-elected ‘grand coalition’ government of Christian Democrats and Social Democrats in 2006. This government’s large majority meant that it was well placed to secure the two-thirds majorities in both houses required to pass constitutional amendments (Turner and Rowe 2013). Among the policy areas affected were:

• education (now even more clearly the responsibility of the Länder)
• environmental protection (in which the Länder were given a new right to deviate from federal rules)
• prisons (laws governing which were previously made by the federal government but implemented by the Länder, and now became a competence of the Länder alone)
• care home regulation (again falling under the purview of the Länder), and
• pay for the millions of public servants known as Beamte,¹ which was previously set federally, albeit with some latitude for Länder to deviate (Auel 2008).

For some, these changes were far too limited in scope. In particular, the power of the federal government to continue to set the levels of most taxes was unaffected, and the more prosperous Länder continued to press for greater fiscal autonomy and to resist the ‘fiscal equalisation mechanism’ that required them to transfer substantial

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¹ Beamte are a distinct class of government employee, ranging across a number of professions including civil servants, the police and most teachers. They enjoy a unique status in German employment law, with guaranteed pensions and high levels of employment protection, but (as a sort of quid pro quo) a legal ban on taking strike action.
sums to their poorer counterparts; these Länder pressed their case both in political debate and before the federal constitutional court. Others believed that the changes would lead to damaging competition between the Länder, which would undermine national solidarity – phrases such as ‘race to the bottom’ were commonly used by those who were sceptical about the reforms.

Below, we briefly assess what has actually happened in three of the areas of policy affected by the 2006 federalism reforms: prisons law, care home regulation, and the pay of Beamte. We chose these three areas of policy as, on the one hand, there was a clear shift of power from the national to the regional level in each case, but, on the other hand, different factors were likely to shape policy responses in each area. For instance, choices regarding the pay of Beamte would have a major impact upon Länder budgets, whereas the impact of decisions on care home regulation would primarily fall on other actors. Equally, in one case decisions would affect a group that enjoys substantial public sympathy (residents of care homes), while in the case of prisons we would expect public pressure to be in favour of harsher treatment.

Of course, at the time of writing the reforms are less than a decade old. Moreover, they concern individual areas of policy (albeit ones of some importance) rather than a systemic change. Nevertheless, careful analysis of the impact of decentralisation in these areas can provide potentially important insights into the policy consequences of passing power downwards from the national level.

### The case of German prisons

The decision to devolve responsibility for prisons law from the national level was a source of consternation among professionals in the sector. There were fears of a ‘competition of harshness’ among the Länder, in which they would pursue the twin aims of reducing costs and pandering to popular support for punitive policies. It was also pointed out that there were already variations in prisons across Germany in terms of differences in access to single cells or entitlement to day-release (Dünkel and Schüler-Springorum 2006).

At the time that the reforms were passed there was a particular need for the Länder to legislate in the area of youth justice, due to a ruling of Germany’s federal constitutional court. Only three Länder chose to legislate on all prisons immediately, while other kept law on adult prisons unchanged until recently. For this reason, our findings in this section draw upon the area of youth prisons in particular.

Most significantly, there is a clear consensus – derived both from scholarly literature and interviews with actors in the field, and among supporters and sceptics of the federalism reforms alike – that there has been no race to the bottom in the area of prisons policy following the decentralisation of this competency. Indeed, there were occasions when Land-level politicians, having had to pay closer attention to the prisons they were required to legislate for, developed greater interest in this area of policy and went on to commit additional funds (for instance, to support increased entitlement to therapy for prisoners).

That is not to say that the Länder have continued with entirely common policies. We found that there were substantial differences in their appetites for ‘going it alone’ in the field of prisons policy. Of the 16 Länder, 10 chose to co-operate in drafting new laws, with minor variations being inserted by politicians at a later stage. It was only the larger Länder (including Bavaria and Baden-Württemberg, the two most enthusiastic proponents of greater autonomy across all policy areas) who chose to go their own way from the start.

However, some variations in policy were brought about – for instance, in terms of the level of entitlement to a single cell in youth prisons, entitlements to therapy, the
treatment of open prisons, and statements in prison law regarding what the aims of punishment should be (Dünkel 2007; Höynck et al 2008; Ostendorf 2012). These variations were driven in part by a desire to formalise (and legitimate) existing practice and facilities, but also by political choices. For example, the political priorities of the conservative government in Bavaria have been reflected in its provisions becoming rather ‘harsher’ than elsewhere. At the other end of the scale, some particularly liberal accents were included in Brandenburg’s laws – the first Land with a Left Party justice ministry. This appears to confirm the view that decentralisation can allow political parties greater scope to flex their muscles at the regional level.

Evaluations of the usefulness of passing power downwards in this area differ sharply. For some, decentralisation has proven highly beneficial, allowing for greater experimentation and ‘policy learning’, greater ability to reflect (democratically-expressed) political priorities, and giving the area a higher political profile. Others disagree: the criminologist Frieder Dünkel, in an essay entitled ‘The Farce of the Federalism Reform’, talks of ‘provincialism and populism’, describing the reforms as an ‘expensive and inappropriate’ instrument which constitute a ‘gigantic waste of taxpayers’ money’ and show no evidence of having prompted innovation (Dünkel 2007: 2, 29–30). However, Dünkel later conceded that ‘the initially feared “competition of harshness” has not happened so far’ (Dünkel et al 2010: 29). Nevertheless, a leading trade union official felt that the reforms hindered co-operation, telling us that ‘German (prison) federalism is a synonym for burning money’.2

The case of German care home regulation
As with prisons, power over the regulation of care homes was passed to the Länder despite substantial reservations among politicians, civil servants and service providers, who feared a growth in complexity as well as possible downward pressure on standards. However, as is true of prisons, there has been no discernable race to the bottom on care home standards as a result of the federalism reforms. If anything, regulation has become more exacting, at least in two specific respects. First, some forms of mobile care that were not previously regulated are now covered by new, Land-level laws; and second, the Länder have increased the demands they make of care home providers. Indeed, the latter complain of competition among the Länder to see who can impose the most onerous requirements.3

As in the case of prisons policy, there is some evidence that different decisions have been taken based upon differences in social and political contexts: the decision to regulate care providers in shared accommodation in Berlin, for example, was driven by a substantial ‘problem pressure’ there, while Bavaria – sceptical of national government requirements for care home transparency – introduced its own requirements for care homes to meet. Länder governed by Social Democrats have been at particular pains to emphasise resident involvement and their ability to lead lives as autonomously as possible (indeed, those Länder discussed such aims explicitly before they drafted their new care home laws). However, all the new laws – adopted by Länder governments of both left and right – have been concerned with autonomy and participation to some degree.

Another commonality with our findings in the area of prisons policy, different Länder have advanced at different speeds. While Bavaria and Baden-Württemberg engaged in a race to get the first Land-level law in place, the eastern Land of Thuringia has not yet adopted its own law, and the old federal legislation remains in place as a default.

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2 From an interview with the authors, 4 December 2013.
3 For more detail on these laws, see Schneider (2013), and Schneidereit J (2013) QM-Lösungen für die stationäre Pflegepraxis: Die Heimgesetze der Bundesländer in Deutschland, Behrs Verlag: 555–563.
On the face of it, it the greatest puzzle in the realm of devolved care-home regulation is why Länder have not taken the opportunity to achieve cost savings through deregulation, as many opponents of the decentralisation of welfare anticipated. The answer would appear to be twofold. First, this is an area of substantial political sensitivity and public scrutiny. For instance, no Land has reversed the previous legal requirement for at least 50 per cent of staff to be qualified professionals (though some have tinkered with the way in which this group is defined) – to do so would generate unwelcome political controversy. Secondly, the Land government would make next to no financial gains by doing so – the costs of increased regulatory requirements are largely borne by care insurers, private individuals paying for their care, and local authorities for those with no other funds. Providers perceive this as dysfunctional policymaking, as the Länder are writing cheques that have to be honoured by others. Others, however, consider it important protection against downward pressure on standards.

The case of German public sector pay

The remuneration of Beamte (who constitute approximately 37 per cent of German public servants [DGB 2013]) has an interesting history. Until 1971, decisions on their pay were the responsibility of the Länder, but the national government of the day felt that this led to damaging competition between the Länder which was sending pay spiralling upwards, so it secured agreement to take such decisions centrally. Central control was later weakened, with the Länder becoming able to vary Christmas, holiday and other bonus entitlements from 2003/04 onwards. Working hours, however, remained a matter for determination by the Länder throughout, as they concerned the implementation of a federal law.

By the time of the 2006 federalism reforms, pressure to decentralise was coming from two directions. Those Länder that were keen on expanding their range of powers across all areas, such as Bavaria and Baden-Württemberg, were predictably keen to gain complete control over this area. They were joined in this by Berlin, whose Social Democratic mayor Klaus Wowereit pleaded, ‘I cannot afford to be dependent upon the Bundestag decisions about the pay of Beamte. We have to be able to take the decision ourselves... This is fundamental for the sustainability of each Land’ (Bundesrat minutes 2006: 211). With pay costs accounting for between 40 and 50 per cent of Land budgets, Wowereit’s claim appeared justified, particularly given the inability of Länder to raise their own revenues (since the levels of most taxes are set at a national level). However, others took a different view – the Land of Schleswig-Holstein, for instance, argued vigorously that allowing regional variations in pay levels would lead to ‘poaching’ by richer Länder, with poorer counterparts losing out. Union representatives were also extremely unhappy, fearing that pay levels would be determined by the arbitrary criterion of the extent of pressure on each Land’s budget. They pointed to variations which had already arisen since the granting of flexibilities around bonuses.

Decentralisation has had immediate and significant consequences in this area. Across most pay grades, there is a gap of around 10 per cent between the pay of a Beamte in Bavaria (the richest and in most cases most generous Land) and Berlin (among the poorest and lowest paying), with pay in other Länder distributed in between (DBB 2014). In addition, promotion prospects, age limits for becoming a Beamte, and the treatment of early retirement also differ sharply.

The single most important determinant of pay levels is the state of the Land budget, although other factors have played a role:

- political choices (by and large, Länder governed by the right are more sympathetic to demands of those parts of the public sector that enjoy the status of Beamte than those of the left)
• the timing of elections (the incumbent Bavarian government was keen to reward its public servants in the run-up to one recent election)
• the extent to which the public sector has to compete for employees with the private sector (greater in those Länder with lower unemployment)
• Land-level institutional arrangements for discussions about pay, and
• variations in living costs (although these – but not pay – may differ within Länder, variation between them is greater, with one minor exception).

In contrast to the other policy areas examined in this paper, co-operation between Länder on this issue has not occurred – rather, each Land has made its own decisions on what to do.

However, there is little evidence of competitive practices between the Länder, with only very limited evidence of ‘poaching’ (at one point, the state of Baden-Württemberg advertised in other Länder for teachers to join it, but the posters soon disappeared after political representations). In the police service, movements are restricted by a voluntary agreement between the Länder, and more generally, our interviews with police staff have indicated that requests for a transfer to a different Land tend to be motivated by personal rather than financial reasons. Competition is more prevalent when it comes to recruitment – for instance, when recruits to the police service choose in which Land to train – and is more prominent in areas close to boundaries between Länder.

Conclusion

Three particularly important conclusions can be drawn from these three areas in which power was decentralised in Germany.

First and foremost, there was no ubiquitous ‘race to the bottom’, or lowering of standards, as a consequence of decentralisation. If anything, there was stronger evidence of a ‘race to the top’, notably in the case of care home regulation. There also appeared to be a strong normative attachment among policymakers (especially civil servants) for common policies across the country, which led to collaboration in drafting legislation, and tempering the extent of variation.

Secondly, there were major variations in the extent to which different Länder sought to take advantage of their newly-gained powers. Some – notably the large, rich, powerful Länder that had pressed for the changes – took advantage of the new powers straight away, while others lacked either the capacity or the political desire (or the functional pressure) to do so.

Thirdly, variations in each of the policy areas have begun to emerge. These appear to be driven by three sets of factors. The first is party politics – in areas where political parties have sharply different visions, they have taken the opportunities offered by these new powers to shape policy in the ways they favour. Secondly, context (socio-economic, fiscal and geographic, as well as the legacies of past policies) has shaped policy choices. Thirdly, some Länder have introduced new legislation in these areas simply to ‘make a point’, and to demonstrate that they are taking advantage of their new-found freedoms.

Clearly, this study relates to the very particular circumstances of Germany’s federal arrangements, at a particular moment in time. Nonetheless, our findings point to a number of lessons for those considering the likely impact of passing power downwards from the national level.

First, grand claims about decentralisation necessarily leading to damaging races to the bottom should be treated with some scepticism. It is particularly important that the possible drivers of such downward pressure upon levels of expenditure, taxation or regulation are examined. This pressure is clearly greater in cases where
reducing expenditure, or levels of regulation, stands to deliver a substantial fiscal reward to the territory in question (as freezing the pay of public servants did for the Länder). Conversely, the pressure is clearly lower if the public compares levels of entitlements across the territory and disapproves of reducing levels of expenditure or regulation (as is illustrated by the regulation of German care homes).

Secondly, predictions of major shifts in population – as people are attracted or repelled by particular policies in particular places – should also be treated with caution. These often form the basis of theoretical models in political science (most famously Tiebout 1956), but the evidence – at least from German public sector workers who might have been expected to move in search of better pay – is rather patchy.

Thirdly, decentralisation can prompt a degree of experimentation, and a desire to learn from neighbours’ policies. It can also inspire greater interest from politicians who are keen to have an impact upon areas that have newly fallen within their purview. At the same time, a thousand flowers may not bloom overnight: capacity might hinder regions from doing their own thing, and decentralisation does not prevent sensible co-operation. Policymakers might well see advantages – both practical and normative – to collaborating on the development of new policies, and to keeping them in broad harmony with those of their neighbours.

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