

FAQ on solutions for employees close to retirement

1. What is the general situation in a restructuring scenario?

Restructuring poses significant challenges for the workforce. These challenges typically do not affect employees close to retirement in the same way as those who are still a long way from retirement age. In addition, employees close to retirement are frequently quite willing to consider early retirement as long as the terms are right. As such, in restructuring situations particular emphasis is always placed on (special) arrangements for employees close to retirement.

The typical instruments used here are statutory early retirement and partial retirement. The core idea behind the German Act on Early Retirement and the German Act on Partial Retirement was that the state should support early retirement of older employees to make way for younger employees who have not yet been fully integrated into the labor market. Government support for employers in the form of subsidies has been dropped, but early retirement and partial retirement are nonetheless still possible and these options are used accordingly.

2. How does early retirement work?

Under the German Act on Early Retirement, statutory early retirement is based on an early retirement contract. Unlike with partial retirement – see below – the employment relationship is terminated and followed immediately by early retirement. The early retirement period ends upon receipt of the statutory pension, and the employee never returns to working life.

3. What should be included in an early retirement contract?

The essential requirements for statutory early retirement and thus the essential elements of an early retirement contract are:

- an early retirement benefit of at least 65 % of the previous gross salary;
- the obligation to pay the early retirement benefit at least until the time when an early retirement pension can be drawn;
- the employee's permanent exit from working life.

In contrast to partial retirement, early retirement does not require a minimum employee age or a specific length of employment with payment of social security contributions before the start of early retirement.

4. How is early retirement benefit treated under social security and tax law?

If the requirements for statutory early retirement are met, early retirement benefit – like “normal” pay – is subject to social security contributions, with the exception of unemployment insurance. There is no obligation to be insured under the unemployment insurance scheme in view of permanent withdrawal from working life. Therefore, no more contributions are due in this regard. The total social security contribution payable in respect of the early retirement benefit is divided equally between the employer and the employee.

As a pension payment, early retirement benefit is subject to income tax. Tax-free allowances on pensions and supplements apply to severely disabled persons from the age of 60 and to recipients of early retirement benefit from the age of 63.

5. Is there an entitlement to early retirement?

Not as such. The statutory early retirement scheme only provides the framework, without establishing an entitlement. Any entitlement to early retirement or to agreeing an early retirement contract must be expressly provided for. If the employer and the works council decide to offer early retirement in connection with restructuring, such an entitlement will usually be included in the social compensation plan.

Another possibility is for employers to offer their own voluntary early retirement programme ahead of restructuring on a unilateral basis. It is important here to avoid employees being able to demand early retirement under the scheme without the consent of the company, as this could trigger higher numbers than desired and lead to an unacceptable financial burden.

6. What are the key points to be aware of in contractual arrangements for early retirement?

It is possible to agree that early retirement will end on the earliest possible date of receipt of an early reduced pension. If this also applies to an early pension for severely disabled persons (sections 37, 236 a and 237 a of Social Security Code VI (*SGB VI*)), this may constitute discrimination contrary to the German General Act on Equal Treatment (*AGG*). It should be made clear, at least in the general provisions, that these two pension options are not an essential requirement for ending the early retirement period.

7. What are the advantages and disadvantages from the employee's point of view?

The main advantage from the employee's point of view is that social security cover remains in place beyond termination of employment and up until receipt of a pension. In particular, this allows statutory pension rights to be accumulated despite stopping work.

The disadvantage – apart from the inevitable difference in earnings between active remuneration and early retirement benefit – is the decision to withdraw permanently from working life that is a necessary part of taking early retirement. During the early retirement period, only marginal employment (dependent or self-employed) is permitted. Taking up more than a mini-job leads to a loss of social security cover.

8. How does partial retirement work?

Under the German Act on Partial Retirement, statutory partial retirement is based on a partial retirement contract. The partial retirement contract converts an existing employment relationship into part-time employment for a fixed period until receipt of the statutory pension. Working hours are halved until the pension starts. The remuneration is halved accordingly, but is topped up by the employer.

9. Who can take partial retirement and what should be included in a partial retirement contract?

The requirements for partial retirement in accordance with the German Act on Partial Retirement are that the employee

- is at least 55 years of age at the start of partial retirement and
- has been employed and paying social security contributions for at least 1,080 calendar days (36 months) in the last 5 years prior to commencement of partial retirement.

The essential elements of a partial retirement contract are:

- reduction of working hours by half;
- reduction of remuneration by half;
- topping up of the halved remuneration by at least 20 %;
- partial retirement must be limited to a maximum of 3 years, or up to 6 years in the event of corresponding collective agreements (at least in the case of the “block

model”), which must extend up to the earliest possible date of receipt of a pension or early pension.

In practice, the block model is normally chosen as the way of distributing the halved working hours, with the first half of the period being the work phase and the employee then being released from work in the second half of the period.

10. Is there an entitlement to partial retirement?

No. In effect, the same applies as for early retirement. Without an expressly regulated basis for entitlement, there is no entitlement to partial retirement or to the conclusion of a partial retirement contract.

11. What is the social security and tax situation with regard to employer payments during partial retirement?

During partial retirement, half of the normal remuneration is paid – corresponding to the 50 % reduction in working hours. This is subject to social security contributions and tax “as normal”; nothing changes in this regard.

Top-up payments and the additional pension contributions to be paid by the employer are exempt from wage tax and, as a result of the exemption from wage tax, also from social security contributions. The top-up payments are subject to the exemption with progression rule, however. This has an impact on taxation of the halved remuneration, with the tax rate typically increasing.

12. What are the key points to be aware of in contractual arrangements for partial retirement?

Here again – as with early retirement – the general provisions at least should not be geared towards early pensions for severely disabled persons, in order to avoid discriminatory unequal treatment.

13. What are the advantages and disadvantages from the employee's point of view?

The advantages of partial retirement from the employee's point of view consist primarily of the comprehensive social security cover provided by the (partial retirement) employment relationship that continues until they start to receive a statutory pension. This also applies in particular to the accumulation of statutory pension insurance rights through the additional pension insurance contributions, which are borne solely by the employer. Originally, partial retirement involved a new and separate right to a premature pension, but this is no longer relevant for the age groups now being considered.

There are no real disadvantages to partial retirement from the employee's point of view, apart from the reduced earnings compared with full-time remuneration.

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