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# HRM in the German Business System: A Review**

Human resource management in Germany is deeply rooted in its institutional environment. Thus, US style HRM cannot be simply transferred to the German context. Nevertheless, the German business system is not hostile to HRM principles. Rather, these practices have to be adapted to the demands and constrains of the German socio-economic context. The key labour market institutions of collective bargaining, co-determination, and initial vocational training in particular require a pluralist style of human resource management. As our review suggests, these institutions support the implementation of some HRM principles while inhibiting others. Also, the concept of Strategic HRM in Germany may only be fully understood against the background of labour market institutions.

Key words: **HRM, National Business System, Neo-Institutionalism, Industrial Relations, Germany**

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## Introduction

HRM philosophy and rhetoric has its origins in the US. From a European viewpoint the US form of HRM is perceived as unitarist and individualistic (Müller, 1999a). While in the US HRM ideas could spread in a relatively unrestricted manner, this was much less the case in Europe. The legal, social, and political environment of European countries limits the unchanged application of HRM ideas. Accordingly, several European scholars have questioned the simple application of American HRM principles and values (e.g., Brewster 1993, 1995, 1999; Guest 1990, 1994; Kabst/Brewster 2004).

In this respect, Germany is a particularly interesting country. Here, managerial decisions are much more strongly framed by the institutional environment than in other countries. As it should become evident throughout this paper, this holds true especially for the management of human resource issues. However, this does not mean that Germany is not receptive to new managerial paradigms, such as the HRM philosophy. Rather, there seems to be a unique way of dealing with these ideas, which is very much related to institutions of the labour market.

This article has two main objectives. First, we want to illustrate if and how the HRM philosophy (or elements thereof) has been taken up by German academics and, more importantly, by German companies and which crucial role labour market institutions played and still play. Secondly, by doing this, we examine via the example of Germany the limitations of a universalist, unitarist, and top-down conceptualisation of HRM.

## Reception of the HRM philosophy in academia

The year 1961 can be marked as the establishment of personnel management as an academic domain in Germany. In this year, the German *Association of University Professors of Management* (*Verband der Hochschullehrer für Betriebswirtschaft*)[1] organised its annual conference under the main heading of "Work and Pay as research project in business administration" (*Arbeit und Lohn als Forschungsprojekt der Betriebswirtschaftslehre*), the first chair of personnel management in Germany was established at the University of Mannheim, and for the first time personnel management was integrated as a specific business administration major in the curriculum. In the following year, Kolbinger (1962) finalized his work on the first German textbook on personnel management. The accompanying boost in numbers of academics specializing in this area started in the 1970's. As a consequence, in 1973 the *Association of University Professors of Management* officially established a sub-division for personnel management with more than 120 university academics (mostly full professors) at present. The number of university professors in business administration who specialise in personnel management rose from about 20 in the mid 1970's to more than 60 today. In relative numbers, the percentage of personnel management professors compared with the total numbers of professors in business administration increased from 5.3% in the mid 1970's to about

[1] For the organisation of the academic field of personnel management in Germany see Matiaske (2002).

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7.3%.[2] Today, in most universities with a moderate to large department of business administration and economics, such a chair has been set up, sometimes in combination with other subjects, such as "Organisation" (Gaugler 2004; Gaugler/Oechsler/Weber 2004).

With respect to the academic discourse, the somewhat dramatic paradigm change from personnel management to the HRM philosophy in the US (see Schuler/Jackson, this issue) was not paralleled in Germany. Nevertheless, German scholars followed the Anglo-American discussion and took up issues they deemed important for the German context (see e.g. Scholz 1996). In the mid 1980's there started what Müller (1999b) called an "enthusiastic embrace" of HRM. Three issues received particular attention. First, the necessity for a shift from a collectivistic to a more individualistic management of the workforce was discussed. This discussion concerned both the companies' need for a more flexible workforce and the employees' change of values towards more individualism (e.g., more autonomy). Thus, academics widely recommended, for example, more flexibility with regard to work organisation or working hours but also a more individual approach to compensation or HR development (e.g., Drumm 1989; Kolb 1992; Wagner 1991). Second, the strategic value of personnel management was discussed. It was argued that it should become part of the business strategy, that is, HR and general business strategy should be connected. This, of course, makes it necessary that a HR strategy is developed and it was suggested (e.g., by Ridder 1994; Schreyögg 1987) that HR issues should be managed strategically, that is, they should be designed along the lines that the general business strategy prescribes. Third, German personnel management scholars suggested that there should be a shift in responsibility from the human resource department to line management. Thus, they recommended (a partial) devolution of HR issues (e.g., Ackermann 1992; Wagner 1992).

Some particularities of the German academic discourse on HRM are worth mentioning. First, within the academic field of business administration there is a strong normative tradition (Müller-Camen/Salzgeber 2005). Second, the dominance of the normative tradition is paralleled by a relatively weak empirical orientation. Although the number of empirical studies conducted by business administration scholars in the field of personnel management has increased, the absolute number is still rather low. Third, there is a noteworthy lack of interdisciplinary communication. Although human resource management, and in particular its German form, is located at the intersection of the fields of business administration, sociology (especially the domain of industrial relations), and work and organisational psychology, there still seems to be only very little scientific exchange (Müller 1999b).[3]

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2 These numbers do not include professors of personnel management at polytechnical universities (sometimes called "Universities of Applied Sciences" or *Fachhochschulen*).

3 It should be noted that the topic of industrial relations is typically not covered by academics in the business school in Germany, but mainly discussed within sociology, that is, institutionally separated from business scholars. There is one exception to the general lack of interdisciplinarity, a significant number of chairs in human resource management is held by academics originating from organizational psychology.

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It is interesting to see that in the past the German academic mainstream followed the idea that HRM is a rather universal idea. The German business system was not perceived as distinct enough from the US system as to question the transferability of Anglo-Saxon HRM practices. However, in recent years there is a growing awareness of the particularities of the German business system and a "German approach" to human resource management. Some scholars have argued (e.g., Sadowski/Backes-Gellner/Frick 1995; Wächter 1997) that the transfer of the HRM philosophy has to reflect the cultural, social and political environment in Germany in general and the crucial role of the German industrial relations system in particular.

## Neo-Institutionalist approaches to the study of human resource management

Neo-Institutionalist approaches to the study of human resource management provide a useful framework for understanding the problems of the transferability of US style HRM. Before exploring these ideas further we first differentiate between the American institutionalist school and the European institutionalist school (Geppert/Matten/Schmidt 2004).

The American neo-institutionalist school, mostly labelled new institutionalism, refers to authors like Meyer/Rowan (1977), Zucker (1977), or DiMaggio/Powell (1983) and views organisations as open systems that are shaped by the environment in which they are embedded. In order to increase their chances of survival, organisations do not only have to be efficient but they have to be legitimate. Legitimacy can be acquired by adopting structural elements that socially constructed environments regard as appropriate. Thus the formal structure of an organisation reflects the societal perception of rational design. In order to survive, organisations need to adapt management practices to societal expectations leading to structural equivalence of organisations. Three mechanisms of isomorphism can be distinguished: coercive (pressures from the environment), mimetic (pressures from reference organisations), and normative (pressures from professional associations).

The European neo-institutionalist school, mostly labelled as the 'business systems' approach, pre-dominantly refers to the works of Whitley (1992, 1997, 1999), Hall and Soskice (2001) and Albert (1991). Whitley argues that differences in institutional environments (divergent capitalisms), in particular on a supranational level, need to be considered in a more systematic fashion. Depending on the institutional frame of a particular economy, a customized national business system evolves. Historically grown institutional traditions and systems of a society determine the nature of the firm, non-ownership mechanism of coordination, and work organisation.

The two strands of neo-institutionalism may be a good reflection of the different approach to the HRM philosophy as set out before. North-American neo-institutional approaches to HR practices are mainly focused on organisational fields explaining how organisations adapt to similar expectations eventually leading to similar management practices. The institutional approach to HR practices in Europe shows greater awareness of national uniqueness and its consequences for organisational practice. However, it is also important to say that both strands of neo-institutionalism are not set up in purposeful contrast to each other, but have historically grown independent

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of each other. North-American neo-institutionalism has (in general) a different focus, namely a more micro-oriented level of analysis looking at specific organisational fields without any respect to supranational issues. European neo-institutionalism purposely highlights the differences in national business systems focusing on the historical development of economic systems and its consequences (e.g., Gooderham/Nordhaug/Ringdal 1999). Thus, while the North-American literature often highlights explanations of convergence within fields, the European strand emphasises divergence between national business systems. Both approaches discuss the process of adaptation to norms, value, and demands, each using a different lens. Thus, differences in HR practices within Europe and with respect to North-America may be considered in both approaches, however, the European school is historically better prepared for this task (Kabst/Brewster 2004).

## Human resource management, industrial relations and the German business system

Turning from the academic debate to empirical evidence, we will illustrate the interplay of human resource management, industrial relations and the legal system which is so important to understand the *status quo* of human resource management in Germany. We will first shortly describe the key labour market institutions. Then, we will summarize the results of empirical studies on HR practices in Germany. We will turn to the specific question of how foreign MNCs deal with the German institutional environment. Finally, we will provide an outlook for the German HRM debate.

## Key labour market institutions

There are three German labour market institutions that had and still have a strong impact on human resource management: collective bargaining, co-determination, and initial vocational training (Müller 1999 a/b).

### *Collective bargaining*

In most industries, terms of individual employment, such as salaries or working hours, are framed by a general contract between trade unions and employer associations or employers. These collective bargaining agreements are negotiated for the respective industry on a regional level. It is important to note that companies are not forced to be members of the employers association and thus to accept the collective bargaining agreements. Nevertheless, about two thirds of the German workforce were covered by collective bargaining by 2001 (Schmidt/Röbenack/Hinke 2003). As a consequence, there used to be a high degree of standardization in conditions of employment within industries. However, in the context of recent national and international economic developments (e.g., reunification, global competition), employers have argued that regulations of collective bargaining are too inflexible and do not take into account specific economic conditions of individual companies. Two different developments can be found as a consequence. On the one hand, companies either leave the employers association entirely or spin-off autonomous parts which are no longer covered by industry-wide collective bargaining. On the other hand, trade unions and employers association agree on more company-specific flexibility allowing companies to deviate from standard bargaining conditions in certain economic and competitive constellations

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(see also Singe/Croucher, this issue). Thus, the influence of collective bargaining on HR decisions, while still strong, seems to be decreasing.

### *Co-determination*

Co-determination is probably the most influential labour market institution as far as HR issues are concerned. The basic idea of the German co-determination model is to let employees participate in management's decision-making processes. This participation is indirect, that is, it functions through employee representatives and formalized bodies of co-determination, backed by an extensive legislation that grants a broad range of rights with regard to information and determination (Works Constitution Acts of 1952/1976 at the board level and Works Constitution Acts of 1972 at the plant level; for a more detailed description see Lane 1989; Jacobi/Keller/Müller-Jentsch 1998). Basically, there are two main institutions of co-determination: co-determination at the board level and co-determination at the plant level in the form of works councils and. With respect to co-determination at the board level, German law requires joint stock (*AGs*) and limited liability companies (*GmbHs*) with more than 500 employees to set up a supervisory board with both employee and shareholder representatives. Although usually the shareholder side has a majority within the board there is at least an informal influence for the employees' side.

Historically, the German system of industrial relations was famous for board level co-determination, however, during the last two decades co-determination at the workplace has become more and more important. Works councils can be set up in companies with five or more employees, if the employees wish to do so. This opportunity is taken up by the vast majority of German companies (Bertelsmann Foundation/Hans-Böckler Foundation 1998; Weber/Kabst 2000). The employee representatives who constitute the works council have to be elected by the employees. The works council has extensive rights with regard to HR issues. As we will see in more detail, many HR policies cannot be implemented without the consent of the works council. Traditionally, strong ties exist between the works council and the trade union of the respective industry, as many employee representatives are also member of a trade union. However, to say that work councils' influence in a company equals trade unions' influence would be an improper (but also quite common) oversimplification.

### *Initial vocational training*

After regular school education, young people have the opportunity to enter a system of initial vocational training or apprenticeship. It is sometimes called the "dual educational system" because it combines both on-the-job training in companies and state-regulated vocational and general training in specific schools. It covers a wide range of clerical, technical, and craft professions. Completion of the training takes between two and three years, depending on the profession and previous education. This system of apprenticeship is jointly governed and regulated by professional organisations (e.g. chamber of commerce or chamber of handicrafts), by employer associations, and by the unions. As with the previous two labour market institutions, compliance with the initial vocational training system is not mandatory even though – in the face of generally decreasing willingness of companies to participate – there have recently been at-

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tempts by politicians to introduce legal sanctions if not all school leavers get the offer to do a vocational training.

## Reception of the HRM philosophy in companies operating in Germany

Against the background of this specific institutional environment, how has the HRM philosophy been adopted in Germany? For years, a rather negative picture has been drawn. Lawrence (1991) provided one of the most frequently cited accounts of HR practices in Germany. Based on case studies of twelve companies in West-Berlin he concluded that German labour market institutions have a restrictive impact on the management of personnel within companies. More specifically, he argued that through collective bargaining managers have lost their direct influence on pay negotiations, that works councils condition their activities in such a way that they become reactive rather than pro-active, and that the necessity of initial vocational training leads to an overemphasis on training issues. Similarly, Wever (1995) emphasized that the German business system is highly institutionalized. She observed some severe disadvantages of what she called a "negotiated approach" to HR issues in German companies. This approach is characterised, for example, by slow change, high bureaucratization and reduced initiative.

Thus, the institutional environment has been perceived as predominantly negative for the implementation of HRM. However, recent studies paint a more complex picture of how HRM principles are being translated into practice in Germany. Based on the (still limited) empirical evidence, we will now review the application of HRM practices along the central topics of HR, that is, selection, training, appraisal, compensation, communication, and employment stability. We are well aware of some differences between economic sectors and between East and West Germany with respect to HR issues but since our intention is to draw an overall picture, we will not go into too much detail.

*Selection.* A key element of the HRM philosophy is the careful selection of the workforce. This includes the use of formal or standardized selection methods (e.g., structured interviews, formal tests, assessment centers). The most common way of selecting applicants in Germany is a multi-step procedure that consists of an initial screening of the application papers (e.g., curriculum vitae, school and academic records, references). In the next phase promising candidates are interviewed at least once, in most cases by an HR expert and a supervisor for the position to be filled. The interview itself is predominantly unstructured or semi-structured. Formal tests are rarely used. Assessment centres are applied mostly for the selection of management trainees. Also, German companies generally refrain from the use of formal written tests, such as IQ tests or personality questionnaires (Dietz et al. 2004; Schuler/Frier/Kauffmann 2000; Weber/Kabst 2000). Written assessment tests (for basic competences such as writing and arithmetic) are only used for the selection of applicants that come directly from school. This tradition of relative reluctance to use formal selection methods may reflect the influence of two of the three mentioned labour market institutions. First, many applicants have undergone the initial (or further) vocational training. During these rather standardised qualifications the employer gets a relatively good picture of the employee's potential. Thus, in-depth exploration of the applicants abili-

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ties seems not to be as important (Müller 1999b). Second, co-determination allows works councils to refuse the use of selection instruments. In our experience, there is a something like a tradition of works councils rejecting standardised systems of appraisal, as in their opinion they often involve unfair procedures and are subject to many biases. Thus, the validity of written tests is questioned and, as a consequence, not in widespread use. In sum, the HRM prescription of careful selection is only followed for the selection of some groups of applicants.

*Training.* A highly qualified workforce is also considered a central goal of HRM. This can be achieved with a large investment in training, which may also support the goal of functional flexibility (Friedrich et al. 1998). In the German system there are three general types of training. First, as noted above, initial vocational training is a highly regulated and, within the respective profession, standardised form of training. Apprentices are trained on-the-job in their "home" company, as well as of-the-job in specific vocational schools. Upon completion of the two to three years of training the relationship between the company and the apprentices officially ends. However, there is a good chance that companies hire the former apprentices as regular employees, because they have acquired company-specific knowledge as well as general competencies in their profession. Second, there is a nationwide standardised system of further vocational training. Here, technical as well as management-related topics are covered. In some industries, certain certificates are officially required to obtain supervisory positions, for example, the "Certified Foreperson" (*Industriemeister*) and the "Artisan Foreperson" (*Handwerksmeister*). However, in most cases the companies' investment in this type of further qualification is limited. Course fees are often only partly refunded and there is only a limited release from work duties. Third, there is company-specific training on both technical and non-technical issues, such as software, safety, foreign languages, etc. Practically all large companies also offer specific courses for management. It is worth noting, that by law, employees in Germany are entitled to utilise a certain number of workdays for qualification, although this privilege is not used widely.

In general, labour market institutions in Germany limit organisational autonomy on qualification issues to a large extent. For example, companies have only an indirect influence on the curriculum for initial and further vocational training, at least with regard to the off-the-job components. There is also some pressure from unions and politics to fulfil a certain quota of apprentices relative to the overall number of employees. Moreover, works councils have rights regarding the implementation and change of training courses and have a say in which employees have access to courses, even though these rights are not used extensively (Müller 1999b). However, while organisational autonomy on training content is reduced, it is safe to say that German labour market institutions in general strengthen the provision of training. Employee representatives have a strong interest in highly qualified employees because qualifications are seen as strong arguments for increasing salaries or against company attempts to reduce workforce. Even the standardisation of initial vocational training has advantages for the company because a company knows more or less exactly what skills are to expect from an applicant who has completed initial vocational training for a certain profession.

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In sum, the relatively high degree of standardization and regulation in the German economic system is reflected in the *form* of the training system(s). However, in line with the HRM philosophy, labour market institutions ascribe training and qualification a high importance.

*Appraisal.* The existence of performance appraisal systems in companies operating in Germany varies significantly between industries and employee types (Müller 1999b; Weber/Kabst 2000). For example, a high percentage of companies in the field of financial services and chemical firms have such a system, while in the health system the rate is rather low. Moreover, often only management is covered by the appraisal system. This is, at least in part, a consequence of the extensive rights of works councils on both the implementation and the content of the system. There is a tendency of employee representatives to reject formal appraisal systems, because these instruments are seen as means to put more pressure on employees, especially when the appraisal is linked to compensation.[4] As a consequence, mostly employees on higher organisational ranks are affected by these systems. These employees (called "exempts") do not fall under collective bargaining agreements because their salary is significantly higher, and works councils have only limited influence on their working conditions. Thus, in the case of employee appraisal, co-determination is a strong restricting factor, but only with regard to lower organisational ranks.

*Compensation.* The HRM philosophy prescribes both adequate basic compensation and performance-related pay. As above, to understand the German compensation system one has to distinguish "regular" or tariff employees and exempts.

Collective bargaining ensures a relatively high minimum wage for tariff employees. Variable pay accounts only for a small part of the overall salary. Often, bonuses are fixed, and thus have lost their character as a motivational instrument. Other bonuses are distributed collectively on a monthly or annual basis. However, over recent years there has been a strengthening of the weight of individual performance (Weber/Kabst 2000). Unions have realized the increasing importance of a more individualized pay, which reflects both perceived economic necessity and the more individualistic orientation of employees. Thus, in some industries, employee associations and unions have started to jointly develop models for linking performance appraisal systems and compensation (e.g., Huber/Schild 2004). However, at the level of works councils and employee representatives, there is still a strong resistance against what is perceived as converting collective compensation into an individualized system, which may lead both to decreasing solidarity between employees and decreasing wages.

Compensation for exempts (see above) is more strongly based on developments in the labour market, company policies, and individual negotiation. Variable and performance-related pay plays a more important role, especially with increasing hierarchical level, although compared to other countries its weight is still small, partly as works councils have some influence on compensation decisions that concern low-level exempts.

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[4] For a more differentiated discussion in respect to profit sharing and employee share ownership see Kabst/Matiaske/Schmelter (in press).

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In sum, when considering the importance of German labour market institutions on compensation decisions a sharp line needs to be drawn between tariff employees and exempts. For the first group, collective bargaining provides a stable frame for individual compensation that strongly reduces managerial autonomy with regard to tariff wages. Everything "on top" is to some extent a result of negotiations between the company and the works council. As a general tendency, it can be said, that agreements in collective bargaining have become somewhat more flexible in recent years. For example, in some industries and under specific conditions companies are allowed to pay wages below the minimum level for new employees. Unions support implementation of more variable and/or individualized pay components to some extent, while works councils are more critical about this development. For exempts there is only a very limited influence of market labour institutions. For this group of employees performance-related individual pay becomes increasingly important.[5]

*Communication.* Frequent employee communication is an important part of the HRM philosophy, because it is believed to instil higher organisational commitment in the workforce. Three types of communication can be distinguished: top down (company to employee), bottom up (employee to company), and two-way (interactive). With regard to top down communication, most companies have some sort of mission statement. Moreover, in medium-sized and large-sized companies management guidelines can also be found. These guidelines prescribe the characteristics of the leadership philosophy, which normally is a cooperative or participative leadership style. In-house journals, which contain all sorts of company-related information, can be found in most of the large companies. With regard to bottom up communication, standardised attitude surveys have become increasingly important. Forms of two-way communication (e.g., workshops) are sometimes used after these surveys, when results and possible consequences are discussed on the level of departments or work groups. As a general tendency, direct communication, either in the form of meetings or electronic has increased (Weber/Kabst, 1999).

Works councils play a crucial role in employee communication. Works councils often consider themselves to be the distributing centre between management and employee. Co-determination law largely backs this. Management is required to share relevant economic information with works councils. Also, the previously outlined rights of the works council lead to a constant exchange between management on all levels and the works council (Müller 1999b). With regard to top down and two-way communication, the works council is entitled to hold regular meetings that all employees can attend during their regular work hours. This is not necessarily a nuisance to top management. In some companies management regard these meetings as a main vehicle for distributing information. Works councils are important also for bottom up

5 Describing the general point of view, significant exceptions exist. Industries faced with strong external pressure from European neighbouring countries in respect to wages (e.g. construction) have an interest in extension of sectoral collective bargaining. Another exception concerns so called "*Öffnungsklauseln*", that is, exemptions from collective bargaining standards in respect to working hours or wage adaptations in industries like metal or chemistry that are, however, surprisingly rarely used (Schlese/Schramm 2004).

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communication, because attitude surveys need to be approved by the works council. Also, employees often communicate with line or top management via employee representatives, although – comparing Cranfield survey data from 1992 and 2000, this medium seems to have lost some importance (Gaugler/Wiltz 1993; Weber/Kabst 2000).

*Employment stability.* Employment stability is another means prescribed by the HRM philosophy to instil commitment to the company (Wood/Albanese 1995). The existence of an internal job market and the preference for internal promotion are two related antecedents of employment stability. Both policies seem to be relatively widespread in German countries (see e.g., Müller 1999b). Indirect evidence comes from the 2000 Cranfield survey, which reported very low fluctuation rates for Germany (Germany West: 5.7%, Germany East: 3.8%; for comparison, UK: 14.0%). Another indicator for a concern for employment stability of companies operating in Germany is the widespread policy of avoiding compulsory redundancy when workforce has to be reduced. Indeed, 2000 Cranfield survey data indicates that the most important strategy to reduce workforce in Germany is to not extend fixed-term contracts, followed by early retirement in West Germany and dismissals in East Germany (which may reflect the still very tense economic situation in this area). Thus, in large companies reducing employee numbers is a matter of years rather than months.

Co-determination is somewhat important for employment stability. Works councils can demand that internal applicants should be preferred when vacant positions have to be filled. As was pointed out above, works councils have a say in the selection of personnel. With regard to workforce reduction, in general co-determination and other laws make it difficult to lay people off. Companies have to attend to very formal procedures, which, for example, require that works councils have to be informed well in advance about dismissals and their reasons. They can veto dismissals and sometimes play a supporting and active role when employees take legal actions against their dismissal. In the case of mass layoffs the works council participates in developing strategies to reduce undue hardship for employees.

In sum, co-determination fosters employment stability to some extent, either in accordance with company policy (e.g., internal promotion) or as a means of protecting employees against undue dismissals.

*Overall conclusion.* Our analysis of how HRM principles have been implemented in German companies shows two things. First, labour market institutions restrain managerial autonomy on human resource issues to a large extent. Second, however, this does not mean, that in general these principles are rejected. Instead, it can be argued that some principles (e.g., with regard to training or communication) are strongly supported by these institutions. Even more, the high priority of these principles has crystallized in formal structures – and this occurred before, and thus independent of, the German HRM discussion that began in the 1980's. Undoubtedly, the implementation of other HRM principles and practices (most importantly appraisal and performance-related pay) is inhibited by labour market institutions. However, this resistance seems to wane and to give way to more innovative solutions.

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## The lack of strategic integration of HRM in Germany – a myth?

The HR function in Germany is predominantly thought of as less strategically integrated than in other countries (e.g., Begin 1997; Sparrow/Hiltrop 1997). Traditionally, three indicators have been used to analyse the extent of strategic integration of the HR function in empirical studies: The HR director is present on the executive board, the HR function is involved early in the planning process of the business strategies, and there is a written HR strategy (Wächter/Müller-Camen 2002). However, Wächter and Müller-Camen (2002) argue that this result may be based on an inappropriate conceptualisation of Strategic HRM as well as on a neglect of the particularities of the German institutional environment (see also Brewster et al. 1997). Instead they argue that the integration of HR and business strategy is not necessarily associated with the HR function but rather with other institutional actors.

With regard to the first indicator, the presence of the HR director on the executive board of the company, Wächter and Müller-Camen (2002) see two problems. First, executive boards of German companies with up to two thousand employees are small and generally not very specialised, thus reducing the sheer probability of HR directors being on the board. Second, according to co-determination law, companies with more than two thousand employees have to appoint a "labour director", who is responsible for HR issues. However, in most cases the labour director is not the head of the HR department because he or she is often responsible for other issues, as well.

Considering the second indicator, the involvement of the HR department in the development of the business strategy, the authors argue that the indicator itself is flawed. It is not enough to look at whether the HR function participates or not. Instead, one should analyse how HR issues, in general, are considered. Co-determination law provides several paths through which HR issues find their way into business strategy. In large companies, employee representatives as well as union officials are part of the supervisory board of a company, to which the executive board has to report. Moreover, because the works council has a say in issues related to personnel policies, companies that want to implement new HR practices as part of a new corporate strategy are advised to discuss these strategies well in advance. Once an agreement is reached, the process of implementation will be less plagued with resistance. Finally, works councils, at least in large companies, are run quite professionally, with full-time employee representatives and supportive staff. Thus, as Wächter and Müller-Camen (2002) argue, it is not unusual that works councils actively demand strategic changes and put pressure on top management.

The validity of the third indicator, that is, the existence of a written HR strategy, is somewhat questionable in the German context. This is also related to co-determination rights. Wächter and Müller-Camen (2002) argue that because of the continuing need for negotiation typical procedures, *modi operandi* and, thus, a common (although not conflict-free) understanding of strategic issues have developed which are a functional equivalent to written HR strategies.

To sum up, Wächter and Müller-Camen's (2002) analysis challenges the mainstream conceptualisation of Strategic HRM. When operationalised in the traditional way, HR strategy in Germany is indeed not well integrated into the corporate strategy

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– if it exists at all. However, this conclusion is also a product of the sometimes one-sided focus on the HR function. The German approach to Strategic HRM cannot be understood without considering the specific role that co-determination plays. Or as Brewster et al. (1997: 19) suggested, "in the German case the integration of HR issues through the collective cultural consciousness and in legislation may be a more important influence on corporate strategy than the direct integration of HRM through the personnel department."

## The human resource management of foreign owned companies in Germany

So far we have mainly described the interplay of HRM philosophy and labour market institutions from the perspective of indigenous companies. However, one can argue that this perspective may overemphasize the role of these institutions, because German companies have operated within this institutional framework for decades. Thus, they have adapted to the status quo without trying to challenge real or perceived constraints of the system. Therefore, describing the way foreign multinational companies (MNCs) in Germany act within this system is a necessary and valuable supplement to what we have said so far. More specifically, strong "country-of-origin effects" in subsidiaries, that is, the relatively unlimited transfer of home-based industrial relations and HR practices, would challenge the notion of Germany as an *objectively* restrictive business system.

There seems to be an increasing interest in HR policies of foreign MNCs in Germany as it is demonstrated by some recent empirical studies (Ferner/Varul 1999; 2000; Gooderham/Nordhaug/Ringdal 2004; Müller 1998, 1999a; Royle 1998; Schmitt/Sadowski 2003; Wächter et al. 2003; see also Singe/Croucher 2005, this issue). Most of these studies deal with the practices of US or UK MNCs, which seems plausible given the significant differences between the German and the Anglo-Saxon business systems. We want to briefly review the main findings with regard to industrial relations and HR practices.

There is mixed evidence on the compliance of UK and US MNCs with collective bargaining. Based on 13 case studies of UK and US MNCs, Müller (1998, 1999a) reported country-of-origin effects with regard to collective bargaining. That is, five of the subsidiaries rejected collective bargaining and settled for local solutions. Similar results reported Wächter et al. (2003), in their study of ten US MNCs. Some of the studied subsidiaries complied with collective bargaining agreements, but nevertheless had a policy of "keeping the union out of the company". In part, the authors suggested, this strategy has to do with keeping up a "non-union" image in the eyes of the parent country. However, in their comparative survey of 165 UK/US subsidiaries and 132 German firms, Schmitt and Sadowski (2003) found that about 69 percent of the subsidiaries were covered by collective bargaining, a percentage rate even slightly higher than in the German sample. Thus, the evidence on compliance with collective bargaining is somewhat ambiguous. Nonetheless, studies seem to suggest that more subtle forms of resistance seem to be more common than outright avoidance.

Results on employee compensation, which is obviously connected with collective bargaining, point to a home country-effect. Schmitt and Sadowski (2003) found in

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their study that about 56 percent of the employees of UK/US subsidiaries but only 35 percent of the German employees received some from of variable pay. Müller (1999b) observed that the subsidiaries that rejected collective bargaining also tended to pay more performance related incentives.

With regard to compliance with co-determination Schmitt and Sadowski (2003) reported that an astonishing 86 percent of the surveyed UK/US subsidiaries had a works council, while this was the case only for 70 percent of the German sample. They termed this an "overshooting" host-country effect. They hypothesized that the subsidiaries seek to give the impression of being "good corporate citizens" (Schmitt/ Sadowski 2003: 420). Moreover, they reported additional survey data that showed that the subsidiaries regard the works council as an important channel for communication between management and employees. Wächter et al. (2003) also observed a high agreement with co-determination, while the case study evidence from Müller (1999b), who found that 6 of 13 UK/US MNCs did not or only partly complied with co-determination, somewhat deviates from this general picture. Wächter et al. (2003) provide some interesting insights on the handling of work councils in US subsidiaries. They found that the studied subsidiaries were quite active and innovative in their relationship with the works council. They used the flexibility which is inherent (but not always recognized) in co-determination law. By keeping the trade unions out of the companies, the works councils function as part of management, for example, supporting it in issues of organisational change.

There are also examples, however, of MNCs that instead of dealing innovatively with co-determination try to avoid it (Royle 1998; Wever 1995). Based on a case study of McDonalds, Royle (1998) developed a typology of strategies that companies can use to avoid or at least weaken works councils. Except for illegal measures, such as harassment and threatening behaviour, all strategies are well within legislation, but they make use of loopholes or simply take advantage of the flexibility of the co-determination law. Strategies that point at avoiding the establishment of a works council are, for example, to transfer corporate units into different 'ownership', or using a marginalised or transitory workforce with less willingness to establish a works council or to simply close a unit and rebuild it with a different workforce. Strategies to weaken the influence of works councils are, for example, to buy-out employee representatives to let works councils collapse or to nominate "company-minded" employees for works council elections.

On the issue of initial vocational training there seems to be a more pronounced country-of-origin effect. In Schmitt and Sadowski's (2003) study about 75 percent of UK/US subsidiaries participated in the vocational training system, while in the German sample about 88 percent of the companies did. Moreover, the rate of apprentices relative to the whole workforce is 2.6 for the subsidiaries and 5.3 for the German sample. Instead, UK/US subsidiaries seem to rely more strongly on on-the-job training, the preferred form of training in the home country (see also Müller 1998).

In general, whether country-of-origin effects or host-country effects in UK/US subsidiaries can be found seems to be dependent on the attribute at which one looks. Works councils have obviously been accepted as integral parts of the German economic system. Some subsidiaries have found innovative ways to integrate it into the

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companies' strategy of internal communication. The results for collective bargaining are mixed, although it seems that the system leaves enough leeway for UK/US MNC's to implement variable pay schemes. For initial vocational training the impact of the home country seems to be stronger. The differences between these characteristics may, as Schmitt and Sadowski (2003) argue, have to do with their visibility. Rejecting the establishment of a works council may evoke considerable public attention (for an example see Royle 1998), while this is less so with regard to the preference for performance-related pay. In sum it appears that the German business system is not as restrictive as it is often suggested. As Wächter et al. (2003: 105-106) put it: "Potential investors tend to regard the German system as being very strongly regulated. They focus particularly on hard factors such as indirect labour costs and often fail to recognise the scope for flexibility which the German system does offer… Companies which have invested successfully in the German business system have learnt how to challenge and use institutional restrictions in order to be locally responsive to the rigidities of the system at the same time as being able to implement standardised HRM strategies. Such companies place significant demands on the German system with the result that their German subsidiaries are successful and productive."

## Conclusion

Organizations need to strive for efficiency in order to survive in competitive markets. Management phenomena like outsourcing or downsizing have become institutionalized practices. Organizations imitate each other not only domestically but increasingly on a global scale. However, mimetic isomorphism is just one facet, coercive isomorphism or more broadly speaking national business systems moderate the dissemination of management practices. The outsourcing package chosen or the downsizing method utilized is heavily influenced by norms and values preferred by society.

Human resource management in Germany is rooted in its historically grown and legally shaped institutional environment. HR practices from the US are not ignored, but quite the opposite, often initially taken up without critical reflection. However, organisations adapting to societal demands in order to survive are eventually forced to analyse whether these practices may be customized to the national business system. Thus, a strong position towards a universalist HRM approach may be at odds with institutional demands requiring to take context into account in order to gain legitimacy.

Human resource management in Germany, however, is also unique for a different reason: re-unification. Organisations in former East Germany (*Neue Bundesländer*) had to cope with a radical change in the institutional environment. As a consequence, human resource management in the western part of Germany (*Alte Bundesländer*) and in the eastern part of Germany (*Neue Bundesländer*) has been and still is quite different. Based on the data of the Cranfield Project, Kabst (2001) analysed what HR managers perceived to be the major challenges for HRM in the early nineties, mid nineties, and end nineties. Whereas HR managers in the *Neue Bundesländer* perceive their room to manoeuvre in respect to HRM as significantly limited by the overall challenge to restructure and the need for staff reductions, even a decade after re-unification, HR managers in the *Alte Bundesländer* perceive the need to adapt to institutional restraints to be less demanding, offering scope for customized HR philosophies.

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Summarizing the above reasoning, institutional pressures originating from the national business system clearly need to be addressed when discussing HRM. Without doubt, this requires more attention across Europe than within North-America. Germany, at first glance, may be an example of a rather restrictive business system, throwing into question the scope for an active and strategically oriented HRM. This is, however, an oversimplification, both in respect to differences between different human resources domains as well as in respect to the differences still existing between the *Alte Bundesländer* and the *Neue Bundesländer*.

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