

Advancing Backwards: Why Institutional Reform of German Federalism Reinforced Joint Decision-Making

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A series of recent reforms in German federalism have created a dynamic development unprecedented in the Federal Republic. They aimed at increasing federal and Länder governments' autonomy by decentralization and separating powers. Being negotiated in established structures of joint decision-making, significant change could hardly be expected. However, change evolved in a sequential process triggered by particular conditions: decisions of the constitutional court in the first federalism reform, the broader fiscal and economic crisis in the second, and a deadline to renovate the fiscal equalization scheme in the third. After first steps to decentralize powers, subsequent reforms reinforced cooperative federalism, but with an even stronger role of the federal government. Following a comparative-historical institutionalist perspective, the federal dynamics can be explained by the interplay of established institutions, routinized negotiation systems and different events triggering change. In contrast to the gradual evolution of cooperative federalism, these triggers caused unintended and contradictory effects.

In comparative research, the German federal system has been considered fairly stable. While some view this stability as a consequence of a homogeneous society and an integrated party system (e.g., [Watts 1999](#)), others emphasize the strong predisposition toward power sharing and negotiated agreements causing the “joint decision trap” ([Scharpf 1988](#)) and institutional rigidity. Against this backdrop, the series of constitutional amendments which changed the federal order in Germany over the past two decades are noteworthy both regarding the process and outcome and the implications for theory. On the one hand, federalism reform responded to altered societal conditions and changing party politics that threatened to destabilize the federal order. On the other hand, these amendments materialized despite difficult institutional conditions for institutional change. For both reasons, this case challenges existing theories of constitutional policy-making and theories of historical institutional change that assume path-dependent evolution of complex institutions with significant turns only materializing in situations of critical

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junctures. Recent changes in Germany do not fit well with these theoretical lenses; therefore, the peculiar dynamics between change and continuity in Germany's federal order outlined below invite our analytical attention.

Two particular features of change of German federalism need to be highlighted from a theoretical point of view. First, reform did not succeed after German unification, despite intense discussion about the need for renovating the federal constitution and even though the federal parliament and the Bundesrat set up a commission preparing a revision of the constitution. If there was a "window of opportunity" for a reform, it was not seized in those days (Jeffery 1995), whereas more than two decades later, a reform process has ended with considerable amendments to the constitution. The second aspect to be noted is the sequence of reforms ensuing after the first constitutional amendments did not meet all expectations of parties and governments. So far, scholars have not studied the reform process in a broader temporal perspective. Rather they focused on the first reform or at best considered the second step, and they explained specific results or evaluated the outcome and consequences of the reform. Moreover, only a few studies used the case of German federalism reform to apply and test theories of institutional change. As we outline in the ensuing section, these studies have so far ignored the challenges this case poses to theories of historical institutionalism.

The following study adopts a comparative historical analytical perspective (see e.g., Mahoney and Thelen 2015). Yet, we suppose that the historical development of complex institutions and federal dynamics cannot be reduced to an alternation between path-dependent evolution and critical junctures. The latter do not always lead to institutional change. Nor can we rule out that intended institutional change may succeed outside such situations. For this reason, we need to go beyond the concept of critical juncture, although we adopt the idea that external impulses are essential to explain change in systems of joint decision-making.

Inspired by the analytical framework of federal dynamics (Benz and Broschek 2013), we place recent reforms of German federalism in a long-term perspective. Accordingly, we observe that crucial historical developments like German unification have turned into a process of incremental adjustment, and the same applies to impacts of European integration after the substantial treaty changes in 1992. Therefore, these "critical junctures" did not induce the sort of significant change usually suggested by the concept. Reform processes set in under more stable conditions, when governments tried to extend their autonomy to change policies. Therefore, rather than exploiting extraordinary situations in which constraints by rules and routines are suspended, they deliberately addressed institutional constraints. To understand institutional changes resulting from these processes of reform, we need to explain why the trap of joint decision-making could be avoided and why constitutional amendments passed the legislative chambers. We argue that dynamics of each partial reform was triggered by

particular factors modifying the status quo and thus the consequences of a deadlock in policy-making. Moreover, in order to explain the overall change of the federal system, the sequence of reform policy needs to be taken into account. Whereas in joint decision-making, we could expect an incremental evolution in a certain direction, the different external triggers affected the three reform sequences in different ways so that the process set in motion in the first stage later ‘advanced backwards’ and reinforced the existing historical legacy of joint-decision-making.

Consequently, without neglecting the historical context, the societal conditions, and the particular patterns of negotiation and decision-making, we focus on the effects of external triggers for change and the recursive processes resulting in inconsistent change that finally supported continuity. As we demonstrate in our case study analyzing three consecutive reforms of German federalism, change was triggered by particular events. They influenced the agenda and substance of reform policy and compelled actors to come to a decision despite the enduring constraints of joint decision making. Thus, our study contributes not only to making sense of the complex dynamics of change and continuity in the German federal order, but also to further theorizing opportunities and boundaries of institutional change especially in federal systems.

Institutional Change Causing Continuity: A Theoretical Framework

State of Research

Change in federal systems has been addressed in different strands of theorizing. Some highlight the dynamic character of federalism as a process coevolving with society; others emphasize the causes of continuity in the sense of a steady evolution without major disruptive events or far-reaching turns of the direction of development. Continuity and change have been analyzed as caused by evolving or constraining structures or as results of policy-making coping with institutional constraints or aiming at institutional reforms.

One cause of political development in federal systems lies in the very nature of these systems. They constitute both a *demos* and multiple *demoi*, while providing different venues for political participation (Lancaster 1999). Their structures and operation are thus affected by changes in society in complex ways. Society-centered theories of federalism have emphasized the general impact of society on federal structures (Erk 2008; Livingston 1956). Economic and social changes can affect the allocation of resources between jurisdictions, social cleavages, or party politics. However, these effects do not lead to institutional change without policies reacting to them. Moreover, although the integration or disintegration of a party system matters in federalism, it is not clear whether it causes dynamics of federal structures (Riker 1964) or whether parties adjust to them (Chhibber and Kollman 2004).

Continuity of structures and institutions has been explained by historical institutionalism, a particularly relevant theory for understanding the gradual evolution of federal systems (see e.g., Broschek 2012, 2013; Pierson 1995). The complex institutions designed to divide and share power inside and between governments are founded on constitutional rules, emergent norms of interaction across boundaries of jurisdictions, and ideas guiding and legitimizing a balance of power. From an institutionalist, particularly historical, perspective, these institutions, designed to address collective action dilemmas and embedded in social structures and discourses, tend to constrain the scope of change to a path-dependent, incremental, sequential development (e.g., Pierson 2000; Thelen 1999). However, scholars applying historical institutionalism have defined institutions both as rules constraining actors' behavior and as social constructions by actors pursuing their interests (Immergut and Anderson 2008, 348). They point out that rules, powers and ideas are never in full accordance (Lieberman 2002), as has been observed in particular in federal systems (Broschek 2012). Instead, institutions create tensions that actors have to cope with. In turn, strategic action to cope with tensions induces change, sometimes with significant consequences. However, these approaches cannot explain sufficiently how change occurs or how tensions are coped with.

At the same time, historical institutionalist perspectives, while emphasizing constraints on change, path-dependency, as well as unintended consequences of institutional reforms, by no means amount to postulating an impossibility of reform and even intended change. For one, scholars have pointed to the necessity of capturing more gradual, incremental and less obvious or 'hidden' change that may occur, e.g. through institutional layering, drift and conversion (for an overview, see Hacker, Pierson and Thelen 2015; Mahoney and Thelen 2010). With regard to more far-reaching changes, reforms, and especially constitutional amendments, of particular importance are the notions of "punctuated equilibrium" (see e.g., Baumgartner and Jones 1993) and "critical junctures" (see e.g., Capoccia 2015) or "focusing events" (Birkland 1998). In simple terms, the latter may be construed as moments (e.g., unexpected events, crises, shocks, etc.) interrupting or loosening the constraining effects of entrenched institutional parameters. They may open up "windows of opportunity" for political change, leading to an overall pattern of more or less continuity in the evolution of a political system or institutional framework "punctuated" by or interspersed with various moments of change. However, whether or not such events actually lead to change will be contingent on a number of circumstances and the actors themselves (see e.g., Soifer 2012). While these theories give reasons for expecting change, they cannot explain appropriately why or under which conditions it occurs and in which direction it develops.

Therefore, approaches addressing policymaking intended to amend or reform institutions should be linked to historical institutionalism (Benz and Broschek 2013). In this context, modifying the guiding ideas and interpretation of rules, amending rules, and revising patterns of interaction or standard operating procedures should be taken into consideration. Accordingly, theories of discursive institutionalism (Schmidt 2010), joint decision-making and intergovernmental negotiations (Scharpf 1997), the multiple streams approach (Kingdon 1995), or theories of policy learning (see e.g., Hall 1993; Sabatier and Weible 2014) can indicate causes and effects of intended or unintended change. Beyond that, comparative policy studies have pointed to party politics, interest intermediation, or veto players as determinants of policy change (Armingeon 2002; König 2010; Schmidt 2002; Tsebelis 2002).

Scholars studying particular reform processes in German federalism have selectively used these theories to explain processes and outcomes. Among them, discursive institutionalism, which draws attention to ongoing re-negotiations of institutional norms, has been rarely applied. This is understandable since this relatively new approach explains endogenous institutional change, while most scholars are interested in reform processes. Nonetheless, some scholars have included ideas and discourses in their analysis of dynamics of federalism and reform processes. Annika Sattler (2012) studied the discursive quality of negotiations in the commissions preparing constitutional amendments passed in 2006 and 2009 and found that patterns of arguing influenced the decisions although bargaining behavior finally prevailed. Others interpreted constitutional negotiations as typical federal-*Länder* bargaining and therefore applied the concept of joint decision-making to explain reform outcomes (Auel 2008, 2010; Benz 2008; Burkhart 2009; Scharpf 2009). In this case, no elaborated reform concept guided the process. Rather, the process was dominated by particular institutional or policy interests of governments or administration. Therefore, this approach appears appropriate to explain compromises and package deals in negotiations characterized by a particular institutional context and particular patterns of constitutional negotiations (for a comparative perspective, see Behnke and Benz 2009; Benz 2016; Broschek 2015). Among these contextual conditions, some scholars have highlighted the party system and party politics (Detterbeck 2016). Indeed, the changing party system has caused new challenges for German federalism, but parties have not been major players in reform policies. Similarly, problem and politics streams have contributed to setting the agenda of federalism reform (Sturm 2010), but the multiple streams approach does not explain negotiations, decisions, or outcome of the reform.

Only a few scholars have so far discerned particular features of the processes and conditions characterizing the three reform sequences evolving in German federalism over the last two decades. Recently, Sabine Kropp and Nathalie Behnke

addressed the interplay of these sequences and dynamics of reform (Behnke and Kropp 2017). They described this process as a zig-zagging between attempts to disentangle shared powers and decisions which reinforce joint decision-making (Kropp and Behnke 2016). Thus, we observe change; but overall the effects are contradictory and neither meet the intentions of reform policy nor do they substantially renovate or “modernize” German federalism. This “stop and go” policy is unusual for systems of joint decision-making.

Theoretical Framework

In order to explain this outcome, we need to understand both continuity and change of German federalism (Benz and Broschek 2013). Continuity can be traced back to the historical legacies which, as Gerhard Lehbruch has demonstrated, particularly concerns the development of a cooperative federalism that evolved through centuries of power sharing between the governments of the federation and of the *Länder* (Lehbruch 2002). These legacies found expression in patterns of joint decision-making requiring agreements between federal and *Länder* governments when exercising shared powers. In constitutional or institutional reform involving a redistribution of power and resources, this pattern should constrain the scope of change, if we follow existing theories (Scharpf 1988). Yet, constitutional policy in Germany considered in the following section does not conform to these assumptions. On the one hand, all three reforms ended with constitutional amendments, with considerable effects on policy-making in federal and *Länder* governments. On the other hand, in contrast to what both the theory of joint decision-making and the concept of path dependence suggest, the outcomes of the individual reforms did not point in the same direction. Rather they appear as one step forward towards a separation of power and decentralization and two steps backwards towards power sharing and centralization.

So why did the reforms end with notable constitutional amendments, but with change going in different directions? Institutional conditions, party politics, and patterns of negotiations hardly varied and cannot provide the answer to this question. For the first two reforms, the federal parliament and *Länder* governments established a joint commission. The third reform was negotiated in usual intergovernmental conferences in the executive, but this did not make a significant difference since all processes conformed to the typical pattern of joint decision-making. What made a difference were external factors. In line with theories of historical institutionalism, one could argue that change occurred in response to critical junctures. However, although we adopt the idea that external impulses are essential to induce change, especially in systems of joint decision-making, there is much reason to doubt that the evolution of German federalism can be explained as an alternation between path-dependent evolution and critical junctures, as the

latter do not necessarily lead to institutional change, while intended institutional change may succeed outside extraordinary situations. Moreover, the concept of critical juncture does not allow us to distinguish between different situations and their particular effects. Instead, our analytical framework pinpoints various crucial triggers for change to capture the dynamics of federalism reform in Germany of the recent past. They are crucial because they modify the status quo in the particular policy and thus compel actors to respond to this externally determined change and to cope with institutional constraints.

Three types of external triggers can be observed in our case, with effects differing considerably. They emerged in the actor constellation, in the relevant policy field, and in the temporal dimension of policy-making. Without claiming to cover all possible types, we can conclude from this observation that change can be triggered by decisions of external actors, a crisis situation, and the pressure of a deadline for making a decision.

- *External actor*: Actors not involved in policy-making processes can trigger change if they modify ideas, patterns of interactions, or effective institutional conditions. Actors changing institutional conditions are most relevant, since they modify the power structure at the cost of those defending the original status quo. Thus, they undermine the positions of veto players and increase the pressure for policy-makers to renovate institutions in response to an actually altered status quo. Presumably, this kind of external trigger is conducive to significant and substantial change, as it directly affects the balance of power among policy-makers and their strategies of negotiation. By influencing or supporting ideas of a reform, these actors might even affect the substance or direction of change.
- *Crisis*: A crisis usually creates conditions for a critical juncture. In a short period arising during a historical process, it can open a window of opportunity to change the direction of an evolutionary path. It does so by weakening the constraining effects of institutions (Capoccia and Kelemen 2007, 342), which may prevent actors from responding to a crisis. However, critical junctures are embedded in a historical evolution of institutions and practices which affect how actors respond to pressure or opportunities for change (see e.g., Capoccia 2015). Although the situation opens room for maneuver for actors, the existing institutions remain in place. Therefore, the effects of a crisis are all but certain. “If an institution enters a critical juncture, in which several options are possible, the outcome may involve the restoration of the pre-critical juncture status quo” (Capoccia and Kelemen 2007, 252). Change in a critical situation implies an intervention into those mechanisms causing path dependence, and this intervention is a political process on its own. Under these conditions, it is essential to turn “permissive conditions” into “productive conditions” (Soifer 2012) in order to elicit reform or institutional change. In a crisis which comes as

an external shock, continuity often prevails even in the presence of permissive conditions, since outcomes of changes are uncertain. This does not rule out the possibility of the crisis setting in motion mechanisms of change, yet much depends on established patterns of policy-making on the one hand and on strategic choices of actors operating within this established environment on the other. In a fiscal crisis, governments in centralized systems tend to exploit this situation in order to further concentrate power, whereas political actors in multilevel governance systems usually prefer cooperation and sharing of responsibility (Braun, Ruiz-Palermo, and Schnabel 2017).

- *Pressure of Time*: Time matters for politics of institutional change in general (Pierson 2004). The relevance of temporal factors applies likewise in the more short-term or immediate context of politics. Policy-makers confronted with a deadline might still fail to reach an agreement. However, different kinds of deadlines have to be distinguished. Usually, they simply end a process, e.g., if the election period of a parliament or government terminates or if committees' time to work on an issue runs out. Yet, deadlines can also modify the status quo, if they imply that a program or a law ceases to be in force. The pressure for policy-makers to come to a decision increases if the constitution requires a replacement of a law endowed with a sunset clause. In this case, change is necessary, but the substance of change will probably turn out as modest. Under the pressure of time, actors usually are not able to agree on significant changes or innovative solutions, and may even accept problematic deals.

In general, the degree and scope of institutional change increase if processes evolving under the mentioned conditions of external triggers combine to a sequence. In this case, change may accumulate. The consequences of an accumulation depends on how external triggers affect the power structure in a particular reform process and whether and how further change occurs in response to outcomes of previous processes (see e.g., Pierson 2015). As we will see in the following case study, a sequence of reforms influenced by different external triggers can also produce contradictory outcomes. Power structures may vary in the different stages, and those losing in one of them might be able to exploit changed conditions to restore their power in a later stage. This is to be expected especially if a reform requires a negotiated agreement of different actors pursuing incongruent interests, such as regarding policies designed to amend a federal constitution.

Politics of German Federalism after 2000

It is obvious that the German system has changed, despite a dense net of interlocking institutions and joint decision-making. However, change by and large did not occur due to extraordinary critical junctures. Under those circumstances,

continuity and path-dependent adjustments to altered conditions predominated. At the same time, change has been achieved “against all odds” of institutional constraints in periods of political stability. German unification and the process of European integration, the former a critical juncture and the latter an evolutionary change, illustrate this point. Unification had, barring a few minor amendments to the constitution, no noteworthy effect on the vertical division of powers and even stabilized the federal system. This should appear surprising since reunification between East and West Germany in 1990 constituted an exceptionally epochal moment opening a window of opportunity for an overhaul of the constitution. After all, the West German Basic Law (*Grundgesetz*) was officially considered a “*Provisorium*”, i.e., an interim constitution until overcoming the division of Germany. It even included with Article 146 a provision specifically for this scenario. And yet, other than the addition of five new “*Länder*”, reunification elicited no relevant amendments to German federalism. Concerning integration in the European Communities and the EU on the other hand, the federal system was incrementally adjusted to various treaty revisions as well as regular policy-making and regulation within the European multilevel system (Wachendorfer-Schmidt 2003). Yet, the structures of cooperative federalism remained intact (Goetz 1995).

With the turn to the 21st century, German federalism became the subject of increasing debates and calls for constitutional reform. For one, the German government tried to meet the challenges of economic recession following the creation of the Eurozone and the growing pressures for competitiveness and flexibility in a Europeanized and globalized market. Moreover, the fiscally well-off *Länder* governments increasingly called for reducing the intensity of fiscal equalization and federal interference into their domain. This represented at least in part a “delayed” consequence of German unification, since the inclusion of fiscally weak *Länder* in East Germany into the system of fiscal federalism and horizontal and vertical redistribution caused significant asymmetries (Benz 1999). At the same time, there was heightened concern about potential deadlock on account of countervailing majorities in the *Bundesrat* (the legislative chamber representing *Länder* governments) vis-à-vis the federal parliament and government in Germany’s extensive system of joint decision-making. The immediacy of reform was underlined by the dynamics of European integration, with the risks of domestic deadlock seen as threatening Germany’s capacity to act at European level. In consequence, federal and *Länder* governments embarked upon a major reform project in the early 2000s dubbed a “modernization” of German federalism. The explicit goals were to disentangle and reallocate a wide range of decision-making competences to make governing in Germany’s federal system more accountable, effective, and flexible.

According to theoretical reasoning (Lehmbruch 2002; Scharpf 1988), established patterns of joint decision-making should have only permitted incremental change.

Yet in this respect, recent experience has defied expectation. A series of reforms of German federalism were undertaken with the goals of making the federal order less entangled by joint-decision making and more flexible. However, the different reforms initially advanced towards the intended reform goals, but then turned “backwards” in subsequent reform stages—i.e., toward more “entanglement,” joint decision-making and centralization. As we will show, different external triggers caused change, but in combination they did not drive reforms in one direction.

The First Step: Reform Triggered by the Federal Constitutional Court

As of 1998, a center-left coalition of the Social Democrats (SPD) and the Green Party formed the government, soon after which a countervailing majority emerged in the *Bundesrat* following several *Länder* elections. During the 1990s, the opposite constellation was to be found, e.g., a center-right (Christian Democrat and Liberal) coalition in government facing a majority of SPD-governed *Länder* in the *Bundesrat*. Both constellations proved difficult for reaching agreements in policy-making, especially where landmark legislative proposals were concerned. However, the variety of coalitions at *Länder* level increased after 2000, rendering it even more difficult to anticipate *Bundesrat* vetoes (Detterbeck 2016). On the other hand, the *Länder* governments, in particular those led by Christian Democrats, called for decentralizing competences in order to make policies on their own instead of merely obstructing federal legislation. In this context, the re-allocation of competences and especially the idea of “disentanglement” and thus retrenching cooperative federalism became a dominant motive (Gunlicks 2005; Meyer 2008; Scharpf 2009).

Thus, both federal and *Länder* governments agreed on the need for constitutional reform of the federal system. To this end, they set up a “Joint Commission of the *Bundestag* and the *Bundesrat*” for the ‘modernization of German federalism’ (2003–2004). It comprised an equal number of representatives from both houses of the federal legislature, with the *Bundesrat* delegating one representative per *Land* government. Though it constituted a special body, the commission essentially mirrored the composition of the federal legislature, while its decision rules conformed to the requirements of a constitutional amendment, namely a two-thirds majority in the *Bundestag* and the *Bundesrat*. Consequently, the familiar interplay between party politics and intergovernmental relations in German federalism was institutionalized into this reform process from the outset, with the commission designed to anticipate vetoes in the legislative process. As is typical in German politics, the different party groups and the *Länder* governments met in separate meetings in preparing plenary sessions of the commission, while the federal and the *Länder* governments each relied on the support of their

administrations to conduct problem analysis and draft amendment proposals (Benz 2008).

As a rule, in constellations of joint decision-making requiring consensus or super majorities, bargaining actors cannot reach a compromise on matters concerning the redistribution of powers or fiscal resources. If they manage to do so, this tends to entail then a package deal or a “least common denominator” compromise (Scharpf 1988, 2009). Given the design of the reform commission, it is unsurprising that the participating governments agreed early on to omit the redistributive issues of fiscal federalism and allocation of financial resources from the agenda (Jochimsen 2008). Instead, the commission aimed at a compromise to modify rules on veto powers of the *Bundesrat*. In turn, the federal government was expected to accept a decentralization of powers and legislative competences through significant concessions to the *Länder* governments. However, the willingness of federal and *Länder* governments to separate powers was not sufficient to enable an agreement. In December 2004, the commission ended its final meeting without deciding on a paper tabled by the chairs of the commission summarizing negotiations results. Still, a complete failure of the reform was avoided after the 2005 federal elections resulted in a Grand Coalition government. From the outset, the party leaders negotiating the coalition treaty revived the proposal of the commission and settled the remaining disputes.

A grand coalition was certainly in a position to achieve a broad majority in parliament. However, the Social Democrats and Christian Democrats could not count on a two-thirds majority in the *Bundesrat*. Therefore, this party constellation in the federal government was not decisive to eventually pass constitutional amendments. In fact, the Joint Commission had been close to reaching an agreement after the federal government decided to concede legislative powers to the *Länder*. It finally did so in response to decisions of the Federal Constitutional Court (FCC), though it would take until after the 2005 elections until the first federalism reform would pass.

As Fritz W. Scharpf (2006) suggested, the court, an external actor not involved in constitutional negotiations, induced change, and it did so because its decisions de facto changed the allocation of power between federal and *Länder* governments. The FCC, which usually decides in accordance with mainstream discussions in politics and society (Vanberg 2004), supported the basic idea of decentralization and disentanglement. In several judgments since 2000, it had reinterpreted the grounds for justifying federal legislative power in matters of concurrent legislation (Benz 2017, 217–218). As a result, these decisions denied the federal government the wide leverage it had become accustomed to over the decades prior. Eventually, the federal government became aware of the real implications of the Court’s revised interpretation of the subsidiarity principle. Not only had it become easier (and more likely) for *Länder* governments to successfully challenge federal

legislation as *ultra vires*, the federal government now also had to face the possibility of losing power to change existing federal laws or parts of them. Under these conditions, the federal government saw the urgent need to revise constitutional rules determining the distribution of legislative powers, and it could achieve this only by transferring powers to the *Länder*. Hence, to avoid the risks of unregulated decentralization, fragmentation of the law and legislative insecurity, the federal government elaborated a list of legislative powers to be transferred to the *Länder* (Burkhart 2009, 346-348; Scharpf 2009, 96).

Following rather swift reform negotiations transpiring in tandem with the negotiations to form a coalition government in 2005, the constitutional amendment passed in June 2006. It modified the distribution of legislative powers and the conditions for a veto right of the *Bundesrat* in federal legislation. In line with the motive of disentanglement, the *Länder* gained sole competence in several areas, most notably over higher education policy and the remuneration of their civil servants, while the federal government had to make due with a slightly decreased number of laws requiring *Bundesrat* assent. This package deal, as well as the exclusion of important issues like fiscal federalism from the reform, demonstrated the constraining effects of joint decision-making in German federalism, but also made clear the enabling effects of the FCC. The constitutional changes achieved in the first reform related predominantly to those matters affected by court decisions. They motivated the federal government to give up its defensive bargaining strategy when it realized that its legislative powers could be undermined by court rulings. Regarding the veto power of the *Bundesrat*—the other part of the package deal—the federal government had to accept a compromise that hardly met expectations. However, since court decisions had changed the fallback position to the disadvantage of the federal government, it had to accept this outcome.

Incidentally, the result (as much as the negotiation processes themselves) wholly conformed to the joint-decision logics embedded in the German system of federalism (Benz 2008; Scharpf 2009). Dynamics of the policy process can be explained by an external trigger. The court in this case supported the aim of the reform, namely decentralization and disentanglement. However, the effect of this trigger remained limited. Important reform issues, fiscal federalism above all, were postponed for a second commission to address. As it would turn out, this time reforms would have to transpire in the context of a crisis.

The Second Step: Reform during the Fiscal Crisis

The decision to start a second reform process was made with the passage of the first legislative package in 2006. Again, the *Bundestag* and the *Bundesrat* established a Joint Commission. This time the commission excluded experts from participating

as members and instead started its work with public hearings. Moreover, the *Bundestag* sent four members of the federal government into the commission, putting the executive in a stronger position in negotiations than in the previous commission. As in the first reform, the agenda for the second reform, negotiated between 2007 and 2009, was set by a comparable interplay of political bargaining, administrative negotiations and court decisions. It found expression in a compilation of questions collected by federal and *Länder* departments, comprising a list of about 500 more or less detailed issues. Again, an impetus was also provided by the FCC. In this case, it was a decision on a proceeding initiated by the government of Berlin requesting special federal subsidies due to its budgetary problems. In 2007, the court ruled against Berlin, but demanded appropriate mechanisms to prevent *Länder* governments from running excessive deficits. The commission acknowledged the decision as a clear order to amend the constitutional rules on deficit spending and to work out an early-warning mechanism for budget policy. However, it was also around this time that the international financial market crisis and the domestic economic crisis broke out.

Economic and fiscal crises in particular can turn out to present profound challenges precisely because they affect the distribution of funds or even call for bailing out constituent units in economic dire straits (Rodden 2006). In retrospect, Germany was able to weather the crisis not only due to basic features of its economy but also thanks to its strict welfare and labor market reforms already undertaken before the outbreak of the crisis (Bonatti and Fracasso 2013; Young and Semmler 2011). However, this should not overshadow the fact that as of 2008 the fiscal crisis heavily affected Germany.

At first, the recession primarily hit the car industry. Second, the banking crisis severely destabilized multiple financial institutions on the Land level, especially regional public banks (*Landesbanken*) in Hamburg/Schleswig-Holstein, North Rhine-Westphalia, and Bavaria. One private bank, Hypo Real Estate, was so beleaguered that it not only received a massive bailout, but eventually was nationalized. Thus, *Länder* with relatively strong economic and fiscal capacities had to confront major effects of the turbulences in the global market. The federal government responded to these problems in close cooperation with *Länder* governments. In addition to several major bailouts in the banking sector, it established a stimulus package to induce public investments especially in infrastructure projects, and demands in the ailing automobile sector such as a 'scrapping bonus' for buying new cars (see e.g., Becker, Höreth and Sonnicksen 2010; Zolnhöfer 2011). These policies, designed to overcome the recession, caused a rapid growth of public debts. They developed at a time when debates about the level of public debts intensified and all governments irrespective of party complexion faced considerable public pressure to reduce the debt load. Therefore, public bailout and stimulus expenditures stood in sharp contrast to the new

consent on budget consolidation. Hence, German governments had to demonstrate that they would soon return to a path of fiscal austerity. Crisis management thus turned into a policy of budget consolidation in tandem with the EU's approach toward struggling Eurozone economies, a policy in which the German government would be playing a pivotal role (Bulmer and Paterson 2013; Young and Semmler 2011).

Moreover, the conditions for consolidation had changed due to the crisis. Because it hit the well-off Western *Länder* even more than economically weaker ones, new imbalances in the federal system became apparent. The fiscal capacities of the *Länder* differ significantly, with Bavaria, Baden-Württemberg, Hamburg, and Hesse profiting from strong regional economies and tax resources, while the fiscal equalization scheme has helped minimize revenue disparities (Hepp and von Hagen 2012). Yet, when taking account of public expenditures and the risks for future budgeting, a different divide appears, since a number of Western *Länder* are confronted with excessive debt loads that are predicted to increase in future (Hildebrandt 2009). Adding to new cleavages between *Länder* governments, the waning of integrative effects in the party system (Detterbeck 2016) exacerbated consequences of the fiscal crisis.

Subsequently, any ambitions to disentangle the system of shared taxes turned out to be unfeasible. While most *Länder* governments feared the risk of tax competition, other governments such as in Baden-Württemberg, Hesse, and Bavaria demanded more fiscal autonomy and increasingly questioned the need for horizontal fiscal equalization, at least to the extent required by the existing law. While contributing to an erosion of the once dominant unitarist paradigm of German federalism, these debates did not lead to further institutional decentralization. Quite the contrary, the crisis constrained the ongoing reform of German federalism. While governments realized the need for reinforced federal-*Länder* coordination in fiscal policy, they postponed yet again significant modification of fiscal equalization. In the wake of the fiscal crisis, the second reform commission narrowed its agenda (Heinz 2012; Renzsch 2010).

As with the first commission, the representatives of *Länder* and federal governments excluded issues that would require decisions with redistributive effects. Consequently, the commission did not take up reform of fiscal equalization either. While a wide range of fiscal federalism matters were certainly discussed, in the end, members of the commission only reached compromises on several administrative issues and on managing public deficits. As to the latter, they proposed a new debt rule and a joint monitoring system, the "Stability Council," for budget policy of the federal and *Länder* governments (Korioth 2016). Both proposals passed legislation by the required majorities.

Consequently, and in contrast to the motives of disentanglement and separating powers guiding the first joint commission, the second federalism reform

introduced additional joint tasks and corresponding institutional structures (Seckelmann 2009). Federal and *Länder* governments have not only maintained the long-established and extensive shared taxation powers and shared revenue, a hallmark of German cooperative fiscal federalism (Adelberger 2001; Conrardt and Langenbacher 2013, 314-317; Egner 2012, 90-120). Moreover, they now coordinate their budget in an institutional setting similar to those of the old “Joint Tasks”, i.e., those areas of policy making where the federal government is compelled to cooperate with *Länder* governments in fulfilling those tasks (Article 91a of the Basic Law). Decisions of the Stability Council are not binding for parliaments, and governments refusing to implement the recommendations cannot be sanctioned. However, the monitoring mechanism in budget policy implies a process of naming and shaming, and enables comparative evaluation of budget policies by parliaments (in particular opposition parties), private interest groups or the public (Heinz 2016). This way governments and majority parties in parliaments have an incentive to avoid budget crises. For the *Länder* this implies the need to cut expenditures given the continued lack of autonomy over revenue. Under these conditions, the room for new public services, investments or salary increases for civil servants is limited. These limitations, furthermore, have been exacerbated, certainly unwittingly, by several previous changes achieved in the first federalism reform prior to the economic crisis, since the federal government’s power to provide grants to *Länder* and local governments had been restricted. While the *Länder* gained more autonomy in some legislative areas, this transpired without nearly any counterpart on the revenue-raising side. For these reasons, the *Länder* (and their municipalities no less) face severe and, ultimately, self-incurred pressures to cut expenditures.

Thus, the economic crisis of 2008 clearly can be regarded as a critical period for federalism, and it operated as an external trigger like the FCC in the first reform. Yet, the effect of the crisis was quite different. While the court decision on federal legislation altered the constitutional status quo, the crisis required immediate reactions deviating from the policy of budget consolidation the federal and *Länder* governments had adopted. Constitutional amendment then aimed at entrenching this policy in the Basic Law for the future. Beyond that, federal and *Länder* governments postponed all further changes in fiscal federalism in view of the uncertain implications of potential amendments in times of economic turbulence. Therefore, if an economic crisis had the potential to create a critical juncture in institutional evolution, it had the opposite effect under the particular conditions of German federalism. While governments agreed on joint measures to stimulate the economy and prevent banks from failure, the crisis intensified conflicts on institutional change. It obstructed joint decision-making on a redistribution of power and only allowed an amendment of constitutional rules which reinforced the existing power structure. Evaluated according to the previous aim of increasing the autonomy of the *Länder* governments, this second reform was a step back.

The Third Step: Reform under the Pressure of Time

After the second reform of German federalism, fiscal equalization remained on the agenda. Despite the recovery of German economy, all *Länder* governments faced the challenge of the balanced budget approach entrenched in the constitution, rendering it all the more difficult to reach consensus on pending fiscal equalization reform. When in 2013 another Grand Coalition government formed at the federal level, the parties agreed to initiate negotiations between the federal and *Länder* governments on this reform and, in addition, to establish a new commission (*Coalition Treaty* 2013, 95). The latter again was supposed to address fiscal federalism issues in general, including the allocation of revenues and expenditures. However, the commission never materialized. Instead, inter-governmental negotiations followed the traditional pattern of German executive federalism. Prepared by experts of the responsible departments, ministers of finance of the federal and *Länder* governments as well as heads of government met in private to discuss proposals to reform fiscal equalization.

Even before the federal elections in 2013, discussions started within parties and the departments of finance of the *Länder* (*Bösinger* 2016). In October 2012, the Prime Ministers of the *Länder* addressed the issue at their annual summit and composed a list of topics to be dealt with in the Conference of the Ministers of Finance. These negotiations commenced in earnest in summer 2014. At about the same time, the prime ministers met with the Federal Chancellor where they endorsed the work of the finance ministers and committed them to provide proposals for a reform. However, the ministers did not manage to elaborate a draft as expected until the conference of the prime ministers in December 2014. Meanwhile, a joint paper tabled by the federal minister of finance and the mayor of the city–state Hamburg, proposing a redistribution of the income tax and social expenditures while maintaining the horizontal equalization among *Länder* governments (published in *Junkernheinrich et al* 2016, 290–291), was rejected by most other *Länder* governments and criticized in the media.

After the failure of this initiative, the federal minister of finance left further negotiations to the *Länder* governments. However, by this time he had already accepted a redistribution of the VAT revenue (a “joint tax” shared by the federal and *Länder* governments) and an increase of federal grants both amounting to about 8.5 billion Euros. Based on this premise, the SPD-led *Länder* governments issued a paper, proposing to abolish the first step of fiscal equalization (which entails redistributing part of the *Länder* share of the VAT according to fiscal capacity) and compensating this ‘loss’ by increasing federal grants for special needs. The *Länder* governments led by the Christian Democrats instead suggested to abolish horizontal redistribution between rich and poor *Länder*, i.e., the second step of the existing fiscal equalization scheme. In view of these conflicting positions

with little common ground, an agreement appeared rather unlikely among the finance ministers. Finally, the Conference of the Prime Ministers settled the conflict with a compromise. It proposed to formally abolish horizontal equalization, though actually to include this step into the distribution of the VAT and apply mainly the same criteria as in the existing scheme. Moreover, the *Länder* governments expected an increase of the federal share to fiscal equalization up to about 9.7 billion Euros so that, at the end, all *Länder* were better off. Thus, they solved the redistributive conflict by turning it into a positive sum game at the cost of the federal government.

The *Länder* premiers published this proposal in December 2015, after which they resumed negotiations with the federal government. Nearly one year later, a package deal was reached. The federal government finally conceded to increase its payments as demanded by *Länder* governments, but on the condition of several changes in administrative powers which had been debated for some time. They included a centralization of highway administration, an extension of federal supervision over tax administration and over the implementation of federal grants by the *Länder*, and a federal legislative power to coordinate e-government policies of the federal, *Länder*, and local level in order to establish a uniform online portal (for documents and analyses see: [Junkernheinrich et al. 2016](#)).

Thus again federal and *Länder* governments achieved an agreement on a constitutional amendment, including amendments of the fiscal equalization law and other relevant laws, in the long-established structures of joint decision-making. Once again legal proceedings overshadowed the negotiations, after the governments of Bavaria and Hesse had decided to submit the matter to the FCC, though in this instance, the Court refrained from hearing the case, leaving the search for an agreement up to politics. As such, external actors served less as a trigger for change. Instead it was ultimately the factor of time exerting pressure to find an agreement: the expiration of the fiscal equalization law at the end of 2019. Without a new law or constitutional amendment, an unconstitutional situation would result since the Basic Law requires fiscal equalization. Politically, federal and *Länder* governments faced an even tighter deadline with the current legislation period ending with the elections in September 2017. It was apparent that all political actors engaged in federal reform wanted a decision by the federal parliament and the *Bundesrat* under the current political conditions, which they achieved in June 2017, after a minor controversies and amendments (for details see Benz forthcoming). They seemed considerably more favorable to reaching an agreement, not least given the uncertainty of the next election outcomes, which could result in quite different majorities, with serious consequences for negotiation powers in intergovernmental relations and the legislative process.

Thus, the deadline triggered change, but like the crisis, this trigger induced limited change achieved by a package deal. Amendments preserved the existing

fiscal federalism in a slightly modified version, without significantly enhancing autonomy of the *Länder* or reducing the need for joint decision-making in fiscal policy. They strengthened the federal powers in administration or extended the participation of the federal executive in *Länder* administration, while federal legislation on online platforms in administration will require assent of the *Bundesrat*. Compared to the primary aim of re-allocating powers and reducing joint decision-making, referred to at the start of the reform process in 2003 toward a ‘modernized’ federalism, the outcome of the third reform step clearly amounted to another setback.

Inconsistent Effects of an Accidental Sequential Process

Amending a federal constitution usually requires an agreement among federal and state governments on redistribution of powers and resources. Regardless of the type of the federation and the formal amendment procedure, this process follows the rules of joint decision-making. However, actor constellations and the structure of negotiations among governments vary. As comparative research has demonstrated, significant change can be expected if reform proposals are negotiated in different arenas including different actors and if they evolve in a sequence starting with discussions on principles and ending with elaborating the detailed rules (Benz 2016). In the German case, we find a certain arena differentiation in the first reform and a sequential reform process. However, none of these features resulted from a deliberate organization of constitutional policy.

The inclusion of the FCC as an additional arena in the first reform occurred by coincidence, when it had to decide on cases filed by *Länder* governments against federal legislation. Court decisions indeed had effects, but less by providing substantial input to negotiations than by triggering the federal government to make concessions. The effect of these triggers was delayed, since the federal government became aware of the implications only after a series of similar decisions. By following the general trend in debates about federalism, the court supported decentralization and thus incited responses of negotiators to move in the intended direction.

The sequence of reform evolved further because important issues had been postponed in previous attempts to “modernize” federalism. Unintended by policy-makers, it developed when parties and governments reacted to disappointing or problematic outcomes by starting a new round of negotiations (Heinz 2012, 131). Throughout this sequence, the historical legacies of German federalism, i.e., stemming not only from formal rules but also especially from the long-established and routinized patterns of intergovernmental policy-making between political executives and administrative actors, increasingly (re)gained traction. The first reform commission can be interpreted as an attempt to institute a new arena of

constitutional policy, although it never opened up the process to deliberation with new actors and civil society. The second commission seemed to continue the first reform approach, but actually insulated the legislative and intergovernmental arena against external influence. In the third stage, governments fully returned to the traditional intergovernmental bargaining in the executive followed by the formal legislative proceedings.

Dynamics of reform most likely would have withered out had it not been for other external triggers intervening in the path-dependent reform sequence. Apparently, the sudden economic crisis erupting around 2008 did not open a window of opportunity for change, at least not in the direction initially proposed by the reform project. As in previous situations that appeared as critical junctures, e.g., the first oil crisis in 1974 and German Unification in 1990 (not to mention post-war crises; see [Thelen and Karcher 2013](#)), governments preferred continuity to change. While the crisis revealed serious fiscal problems not only in East Germany but also in some Western *Länder*, it undermined the policy of budget consolidation prevailing since the turn of the century. Under this condition, governments tied their hands for the future by imposing a strict debt rule with its implementation to be jointly monitored between *Länder* and Federal governments. Revising the distribution of tax powers and fiscal equalization was postponed again and the latter had to be addressed in a third reform, now due to an approaching expiry date of the existing law, with upcoming elections only adding to the pressure to reach a consensus. This deadline compelled policy-makers to come to an agreement which was achieved by a package deal with the *Länder* gaining resources and the federal government gaining administrative power. The overall pattern (see [Figure 1](#)) to this sequence of reform thus has elicited quite contradictory results.

Consequently, aside from the intervention of the FCC, these external triggers intensified the bargaining logics of joint decision-making. Under pressure to come to decisions and avoid a deadlock, these logics accumulated towards institutional change enforcing existing structures of power sharing and centralizing powers in federalism, i.e., exactly those features the policy to “modernize” German federalism initially aspired to change. Whereas the court served as an external actor with the power to drive actors negotiating a constitutional amendment in the envisaged direction, economic and fiscal crisis caused uncertainties and prevented policy makers from far-reaching changes. Finally, under the pressure of time to replace constitutional or ordinary law, negotiators concluded a package deal irrespective of the high costs of these decisions for federal and *Länder* governments, because a non-decision would have caused even higher costs. The parliament had no alternative than to agree to this deal. These different effects of the external triggers explain both the dynamics of change and the inconsistent outcome.

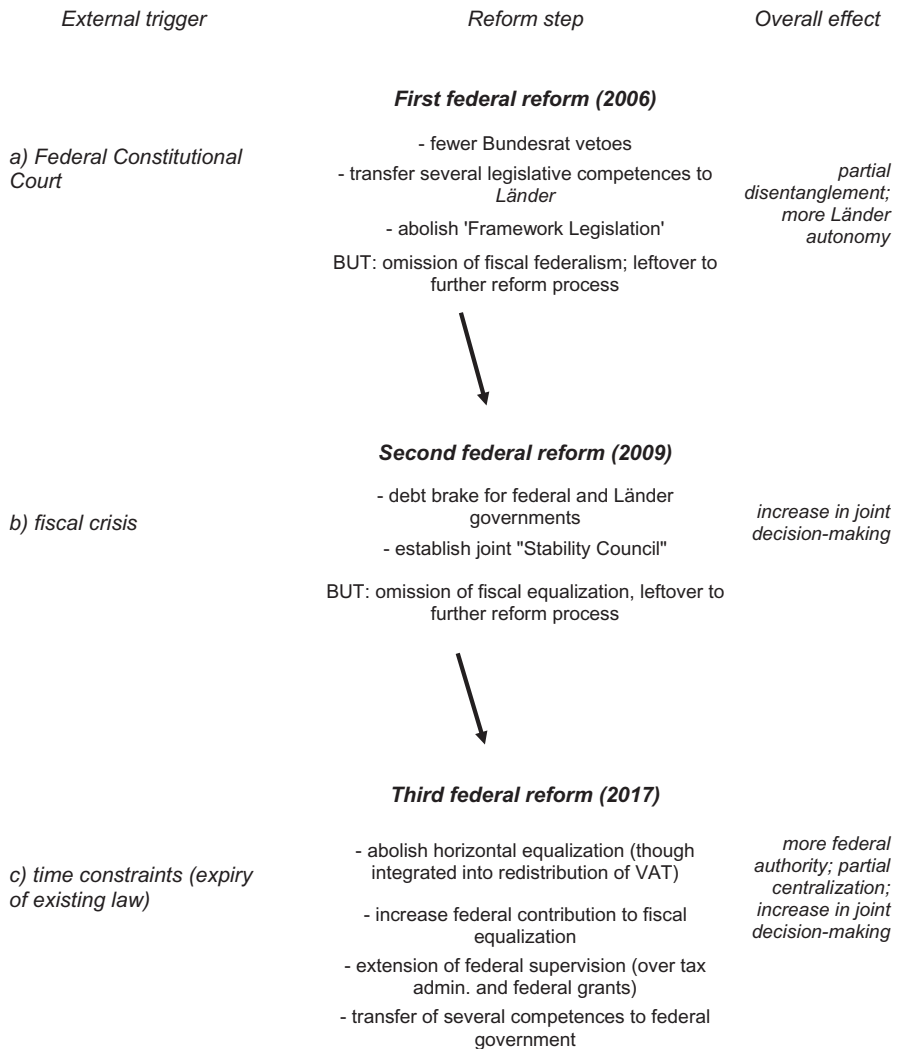


Figure 1 Federal reform project as of 2000s (“modernization of German federalism”).

Conclusion

Policies of institutional change interact with historical evolution. In German federalism, these policies have been based on institutions causing path-dependence and considerable stability (Lehmbruch 2002). Since the 1980s and in particular after German unification, context conditions in society, expressed by economic divergence

between *Länder*, the erosion of the integrative effects of party politics, and the waning of federal solidarity instigated tensions between existing institutions and a territorially differentiating society. Against this background, governments engaged in a series of reforms of the federal system. After the third major constitutional amendment passed in 2017, we can conclude that German federalism still operates under institutional conditions favoring joint decisions and uniform solutions. This institutional continuity contrasts with changes in society, and it may not be exaggerated to argue that instead of a decentralized state in a centralized society (Katzenstein 1987), changes in German federalism tend towards uniform policies in a regionalizing society.

Historical legacies of institutional principles, ideas, and rules have to be taken into account to determine inherent continuity of existing structures and the conditions constraining policies of institutional change. Informed by the historical approach, our case study provides evidence for institutional continuity. However, the legacy of intergovernmental patterns of joint policy-making does not prevent political actors from amending the constitution, although they may achieve this end in steps. Regardless of the motivation of policy-makers to find compromises in order to avoid deadlocks, results of constitutional policy are induced and influenced by external factors arising outside the processes of negotiation and decision-making. They trigger policy dynamics towards institutional change. Yet, in contrast to approaches of historical institutionalism, the dynamics captured here should not be perceived as a shift from path-dependence to a critical juncture. Indeed, two of the most significant triggers identified here, namely a shift in interpretation by the FCC concerning the federal government's legislative powers in the first reform or the expiration of the fiscal equalization law and upcoming national elections in the third reform, are far from extraordinary events. Yet, they had a decisive impact on constitutional negotiations, not unlike the economic crisis in 2008.

The sequence of changes does not conform to incremental policy-making accumulating to gradual institutional evolution. Instead, changes driven by different triggers have different effects despite similar institutional conditions and patterns of policy-making. These factors cause discontinuity contrasting the continuity of incrementalism. However, the accumulated effects can, as in the German case, amount to unintended and inconsistent consequences.

On the whole, German federalism and the politics of constitutional reform have not ended in the joint-decision trap or gradual evolution. Instead, federalism reform evolved on account of actors having to respond to external triggers in their efforts to negotiate agreements on redistribution of power and resources. And the three reform results analyzed here demonstrate that policy-makers managed to reach agreements despite the high thresholds to amending the constitution in general and German federalism in particular. Yet, as different triggers have materialized though the sequence of the reform process, their impact as well as respective directions of change varied. At the end German federalism changed, but

compared to the declared intentions of reformers to “modernize” federalism by disentanglement of powers, it advanced backwards.

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