

Procedural Inconveniences and Severance Pay as Employment Protection Regulation

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Abstract

We consider the effects of employment protection regulation to incentives of workers and the labor market with search friction. Two types of the regulation are concerned: one is severance pay and the other is procedural inconvenience like providing advance notice or requiring negotiation with unions. The former is just transfer, but the latter yields social wasteful transaction cost. We would show that the procedural inconveniences give less damage to incentives of workers than severance pay, and conduct numerical illustration to highlight that appropriate regulation may reduce job flow and unemployment rate and improve welfare. Moderate procedural inconveniences improve welfare, however, the range of severance pay consistent with the incentive compatibility of workers is narrower.

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