

# Optimal Unemployment Insurance Design: Time Limits, Monitoring, or Workfare?\*

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## Abstract

This paper analyses crucial design features of unemployment insurance (UI) policies. We examine three different means of improving the efficiency of UI: the duration of benefit payments, monitoring in conjunction with sanctions, and workfare. To that end we develop a quantitative model of equilibrium unemployment. The model features worker heterogeneity in preferences for leisure. The analysis suggests that a system with monitoring and sanctions restores search incentives most effectively, since it brings additional incentives to search actively so as to avoid the sanction. Therefore, the UI provider can offer a more generous UI replacement rate in a system with monitoring and sanctions than in the other two systems. Workfare appears to be inferior to the other two systems.

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