

# Turning Down Higher Wages? A Lab-in-Field Experiment on Tax Code Notches and Labor Market Decisions



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## Introduction

Though often portrayed as an international issue, poverty is a phenomenon that plagues over 37 million Americans, forcing them to shift focus away from achieving personal and career goals in favor of finding the resources to survive (“Income and Poverty in the United States: 2020” 2021). Current welfare programs are plagued by benefits cliffs, which occur when increased wages result in the loss of essential public assistance so that a working individual experiences a net loss in revenue (“What are Benefits Cliffs?” 2021). This makes upward economic mobility difficult for the impoverished to attain. In our study, we intend to replicate the findings of Mani *et al.* in “Poverty Impedes Cognitive Function” (2021), which conclude that cognitive capacity is decreased by poverty. Because of this documented limitation on general cognitive function, we also seek to explore how poverty affects the decision-making of the poor in a labor market setting. Specifically, we simulate the stress of poverty using scenarios as a prime and real-effort tasks that mimic benefits cliffs, and assess the cognitive performance and subjective reasoning of study participants. We anticipate that low-income participants will score lower on executive function assessments and will make economically poor decisions during the real-effort tasks and prime scenarios at a higher rate than high-income participants.

## Results

- Anticipate that we will replicate the results found by Mani *et al.* (2013), and that additional insights will be gained from extending these ideas to a labor market setting

## Discussion

- If we find that poverty negatively impacts labor market decisions:
  - Suggests that the poor want to attain upward economic mobility, but are hindered by the current system, which has a negative affect on their cognitive capacities.
  - Public policy implications: Push for a simplification of our welfare systems; complexity only benefits those with resources and cognitive capacity to deal with it, thus excluding the poor.
- If we find that poverty positively impacts labor market decisions:
  - Suggests that the poor carefully consider how tax-benefits relate to each other, and economic mobility is likely harmed when the poor realize they lack an incentive to continue to work.
  - Public policy implications: Incentivize career advancement for the poor.

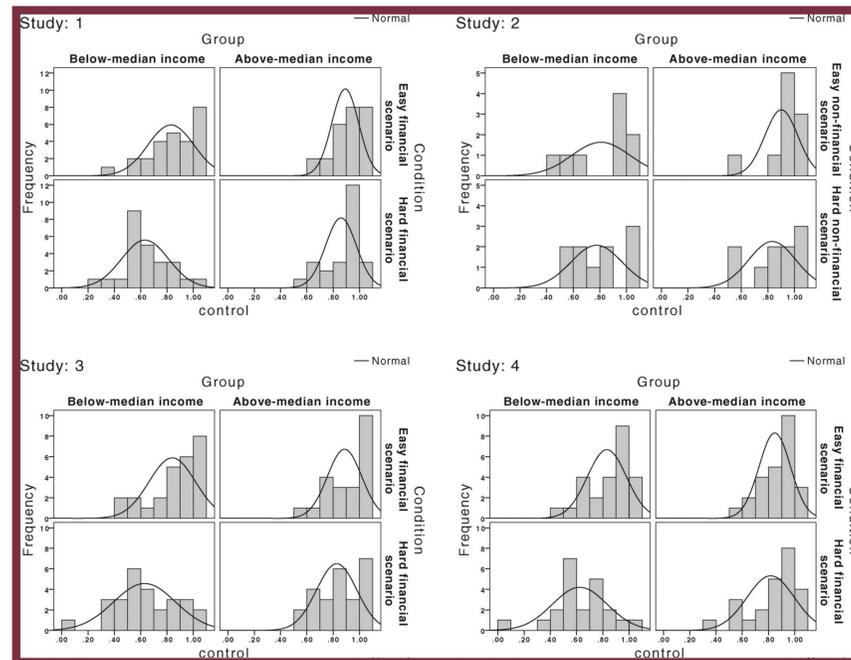


Figure 1: Results from Mani *et al.* showing decreased performances on cognitive function tests for poor participants compared to rich participants, and the disproportional effect of the hard prime on poor participants

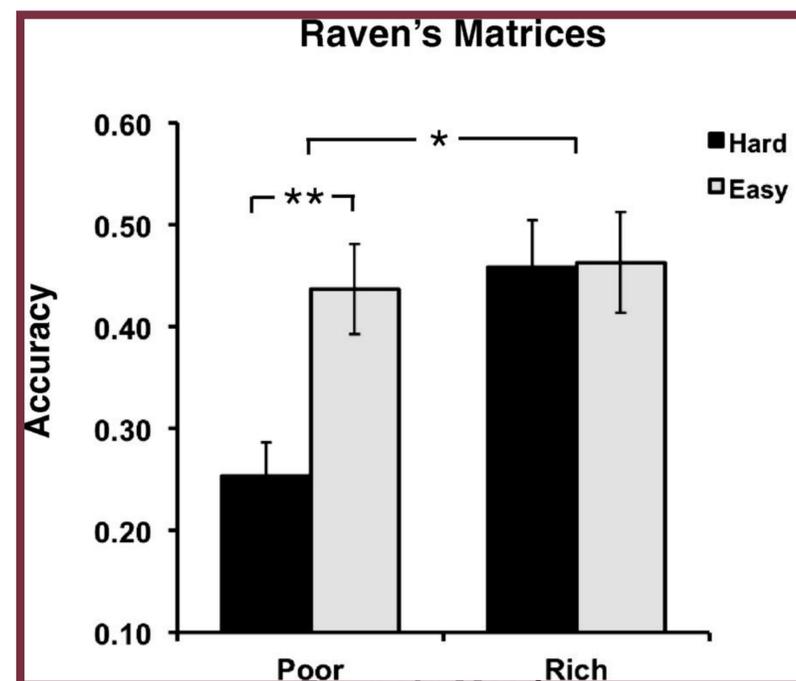


Figure 2: Results from Mani *et al.* showing decreased performances on the Raven's Matrices test for poor participants compared to rich participants

## Methodology

- We mimic the methods of Mani *et al.*, conducting a lab-in-field experiment
- Participants taken from Tallahassee Community College
- Assess participants' poverty status using Pell Grant eligibility
- Simulate economic stress by presenting participants with an easy or hard prime, made up of different financial scenarios
  - E.g. (“easy” scenario in parentheses): Suppose you have reached the point where you must replace your old refrigerator. The model you plan to buy offers two alternative financing options: (1) You can pay the full amount in cash, which will cost you \$999 (\$399). (2) You can pay in 12 monthly payments, of \$100 (\$40) each, which would amount to a total of \$1200 (\$480). Which financing option would you opt for? Would you have the necessary cash on hand? Would the interest be worth paying in this case?
- Assess executive functions using the Raven's Matrices test, Stroop Task, & Hearts and Flowers Task
- Labor market environment simulated with activities in which participants choose a wage each round in order to maximize earnings from two series of tasks
  - Participants complete brief survey to ensure they understand instructions
- Return to the prime and ask participants how they would respond to scenarios
- Conduct interviews of randomly selected participants to learn about their reasoning during their game along with their experiences within the real labor market

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