Notes on Behavioral Economics and Labor Market Policy

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0. Background and motivation

Recent years have been trying ones for American workers. The unemployment rate has reached double digits for the first time in over a quarter of a century. Worker compensation growth has all but stalled. The human costs of labor market turbulence have rarely been clearer, and the value of public policies, such as unemployment insurance and job training programs, that assist workers in managing that turbulence, gaining new skills, and navigating the labor market have rarely been more apparent.

And, even in the best of times, the United States' labor market is a dynamic and turbulent one, with high rates of turnover (over five million separations and five million new hires in a typical month in normal times) but substantial frictions as well. As a result, labor market programs and regulations are key components of economic policy. Such policies help support the unemployed, provide education and training opportunities, and ensure the fairness, safety, and accessibility of the workplace. The challenge for policymakers is to design such policies so that they meet these goals as effectively and as efficiently as possible.

Labor market policies succeed in meeting their objectives, however, only to the extent that they accurately account for how individuals make decisions about work and leisure, searching for jobs, and taking up opportunities for education and training. To a substantial extent such policies are built around standard economic assumptions of behavior that individuals are perfectly rational, time consistent, and entirely self-interested. The design of unemployment insurance with job search requirements intended to minimize distortions to incentives to return to work, the use of complicated eligibility criteria and administrative hassle factors to discourage social program participation except for the presumed most needy, and the shift to vouchers for training services all may be justified by these assumptions.

However, recent research at the intersection of psychology and economics—behavioral economics—is changing our understating of how individuals choose and act, and with it, some of our conclusions for policy design. Behavioral economics stresses empirical findings of behavior that are partially at odds with standard economic assumptions. The key empirical findings from field research in behavioral economics imply that individuals can make systematic errors or be put off by complexity, that they procrastinate, and that they hold non-standard preferences and non-standard beliefs.[1] To the extent that these behavioral tendencies operate in labor market contexts, they change both our understanding of the challenges that policy design must meet, as well as the opportunities and design tools available to policymakers.

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[1] S. DellaVigna, "Psychology and Economics: Evidence from the Field," *Journal of Economic Literature* 47 (2009): 315-72.

In these notes, we briefly review selected topics in labor market policy though the lens of behavioral economics. We identify aspects of existing U.S. policy design that appear at odds with behavioral findings, as well as unrealized policy opportunities those findings suggest. And we make recommendations for either policy reform or further study, according to what the evidence supports. The results of this review are prescriptions for policy design and innovation that reflect a synthesis of traditional and behavioral economic insights. We consider implications of behavioral findings in three areas of labor market policy: unemployment insurance, job search assistance, and job training.

Some of the implications of behavioral economics for policy are overlooked in traditional formal economic analysis but reflect what might best be called "common sense" and are similar to the critiques and prescriptions of many long-time policy practitioners and analysts. These include common-sense recommendations to reduce the fragmentation and complexity of U.S. job training, employment, and social welfare programs. The behavioral approach also provides a reinterpretation of traditional labor market policy proposals such taking into account loss aversion and potentially biased wage expectations in considering the case for and the design of wage-loss insurance policies. And behavioral findings from other domains generate new insights related to the choice architecture and choice platforms for helping guide unemployed and disadvantaged workers through training and education options.[2]

1. Overview of recommendations for U.S. labor market policy

A review of the intersection of behavioral economics and current U.S. labor market policies leads to two categories of policy recommendations: Where the research is sufficiently clear and informative at the appropriate level of detail, it directly suggests changes to policy. Where the promise of behaviorally informed policy changes is clear but the specific policy implications are not, it suggests demonstration and evaluation projects.

1.1 Recommendations for policy reform

- *Unemployment compensation*. Should include wage-loss insurance in some form. In addition to the insurance benefits it provides, wage-loss insurance offers a way of assisting individuals with the psychological adjustment to changing labor market conditions and addresses likely biases in wage expectations that impede work incentives.
- *Employment services and job search assistance*. Should be expanded to provide more accessible and meaningful information about labor market conditions and occupational

[2] R.H. Thaler and C.R. Sunstein, *Nudge*, Yale University Press (2008).

projections. These programs should help address procrastination in job search and provide guidance to unemployed and low-wage individuals in a way that both reflects and takes advantage of the way people process information.

- *Job training*. Should simplify program take-up, navigation, and completion, and provide user-friendly information on the quality of training providers. These programs should structure choices to reflect the limited abilities of individuals to manage complexity and exert self-control.

1.2 Recommendations for future investigation

- *Unemployment compensation.* Should experiment with alternative incentives for encouraging workers to return to employment that reflect their propensity to procrastinate job search. For example, the unemployment insurance system should test the use of small, high frequency bonus payments that are contingent upon events other than finding employment and retaining a job for many months.
- *Employment services and job assistance.* Should study the impact of counseling with the goal of debiasing beliefs and alternative framings of employment opportunities that address reference dependence. For example, tests of alternative methods of debiasing wage expectations.
- *Job training.* Should experiment with choice platforms in which providers compete to offer services, as a way to encourage innovation in meeting the needs of worker with limited capacity for managing complexity. For example, by creating markets for advice in which providers are rewarded based on meaningful performance measures (employment and earnings outcomes) instead of just the use of services.

The remainder of this paper describes these recommendations, and their justifications, in more detail.

2. Unemployment compensation

Providing income support for the unemployed while encouraging their speedy return to work is a primary goal for labor policy. The ability of individuals (and even of many extended families) to self-insure, to smooth income and consumption out of savings and transfers from relatives and friends, is limited in the face of job losses and potentially extended spells of unemployment. And private markets may fail to provide adequate mechanisms, such as loans, because of asymmetries of information. Our main policy instrument to maintain the consumption of job losers as they seek to gain reemployment is unemployment insurance (UI). In the United States, UI is a program administered jointly by the federal government and the states that replaces a fraction of a qualified individual's lost wages when she becomes

unemployed (through no fault of her own) and while she looks for new work. Ordinarily benefits can be collected for a maximum of six months (26 weeks), although this limit is often relaxed during national economic downturns by Congress through discretionary federal UI extensions. Longer potential benefit durations (extended benefits) can also be triggered at the state level in response to state-specific adverse economic shocks. Related programs and variants include wage-loss insurance, personal reemployment accounts, reemployment bonuses, and subsidies for the continuation of health insurance coverage following job loss.

The main design challenge for these policies is traditionally taken to be balancing the provision of liquidity and support for consumption smoothing during unemployment against the tendency of such benefits to distort incentives to search for and take new employment.[3] Increases in the generosity of benefits, either through increases in benefit levels or the duration of benefits, appear to lengthen the unemployment spells of unemployment insurance recipients.[4] In part to combat these effects, U.S. unemployment benefits are contingent on active job search efforts (job search requirements) and benefits are strictly time limited. There has been some experimentation with the terms of unemployment compensation to further promote reemployment including the use of reemployment bonuses, variation in the intensity of monitoring job search, and the provision of job search assistance and self-employment assistance. But such efforts have to date generated only mixed results.[5]

The behavioral economics of unemployment compensation

Behavioral economics identifies psychological barriers to job search and reemployment that may help to explain the persistent challenge of encouraging work among those collecting benefits. One set of barriers arises from the way in which individuals form expectations about wages and evaluate their employment prospects. Behavioral economics introduces the possibility that individuals will form such expectations with error or systematic bias, and are likely to be "loss averse" in evaluating job offers asymmetrically around those expectations.[6] These effects may operate to slow their return to work and reinforce the moral hazard problems in unemployment compensation schemes of unemployed workers not putting in adequate search efforts and setting inefficiently high reservation wages in response to more generous benefits while unemployed.

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[3] M. Baily, "Some Aspects of Optimal Unemployment Insurance," *J. Public Econ.* 10 (1978): 379–402; and R. Chetty, "Moral Hazard vs. Liquidity in Optimal Unemployment Insurance," *Journal of Political Economy* 116 (2008), 173-234.

[4] B.D. Meyer, "Unemployment Insurance and Unemployment Spells," *Econometrica* 58 (1990): 757–782; and L.F. Katz and B.D. Meyer, "The Impact of the Potential Duration of Unemployment Benefits on the Duration of Unemployment," *J. Public Econ.* 41 (1990): 45–72.

[5] B.D. Meyer, "Lessons from the U.S. Unemployment Insurance Experiments," *J.E.L.* 33 (1995): 91–131.

[6] D. Kahneman and A. Tversky, "Prospect Theory: An Analysis of Decision under Risk." *Econometrica* 47 (1979): 263–291.

Another set of behavioral barriers to reemployment arise from the tendency of individuals to have imperfect self-control, such as expressed by time inconsistent preferences.[7] As a result, individuals may procrastinate in their job search efforts even when such delay is against their own, long-run self-interest. These considerations complicate the moral hazard problem creating potential conflicts between an unemployed individual's current and future selves as well as the standard conflict between benefit the recipient and the program operators. These factors create a situation where stronger work and job search requirements that appear overly paternalistic in the usual model of *homo economicus* may actually benefit the program participants themselves by helping them overcome self-control problems.

Reform proposal: Implement some form of wage loss insurance

Individuals return to work when they get a job offer paying above their reservation wage. In standard theory, individuals are assumed to form reservation wages in a rational manner incorporating unbiased expectations of market wage and an accurate assessment of the market value of their skills. As a result of the behavioral tendencies outlined above, however, unemployed individuals may be reluctant to entertain and slow to accept even objectively reasonable wage offers. The current structure of unemployment insurance and related programs does not address this tendency, but the efficiency of these programs may suffer because of it. Individuals holding out for offers that will not come remain on the unemployment insurance roles for inefficiently long periods. Of particular concern is the possibility that individuals will set their reservation wage at the level of wages they have received on past jobs, whether or not this is realistic given prevailing labor market conditions.[8] Moreover, individuals might be loss averse in the sense of having preferences that are asymmetric around their previous wage with a particularly large psychological cost to taking a job paying below their past earnings. The combined effect might be to lead individuals to be irrationally reluctant to accept job offers below their pre-separation wage, to be unwilling to relocate to areas with greater labor market opportunities, and to search mainly for jobs like their previous one or to pass up reasonable opportunities while waiting for their old job (or one just like it) to return. This phenomenon has been called "retrospective wait unemployment" and is particularly important for long-tenured workers displaced from high-

[7] D. Laibson, "Golden Eggs and Hyperbolic Discounting," *Q.J.E.* 112 (1997): 443–477.
[8] M. Feldstein and J. Poterba, "Unemployment Insurance and Reservation Wages," *J. of Public Econ.* 23 (1984): 141–167; L. Ball and R. Moffitt, "Productivity Growth and the Phillips Curve", NBER working paper 8421 (2001); and V. Hogan, "Wage Aspirations and Unemployment Persistence," *Journal of Monetary Economics* 51 (November, 2004): 1623–1643.

wage sectors in decline (such as autos and steel).[9] It is reinforced by the social status and personal identities of many workers being strongly tied to their previous jobs.

A promising policy to address these issues and supplement UI for likely permanent job losers is wage-loss insurance (also called wage insurance) which (at least temporarily) subsidizes worker earnings upon reemployment when the wage they receive on their new job is less than that of their old job. Economists have noted several advantages to wage-loss insurance, such as the ability to better target benefits to those workers who face the most severe consequences of job loss.[10] Although behavioral economics does not change that logic, it does identify additional advantages to wage-loss insurance. By manipulating the realized value of wages (especially if the wage-loss insurance payments show up directly in one's regular paycheck) and making job offers more attractive, it averts to some degree the impacts of biased wage expectations and mitigates the effects of loss aversion. In the longer run, it may smooth the painful but sometimes necessary process of psychological adjustment to lower-wage employment. Consideration of wage-loss insurance proposals should weigh these behavioral advantages, and any demonstration projects or evaluations of wage-loss insurance, such as that currently being conducted as part of the Trade Adjustment Assistance program, should take care to test for the possible importance of these behavioral dimensions.

In addition to providing further justifications for existing wage-loss proposals, behavioral factors also generate specific design recommendations. For example, the effects of biased wage expectations or reference dependence with respect to those expectations call into question the likely efficacy of partial wage insurance at speeding up returns to work for displaced workers. These behavioral concerns are also consistent with the limited impacts on reemployment rates and job search efforts found in a major Canadian demonstration project testing partial-replacement wage insurance for displaced workers.[11] An alternative might be to structure wage-insurance as full or nearly full insurance upon reemployment, and declining over time possibly in a manner linked to typical wage growth patterns on new jobs. Of course, the benefits of such a redesign in mitigating the effects of biased wage expectations and loss aversion must be weighed against the possible costs it might impose on targeting and allocative efficiency.

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[9] L.H. Summers, "Why is Unemployment So High at Full Employment?," *BPEA* (1986), 339-82; and E. Balls, L.F. Katz, and L.H. Summers, "Britain Divided: Hysteresis and the Regional Dimension of Britain Unemployment Problem," Harvard University working paper (1991).

[10] L. Kletzer and R. Litan, "A Prescription to Relieve Worker Anxiety," Brookings Institution Policy Brief 73, (March, 2001); and J. Kling, "Fundamental Restructuring of Unemployment Insurance," Hamilton Project Discussion Paper 2006-05 (September, 2006).

[11] H.S. Bloom et al., "Testing a Financial Incentive to Promote Re-employment Among Displaced Workers: The Canadian Earnings Supplement Project (ESP)." *Journal of Policy Analysis and Management* 20 (2001): 505-23.

Research agenda: Experiment with incentive schemes in unemployment compensation

Limits to self-control represent another likely behavioral barrier to creating incentives to return to work in unemployment compensation programs. A key design challenge for UI is to provide temporary income support while maintaining the incentives of the unemployed to search for and return to work. Procrastination and other expressions of bounded self-control complicate that problem substantially. Findings that the unemployed spend only a modest amount of time per week searching for work are consistent with such procrastination.[12] Much suggestive evidence indicates that many job seekers may have time inconsistent preferences and tendencies to procrastinate in job search efforts.[13] The effects of benefit design on search intensity are thus not simply a product of financial payments from continued unemployment, but instead a more subtle interaction between benefits, incentives, and willpower. Particularly problematic for policy, these tendencies may serve to blunt the force of design features intended to align incentives. The result is that work incentives in programs like UI must address both moral hazard as well as procrastination.

That the work incentive problem in UI may take on this different character when allowing for behavioral tendencies such as procrastination suggests an agenda of experimentation with the structure of unemployment benefits. Demonstration projects experimenting with changes to the UI compensation structure have a long history. Past efforts have included reemployment bonus experiments and a demonstration of Personal Reemployment Accounts (PRAs).[14] However, evaluations of these efforts have yielded somewhat mixed results. This may be in part due to the failure of these projects to consider factors such as bounded self-control. For example, reemployment bonuses, contingent as they are on possibly distant outcomes such as gaining reemployment and holding the new job for at least several months, may provide little in the way of an effective incentive to individuals who choose levels of search effort day to day.

Behavioral economics suggests new directions for experiments with alternative incentive schemes in unemployment insurance and related programs that recognize the role of self-control in returning to work. One tack that appears promising would be to offer small, immediate, and high frequency reminders and incentives to search. So instead of tying rewards and penalties to large, distant, low frequency objectives, such as reemployment for a

[12] A. Krueger and A. Mueller, "The Lot of the Unemployed: A Time Use Perspective," IZA Discussion Paper 3490 (2008).
[13] S. DellaVigna and M.D. Paserman, "Job Search and Impatience," *Journal of Labor Economics* 23 (2005): 527-88; and M.D. Paserman, "Job Search and Hyperbolic Discounting: Structural Estimation and Policy Evaluation," *Economic Journal* 118 (2008): 1418–1452.
[14] B. Meyer, "Lessons from the U.S. Unemployment Insurance Experiments," *J.E.L.* 33 (1995): 91–131; and G. Kirby et al., "Responses to Personal Reemployment Accounts (PRAs): Findings from the Demonstration States," Mathematica Policy Research, report to Dept. of Labor (2008).

significant duration of time, unemployment insurance might offer rewards and penalties that trigger at smaller, higher frequency objectives, such as make a specific number of active employer contacts in a week. Other candidates for testing are incentives that trigger avoidance of anticipated regret, and rewards with lottery-like characteristics, which have been effective in the presence of self-control problems in other contexts.[15] Another direction for experimentation entirely would be to test the possibility of overcoming imperfect self-control by creating a principal-agent relationship in which placement agents receive the bonuses. Key issues that will need to be addressed in the design of such policies using employment intermediaries are limiting cream skimming incentives (which arise if the intermediaries can "choose" their clients) and making sure that payments to intermediaries are at least partially tied to longer-term employment and earnings outcomes rather than only to short-term reemployment rates and use of services.[16]

3. Employment services and job search assistance

Another goal of labor market policies is to assist individuals with searching for and finding jobs. A portfolio of interconnected programs supports this goal, and includes informational services as well as active job search assistance. The Employment Service (ES) provides placement assistance to both workers and employers, maintains labor exchange listings, and performs outreach to employers. Services provided under the Workforce Investment Act (WIA) include counseling and assistance for job seekers. Workers obtain access to these services through multiple points of entry, one of the most important of which are worker profiling referrals from the UI system. These services are supported by employment data and projections complied by the U.S. Department of Labor and its state partners. The overarching goal of these programs is to help individuals return to work quickly and to some extent to help improve the quality of matches between workers and jobs.

The evidence from a wide range of evaluations suggests that services of this nature are typically effective at helping individuals to obtain employment more rapidly, and, largely as a result, can raise earnings at least in the short-run.[17] This seems to be generally true for most types of these services, including employment services and job search assistance, and for most populations who use them, including those on UI as well as the more economically

[15] K. Volpp et al., "A Test of Financial Incentives to Improve Warfarin Adherence," *BMC Health Services Research* 8 (2008).
[16] D. Autor and S. Houseman, "Do Temporary Jobs Improve Labor Market Outcomes for Low-Skilled Workers? Evidence from Work First," *AEJ: Applied Economics* 2 (2010), forthcoming; and C. Heinrich and Y. Choi, "Performance-Based Contracting in Social Welfare Programs," *The American Review of Public Administration* 37 (2007): 409-35.
[17] R. LaLonde, "The Promise of Public Sector-Sponsored Training Programs," *J.E.P.* 9 (1995): 149-168. C. O'Leary, "Evaluating the Effectiveness of Labor Exchange Services," in *Labor Exchange Policy in the United States*, E. Balducchi, R. Eberts, and C. O'Leary, eds. (2004): 135–178.

disadvantaged including the participants in welfare-to-work programs. Moreover, because such services are relatively inexpensive to provide on a per participant basis, they are usually found to be cost effective.

The behavioral economics of employment services and job search assistance

Behavioral tendencies may help to explain the consistent effectiveness of employment services and job search assistance. All of the behavioral barriers to returning to work described above in the context of unemployment compensation programs—biases and error in setting wage expectations, procrastination in searching for work, and so on—are operative in the general context of job search in general, as well. To the extent that formal assistance can ameliorate or overcome these problems, these policies will speed reemployment.

In addition, there are behavioral barriers to job search that arise simply due to the fact that it is an intrinsically difficult problem. Optimal job search requires considering information about job market conditions and how they match with personal characteristics in a way that is likely to be difficult for imperfectly rational individuals. Behavioral economics stresses that individuals are limited in the attention and the computational capacity they can bring to multifaceted and complex problems.[18] As a result, the speed and quality of employment matches may both suffer due to the tendency of fallible individuals to manage the complex tasks of job search. And programs that assist individuals with managing that complexity can help them obtain work.

<u>Policy proposal: Simplify and expand employment services and job search assistance</u>

Searching for jobs may be more difficult for individuals than the standard model typically allows. Looking for work is, in the first place, a substantial information problem. Workers have to understand labor market conditions, have knowledge of openings and applications processes, possess an accurate understanding of their own skill level and how firms and markets might value those skills, and determine the quality of matches with employers. Moreover, searching for work requires willpower, which can be costly for individuals to draw upon. Workers may be tempted to procrastinate in their job search efforts in favor of other activities. Well-designed employment services and job search assistance programs have the potential to assist with both of these issues.

[18] A. Tversky and E. Shafir, "Choice under Conflict: The Dynamics of Deferred Decision," *Psychological Science* 3 (1992): 358–361. A. Tversky and D. Kahneman, "Judgment under Uncertainty: Heuristics and Biases," *Science* 185 (1974): 1124–1131. S. Iyengar and M. Lepper, "When Choice is Demotivating: Can One Desire Too Much of a Good Thing?," *J. of Personality and Social Psychology* 79 (2000): 995–1006.

One proposal that follows from a behavioral view of job search is that expanding access to employment services or job search assistance is likely to be worthwhile. For one thing, there is evidence that individuals are bad at knowing that job search is effective, that is, that they underestimate the benefits of search.[19] Policies might thus seek to promote enrollment in these activities beyond what individuals would choose on their own, for example, by increasing the instances in which individuals can be defaulted into such services, such as through worker profiling upon signing up for UI. Default required job search activities might help individuals to overcome any tendency to procrastinate search. Evidence that individuals can be encouraged to take jobs just by enrolling them in job search programs—that individuals are encouraged to take jobs either very early into such programs or before such programs even begin—is consistent with this hypothesis.[20]

Another proposal is to simplify and streamline the experience of workers seeking employment services or job search assistance. Employment and job search assistance tools should be widely available and easy to use, both in One-Stop Career Centers and online. These tools could gather information on an individual's background and interests, provide feedback on the education and employment opportunities pursued by others like them, list job openings they may be interested in, and provide information on the projected growth in occupations and in other local areas in a manner that is easily accessible.

In addition to simplifying the process of obtaining assistance, employment service activities should also present information on local labor market conditions and occupational projections with an eye to how it will be construed by recipients, not just what information it contains. For example, it is one thing to say that a certain sector is expanding or contracting but probably a different level of information transmission to convey what it means to be in that sector and incorporate this information into labor exchange systems. That is, policy should seek not only to improve the precision of information like occupational projections, but also the way in which that information is conveyed to individuals. Information should be simple and personalized.

Research agenda: Study methods of presenting job search information

Employment services and job search assistance face behavioral barriers to their effectiveness beyond the difficulties individuals may have with the complexity or the willpower

[19] J. Spinnewijn, "Unemployed but Optimistic: Optimal Insurance Design with Biased Beliefs," MIT working paper (2009).
[20] S. Director and F. Englander, "Requiring Unemployment Insurance Recipients to Register with the Public Employment Service," *Journal of Risk and Insurance* 55 (1988): 245-258. D. Black et al., "Is the Threat of Reemployment Services More Effective than the Services Themselves? Evidence from Random Assignment in the UI System," *A.E.R.* 93 (2003): 1313–1327.

requirements of job search. Most prominently, the systematic biases or reference dependence related to previous earnings that unemployed individuals may exhibit with respect to wage expectations can remain an impediment to seeking and accepting work. Job search assistance can potentially work to address the biases, frames, or other cognitive obstacles to employment because it represents an opportunity for policy to influence how individuals understand the possibilities before them in the job market. Behavioral economics suggests that the way in which job opportunities are framed can matter for how individuals respond to choices. This suggests a research agenda to experiment with modifications to the presentation of job search information beyond simplification. Policymakers can innovate in the way that employment services are presented to individuals.

One area for research and experimentation is the potential of using the presentation of information or counseling that can be part of job search assistance programs to debias wage expectations. As discussed above, there are reasons to think that one behavioral barrier to job search and employment is that individuals may have biased wage expectations. Evidence from other contexts suggests that debiasing of such beliefs is possible through carefully designed interventions.[21] This research suggests that having people question their own judgment by explicitly considering counterarguments to their own thinking can be effective. Job search assistance could potentially incorporate such an exercise with respect to wage expectations. There has been some comparative effectiveness type research on job search assistance, testing the relative success of differently structured job search assistance programs.[22] Research into wage expectations debiasing could follow a similar path.

There is also scope for research into other aspects of the presentation of employment services information or job search assistance. The presentation and context of this information can potentially invoke frames of loss or gain, emotions such as anger or sadness, different propensities toward risk taking, and so on. This framing can affect choices not by overcoming biases or behavioral tendencies but by working within their limits. One promising area of study involves manipulations to the way job search assistance is framed for participants. Framing consequences as losses instead of gains, for example, is known to affect behavior in other contexts.[23] This framing can also affect the willingness of participants to take risks, such as the risk of interviewing for or starting a new job. Framing might also be used to attempt to influence the reference points around which individuals judge alternatives and thereby impact attitudes toward job opportunities.

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[21] L. Babcock, G. Lowenstein, and S. Issacharoff, "Creating Convergence: Debiasing Biased Litigants," *Journal of Law & Social Inquiry* 22 (1997): 913–920.
[22] P. Decker et al., "Assisting Unemployment Insurance Claimants: The Long-Term Impacts of the Job Search Assistance Demonstration," Mathematica Policy Research, report to the Dept. of Labor, (2000).
[23] A. Rothman et al., "The Strategic Use of Gain- and Loss-Framed Messages to Promote Healthy Behavior: How Theory Can Inform Practice," *Journal of Communication* 56 (2006): S202–S220.

4. Job training

Another important set of labor market policies is concerned with providing access to opportunities to acquire and upgrade skills and earning power. The current centerpiece of U.S. public-sector job training program efforts is the Workforce Investment Act (WIA). WIA offers occupational skills training and on-the-job training programs to both dislocated and disadvantaged workers. Services are delivered through One-Stop Career Centers, and funds are provided in Individual Training Accounts (ITAs), which workers draw on to purchase training services from various providers, such as community colleges. Other major supports for job training include Pell Grants, which low-income workers can use to fund educational programs that lead to a certificate or degree, and the Lifetime Learning Credit, which is a nonrefundable tax credit available to offset educational expenses.

Although the labor market returns to education in general are well established, programs that support job training for mid-career individuals have a mixed record of effectiveness.[24] In part, this reflects the heterogeneity of both programs of this type as well as the populations they serve. Historical evidence suggests that some participants, in particular adult women, benefit consistently from job training, in the form of improved earnings, while others, including adult men, often do not. Benefits to specific training programs, where evident, are typically small in absolute terms and evidence about their persistence is scattered. A key caveat in interpreting this evidence is most of the evaluations cover training programs that are not intensive, of short duration, and not very different from the substitute education and training programs utilized by members of the control group. Some evidence shows that more intensive training treatments, such as completing courses leading to a certificate or degree at a community college, generate substantial improvements in earnings.[25] The direct evidence on WIA training services is in the form of non-experimental work, and is inconclusive.[26]

The behavioral economics of job training

Behavioral economics suggests that the disappointing results of some job training programs may be due in part to a failure of such programs to respond accurately to the psychology of workers who could benefit from training. Results from behavioral economics suggest that the

[24] D. Greenberg, C. Michalopoulos, and P. Robins, "A Meta-Analysis of Government-Sponsored Training Programs," *Industrial and Labor Relations Review*, vol. 57, no. 1 (October 2003), pp. 31–53.
[25] L. Jacobson, R. LaLonde, and D. Sullivan, "Estimating the Returns to Community College Schooling for Displaced Workers," *Journal of Econometrics*, vol. 125, no. 1–2 (2005) pp. 271–304.
[26] C. Heinrich, P. Mueser, K. Troske, "Workforce Investment Act Non-Experimental Net Impact Evaluation," IMPAQ International, report to Dept. of Labor (2008). K. Hollenbeck et al., "Net Impact Estimates for Services Provided through the Workforce Investment Act," report to Dept. of Labor (2005).

determination of whether and when to undertake job training, the selection of a field to be trained in as well as a provider, and the pursuit and completion of that training, represents an intrinsically challenging sequence of choices and actions for imperfectly rational individuals. As noted above, research shows that individuals often fail to choose "optimally" in such settings and can have difficulty exerting self-control in starting up and persisting in investment activities with distant payoffs. A successful workforce investment system is likely to be one that reduces complexity and the need for willpower from the perspective of workers, and relies less heavily on well-informed, patient participants for its smooth operation and success.

Policy proposal: Simplify job training services

Existing job training programs are not focused on being easy to use from the perspective of participants. Past efforts to streamline services have mainly emphasized administrative efficiency, rather than the experience of the user. As a result, programs remain somewhat fragmented and can be complicated to access and navigate. Moreover, in recent decades, job training policy has moved from a model of publicly providing job training services to one of providing individuals access to funding to pursue their own choice of training opportunities in a marketplace of competing providers. Although this shift in focus has many potential benefits, it also places a burden on workers they may be ill equipped to manage, and which may impair the effectiveness of these programs. In addition, this burden may impact participants differentially, raising the possibility that the very individuals who might benefit most from training may have the most difficulty in obtaining it.

One set of policy recommendations that follow from these observations is that it should be an explicit goal of WIA to provide job training services in a manner that is streamlined from the perspective of prospective users. Job training services in WIA should seek to minimize barriers to take-up. These programs should also take active steps to ensure that program requirements are not, in practice, most onerous for those individuals most in need. In addition, training programs provided through One-Stop Career Centers should emphasize reducing complexity and providing guidance to participants as priorities. One method for providing guidance would be to enhance the counseling services that accompany ITA receipt, although previous experimentation along these has not been promising.[27] Another approach would be to institute rules or tailor program parameters, such as ITA value, in such a way so as to better structure or direct choice. A further option currently being tested is the integration within One-Stop Career Centers of both guidance on training and education

[27] S. McConnell et al., "Managing Customers' Training Choices: Findings from the Individual Training Account Experiment," Mathematica Policy Research, report to the Dept. of Labor, Employment and Training Administration (December 2006).

options as well as help in accessing and understanding available financial work supports (e.g., the EITC and child care subsidies) and social assistance programs (e.g., food stamps).[28]

A similar set of recommendations also applies to job training services available outside of WIA. On the one hand, access to these services, such as Pell grants, should be simplified. Current proposals to simplify the FAFSA form and application process for federal student aid are consistent with this goal.[29] Likewise, the Lifetime Learning Credit could possibly be more effective if structured as a match. On the other hand, programs such as these should be integrated with WIA services to the greatest extent possible. For example, where not already the case, Pell recipients enrolled at a community college should receive services through the associated One-Stop Career Center. The One-Stop system is many ways the right model on which to build, but policy should reflect a renewed emphasis on the ease of use from the perspective of participants. Available qualitative evidence supports that idea that integrating services is likely to improve the participant experience.[30]

Finally, an emphasis on simplifying the user experience in job training recommends continued experimentation with job training policies that require less active decision-making on the part of participants. Examples include the support of employer-provided incumbent worker training, or of other demand-side programs that directly fund training services in high-wage and expanding industries.

Research proposal: Experiment with choice platforms for job training advice

A different model for ensuring that individuals qualifying for job training services receive effective guidance and assistance would be to experiment with creating a structured market for providers of counseling and advice. The current system of training assistance, both through ITAs under WIA and through funds available through student financial aid or tax credits, is built upon markets for training services in which providers such as community colleges and proprietary schools compete for training dollars. The idea behind this approach is that participants will apply competitive pressure on training providers to offer effective services. But the complexity of the choices involved limits the capacity of individuals to drive these markets toward such outcomes. In other contexts such as the prescription drug plan choices by the elderly under Medicare Part D and public school choice programs,

[28] C. Miller, B. Tessler, and M. Van Dok, "Strategies to Help Low-Wage Workers Advance: Implementation and Early Impacts of the Work Advancement and Support Center (WASC) Demonstration," Manpower Demonstration Research Corporation (June 2009).
[29] S. Dynarski and J. Scott-Clayton, "Complexity and Targeting in Federal Student Aid: A Quantitative Analysis," *Tax Policy and the Economy* 22 (2008): 109-50.
[30] B. Barnow and C. King, "The Workforce Investment Act in Eight States," report to the Dept. of Labor, Employment and Training Administration (February 2005).

behavioral economics research has found that a large number of complex choices hinders decision-making and that interventions providing personalized and transparent information on the most "relevant" choices can improve decision-making outcomes.[31] Thus, there is some reason to believe that similar efforts could bear fruit with respect to job training.

Job training policy should experiment with the creation of new markets for job training advice in order to improve the capacity of individuals to make good choices about providers of job training service, and, ultimately, improve the operation of the market for job training services. Such an approach would operate by creating a market in which providers of counseling and advice competed to serve individuals. The key would be that the success or failure of those providing counseling and advice would be determined objective measures of their performance.

Practical considerations for making such a proposal work would be paramount, and so experimentation is necessary. Competition could work by having it so that firms doing well in providing advice and counseling according to workforce performance measures gain market share. Individuals registering for training would be referred to one of several providers of counseling. More effective providers will be given progressively more referrals, by reallocating the flow of beneficiaries over time, while ineffective providers will see their client base decrease. Considerable attention would need to be devoted to preventing selection of particular trainees by providers. Referrals could be assigned randomly, or on a rotational basis, to allow direct comparisons of the average performances of different providers.[32] Finally, to avoid conflicts of interest, it would also be necessary that these intermediaries have no connection to the underlying service providers. A regulatory firewall could prohibit financial ties between providers and employers with whom individuals are placed, to solidify the counselors' role as honest brokers. It could be possible for government and private providers to operate in the same market, with each receiving fixed funding per person served.

Finally, note that any innovation of this nature would be dependent for its success on the WIA performance measurement system. There is a good deal of evidence that the existing system is inadequate to such a task, and there are a number of proposals for improvement.[33] These efforts would be complementary to efforts to build and effective choice platform for advice markets.

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[31] J. Kling et al., "Misperception in Choosing Medicare Drug Plans," unpublished working paper (October 2009). J. Hastings and J. Weinstein, "Information, School Choice, and Academic Achievement: Evidence from Two Experiments," *Quarterly Journal of Economics*, 123 (November 2008): 1373–1414.
[32] T. Bartik, "Using Performance Indicators to Improve the Effectiveness of Welfare-to-Work Programs," Upjohn Institute Staff Working Paper 95-36 (1995).
[33] L. Jacobson, "Strengthening One-Stop Career Centers: Helping More Workers Find Jobs and Build Skills," Hamilton Project Discussion Paper 2009-01 (April 2009).