

Economic Incentives and Family Formation

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Extended Abstract

In light of the dramatic changes in marriage, divorce, and cohabitation rates seen in the United States in the last three decades, researchers continue to seek a better understanding of the behavioral mechanisms by which individuals choose among these states. The current study offers new evidence on the determinants of family formation by estimating a choice model in which (a) single, never married adults decide whether to remain single, cohabit, or marry; (b) cohabiting couples decide whether to continue cohabiting, separate, or marry; and (c) married couples decide whether to divorce. While numerous studies have analyzed these same transitions, this paper extends the literature in three ways:

First, the study distinguishes between gains that result from division of labor and income pooling within households, and gains accruing to *legally sanctioned* unions. Most studies of union formation consider the former type of economic gains, but ignore the additional rights and obligations associated with civil marriage. Married couples often incur different income tax burdens than they would if single or cohabiting and lower financial losses in the event of one partner's disability or death. They are usually entitled to extend employer-provided health insurance (and other benefits) to their spouses and spouses' children, and to secure property rights if the union is dissolved. The model estimated in this paper includes covariates that proxy the value of these legal benefits and obligations. To identify the effects of interest, we rely on intertemporal and within-state variation in each legal factor arising from differences across states and over time in income tax laws, divorce laws, and so forth.

Second, the model explicitly accounts for the sequential nature of union-forming decisions—for example, the fact that the same unobserved factors influencing the decision to enter cohabitation are likely to affect subsequent decisions to marry and divorce. The sequential stages of the decision-making process are estimated jointly, and unobserved factors affecting the value of each alternative are allowed to be correlated across (and within) stages. Estimates from this dependent, sequential choice model identify the *causal* effects of each covariate on union-forming decisions. Only two previous

studies control for the confounding role of unobserved factors in modeling the union-forming process, but neither considers the entire sequence of cohabitation, marriage, and divorce decisions.

Third, the study uses data from the 1979 cohort of the National Longitudinal Survey of Youth (NLSY79). The NLSY79 has not been used extensively for studies of cohabitation because, until recently, it was not possible to determine whether respondents' cohabiting partners changed identities over time. A recently completed project used proprietary information in the household rosters to construct detailed cohabitation histories for each survey respondent. Thanks to these efforts, the NLSY79 is now a rich data source for the study of cohabitation decisions. It is particularly well suited for the current study because it contains detailed information on respondents' earnings, nonlabor income, assets, job benefits, schooling, family background, children, and demographic characteristics. Information on federal and state-specific income tax, probate, and divorce laws is combined with respondent-specific data to form the key covariates.

The belief that legally married couples receive significant economic benefits is central to the ongoing debate over same-sex marriage—throughout the U.S., gay and lesbian couples are suing for the right to marry because they seek the economic gains enjoyed by married couples. It stands to reason that the cohabitation, marriage, and divorce decisions of opposite-sex couples are influenced by these same factors, yet they have been given only cursory attention in the family formation literature. By controlling for the benefits and obligations associated with legally sanctioned unions, using detailed data for a nationally representative sample of young adults, and acknowledging the interdependent, sequential nature of the decision-making process, the current study is able to determine whether the gains associated with legally “tying the knot” play an important role in union-forming decisions.