

Book Review

Nudge: Improving Decisions About Health, Wealth, and Happiness

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Authors: **Richard H. Thaler** and **Cass R. Sunstein**

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How many people skip the introduction of a book and jump right into Chapter 1? Doing so would be a mistake with this book. In the Introduction, the authors identify choice architects. “A choice architect has responsibility for organizing the context in which people make decisions” (p. 3). Choice architecture and traditional architecture both require planning and following guidelines/restrictions. The devil really is in the details. Every little thing matters! A choice architect can choose an arrangement or environment which provides individuals with the freedom to choose, but still “influence people’s behavior in order to make their lives longer, healthier, and better” (p. 5). Thus, a nudge.

The authors also describe the difference between Humans and Econs (these terms are utilized throughout the book). *Homo economicus*, or economic man (Econs), is based upon the idea that individuals think and choose unflinchingly well. Whereas with *homo sapiens* (Humans), the same cannot be said. We forget things and sometimes make bad choices. For this book, Humans are real and Econs are imaginary. It is important to identify this difference as a choice architect will need to consider this when developing a nudge.

As choice architects, we have opportunity to nudge people toward what is better for them. Thaler and Sunstein call this libertarian paternalism.

The libertarian aspect of our strategies lies in the straightforward insistence that, in general, people should be free to do what they like and to opt out of

undesirable arrangements if they want to do so. Libertarian paternalism is a relatively weak, soft, and non-intrusive type of paternalism because choices are not blocked, fenced off, or significantly burdened (p. 5).

The authors have divided this book into five sections. Each section consists of three to five chapters. They have also provided a Notes section, a bibliography, and an extensive index.

Humans and Econs

In Chapter 1, “Biases and Blunders,” the authors imply that we think within two systems; one is automatic, which they refer to as the Automatic System and the other is reflective, which means taking time to think before making a decision. This is called the Reflective System. In making choices or decisions, the Automatic System can be considered our gut reaction and the Reflective System as our conscious thought. One of the authors’ goals is to nudge readers to change and adapt so that we can rely upon our Automatic System to lead to easier, better, and longer lives.

Utilizing research, the authors identify how rules of thumb can lead to what they term “heuristics and biases.” Anchoring, availability, and representativeness heuristics are identified and discussed, as well as how optimism and overconfidence can lead to realistic or unrealistic decisions (which need a nudge). In almost all cases, individuals are loss averse which can lead to an emotional Automatic System; thus, holding us where we are at this current point in time.

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“...loss aversion operates as a kind of cognitive nudge, pressing us not to make changes, even when changes are very much in our interests” (p. 34).

Status quo is also a source of bias, which may come from a lack of attention. The authors use watching television as an example. If a TV viewer starts the evening watching a particular network, they are very likely to stay on that network for the entire evening due to a “devil may care” attitude. Another example shared related to automatic renewals; often viewed as defaults. The authors imply that default options can be very strong nudges. “...defaults have some extra nudging power because consumers may feel, rightly or wrongly, that default options come with an implicit endorsement from the default setter, be it an employer, government or television scheduler” (p. 35). As a choice architect, setting the best possible defaults is important.

How information is framed can influence individuals. The person framing information may interject their own biases. Choices can be affected based upon how a question is framed. Framing works because people tend to not think deeply about things and sometimes take the easy way out. In essence, even though we may make decisions automatically using biased rules of thumb, we are nudge-able.

Temptation began with Adam and Eve and it has continued over time, which is the focus of Chapter 2, “Resisting Temptation.” It is easier to recognize than define. The authors use the term arousal to explain temptation, a state of hot and cold. For example, if a person is very hungry and wonderful aromas are drifting from a bakery nearby, the person is said to be in a hot state and more easily tempted to consume more than in a cold state. Temptation is often accompanied by mindless choosing, sometimes termed as automatic pilot, or not really paying attention to the current task. For example, needing to run an errand on the weekend, but finding yourself driving to your office which is in the opposite direction. Eating is probably our most mindless action. We tend to eat whatever is placed in front of us or easily within our grasp. Research experiments have shown that subjects will continue to eat as long as food is in front of them, even if the food is stale popcorn (research experiment conducted by Brian Wansink and colleagues in a Chicago movie theater). This research also found that plate and package size were related to choice architecture and could be used as effective nudges.

Both temptation and mindless choosing are self-control issues. The authors talk about each person being made

up of two semiautonomous selves; a far-sighted “Planner” who uses the Reflective System (e.g., Mr. Spock from Star Trek), and a myopic “Doer” who uses the Automatic System (e.g., Homer Simpson). The Planner is working toward long-term success in retirement, but must put up with feelings and attitudes of the in the now Doer. “When self-control problems and mindless choosing are combined, the result is a series of bad outcomes for real people” (p. 44).

Since we know self-control may be an issue, we develop strategies to help us, (i.e., to-do-lists, grocery lists, and alarm clocks). In this case “our Planners are taking steps to control the actions of our Doers” (p. 44). One such strategy is informal bets. The example shared by the authors related to a Ph.D. candidate being hired as an instructor because the dissertation was not completed for graduation. The candidate’s Planner knew what he needed to accomplish, but the Doer was off to more new, exciting projects. The department head made a bet with the candidate. On the first of each month, the candidate would write a check for \$100 to the department head. If there was not one completed chapter of the dissertation slipped under the department head’s office door by midnight of the last day of that month, he would cash the check. The money would then be used for a party that the instructor/candidate would not be allowed to attend. The outcome of the department head’s stipulation was four chapters completed in 4-months time. Christmas clubs, although costly, are also an example of external efforts of our Planners trying to control the actions of our Doers.

One internal strategy used to assist with self-control is mental accounting. This is a method to process and control the family budget. Gamblers use it, in that recently won money is called house money. It is different from their money they started with for the evening.

In Chapter 3, “Following the Herd,” the authors provide more insight into Econs and Humans. Econs (remember they are imaginary) are unsociable. They communicate only for their own gain, but they are not followers. “Humans...are frequently nudged by other Humans” (p. 53). We can be influenced by the words and actions of others. Experiments conducted by psychologists and social scientists have proven individuals conform to group responses even if they know an answer is wrong 20% - 40% of the time. One-on-one counseling is more likely to give honest, correct information. In a group counseling situation, hearing someone else’s response may lead a person into giving the same response rather than his or her own. The ac-

tions of groups can be described by the terms “collective conservatism” and “pluralistic ignorance.” These terms refer to old patterns of behavior and believing we should think the same way because other people do. The authors emphasize information, peer pressure, and priming as the three social influences easily enlisted by private and public nudgers; “...both business and governments can use the power of social influence to promote many good (and bad) causes” (p. 73).

“When do we need a nudge?” is the title of Chapter 4. Are you asking yourself this question now? There is a short answer and a long answer to this question, but both get us to the same description. “...people will need nudges for decisions that are difficult and rare, for which they do not get prompt feedback, and when they have trouble translating aspects of the situation into terms that they can easily understand” (p. 74). Therefore, we need nudges when we have to make decisions fraught with choices-choosing between benefits now or costs later-issues with a high degree of difficulty, infrequent decisions, lack of feedback on decision results, and a history of making poor choices.

The final chapter in Section I (Chapter 5) describes the principles of choice architecture.

If you indirectly influence the choices other people make, you are a choice architect. And since the choices you are influencing are going to be made by Humans, you will want your architecture to reflect a good understanding of how humans behave. In particular, you will want to ensure that the Automatic System doesn't get all confused (p. 85).

These principles of choice architecture can be remembered with the assistance of a mnemonic device:

iNcentives
Understand mappings
Defaults
Give feedback
Expect error
Structure complex choices

As a choice architect, you can think about incentives by asking yourself a few questions: Who uses? Who chooses? Who pays? Who profits? The authors stress the need for salience when considering incentives, as there can be conflicts and manipulation, both of which can be good and bad. Understanding mappings relates to the relationship between choice and welfare. “A good system of choice ar-

chitecture helps people improve their ability to map and hence to select options that will make them better off” (p. 94). In a previous chapter, the authors discussed designing environments so that the Automatic System does not get confused. You have to make information understandable (e.g., adapt numerical information into a language that can be readily translated into actual use).

Thaler and Sunstein propose a bit of government regulation related to libertarian paternalism they call RECAP: Record, Evaluate, and Compare Alternative Prices. The regulation applies to disclosing prices and fees that are easily understood and comparable side-by-side with similar options. This strategy is considered in the following sections of the book to assist in choice architecture.

The authors call defaults ubiquitous and powerful, and also unavoidable. Defaults are a definite aspect of choice architecture as there must be a rule of thumb to cover a decision maker's lack of deciding. As a choice architect, you can force choosers to make a choice. The authors call this forced “required choice” or “mandated choice.” However, Humans tend to “consider required choice to be a nuisance” (p. 88), and it is generally more appropriate for complex choices than simple yes-or-no decisions.

Giving feedback enables Humans to learn from their mistakes and indecision. Good choice architecture “tells people when they are doing well and when they are making mistakes” (p. 92). Choice architecture should expect that everyone makes mistakes and be as forgiving as possible.

Selecting strategies for making choices depends upon the size and complexity of options. If the options are limited and well-known, we review the alternatives and make trade-offs, if necessary. We might use a compensatory strategy where a high value of one attribute can compensate for another attribute with a low value (i.e., selecting an office at a new job). Another option would be to use an “eliminate by aspect” approach, in that you decide which aspect is most important, establish a cutoff point, and then eliminate alternatives that do not make the cut (i.e., choosing an apartment in the city of a new job). However, if choices are large in number and may be outside our common knowledge, we tend to use simplifying strategies. In this case, “choice architects have more to think about and more work to do, and are much more likely to influence choices (for better or worse). Structuring choice sometimes means helping people to learn, so they can later make better choices on their own” (p. 99).

Money

Humans and Econs manage money very differently. Econs are savers and they spend money responsibly. The same cannot be said for Humans. Section II of the book discusses saving, investing, and borrowing, and explores how we can do a better job with these tasks.

The theme for Chapter 6 is Humans are not good at saving. Thaler and Sunstein offer two suggestions (actually, they are nudges), automatic enrollment and the *Save More Tomorrow* program. Enrollment decisions become the nudge. One option is to make savings automatic (make it the default). Forced choice in a yes-or-no situation is an alternative to automatic enrollment. Simplifying the entire process is also seen as a strategy.

Automatic enrollment and forced choosing generally have low default savings rates and very conservative investment choices. People can be nudged to spend more time choosing a savings rate (doing their own research and through education) and to contribute at least the minimum amount necessary to get the full employer match. Employers also try to provide education to assist their employees in making better decisions.

The *Save More Tomorrow* program is a choice-architecture system designed by Thaler and Shlomo Benartzi, based upon the premise of automatic escalation of retirement savings plan contributions over time. *Save More Tomorrow* invites participants to commit themselves in advance to a series of contribution increases timed to coincide with pay raises.

While it may seem that automatic savings escalation occurs only in the private sector (and without any nudging from government), the authors indicate there is a role for government. In most cases, the government has just stayed out of the way. The Pension Protection Act of 2006 served as an incentive to employers “to match employee contributions, automatically enroll them in the plan, and automatically increase their contribution rates over time” (pp. 117-118). This is an excellent nudge.

Unfortunately the government can also blunder (i.e., the Social Security Administration-SSA). Every Human can figure this out as there is only one decision we are allowed to make, when to start claiming it. Determining when to start receiving Social Security benefits is tricky and several factors should be considered in the decision. At the printing of this book, SSA had very limited tools to assist

Humans; they definitely did not have a choice architect on staff as this person would have utilized important retirement factors and developed a possible default option. The authors feel that “in an environment in which people have to make only one decision per lifetime, we should surely try harder to help them get it right” (p. 119).

Next comes how to invest the money (Chapter 7, “Naïve Investing”). Topics in this chapter include risk, asset allocation, stocks or bonds. Econs love these types of decisions. Humans, on the other hand, become very confused. If the choice architecture was more helpful, Human investors might make fewer investment mistakes.

Chapter 7 also discusses investing rules of thumb regarding investment selection and company stock. The authors discuss aspects of company stock at length and suggest a strategy they call Sell More Tomorrow. It “gives employees the option to sell off their shares gradually over a period of time, with the proceeds directed into a diversified portfolio” (p. 130). They also describe how nudges can be applied to Humans’ investing decisions.

Reviewing mortgage loans, student loans, and credit cards within choice architecture is the focus of Chapter 8, “Credit Markets.” The majority of the discussion, statistics, examples, and strategies are not unknown, nor a surprise, to financial researchers and educators. The most important take-away message from this entire chapter is that “when markets get more complicated, unsophisticated and uneducated, shoppers will be especially disadvantaged by the complexity” (p. 136).

Privatizing Social Security is not a new idea. Presidents have been discussing the issue for the past several years. Chapter 9 shares Sweden’s system and their trials and tribulations experienced throughout the process. According to the authors, Sweden’s main problem was they did not use the best choice architecture. They used a maximizing choices approach that experiences bias and inertia issues. They also encouraged participants to choose their own retirement investment portfolio.

Health

The third section of this book focuses on health-related issues. Doctors are crucial choice architects in the health area. Another strong factor in health is social influence. Three specific topics included in this section include Medicare Part D, organ donation, and the environment.

The title of Chapter 10 is “Prescription Drugs: Part D for Daunting.” An apt title, for that was true for many senior citizens across the United States. Thaler and Sunstein indicate that Part D met planner’s expectations; however, “as a piece of choice architecture, it suffered from a cumbersome design that impeded good decision making” (p. 162). The authors suggest nudges to improve the choice architecture. The first possibility is to replace random default plan assignment with intelligent assignment, providing a better system to match seniors and drug plans. Secondly, RECAP could be used to nudge seniors away from choosing the status quo and to encourage them to comparison shop to meet their prescription needs, as prices would be salient. Part of this would also be to show the costs of delaying selection. When there are many options and the whole process is complex, the more important good choice architecture becomes.

The authors share enlightening information about the organ donation process and outcomes (Chapter 11). Choice architecture, as in a good default plan, could go a long way in saving the lives of many individuals in need of a kidney, heart, etc. Consent seems to be the largest obstacle. The authors recommend an opt-out default plan. Unless individuals specifically register to opt out, they will be considered future organ donors.

Choice architecture can also be applied to environmental protection (Chapter 12, “Saving the Planet”). Usual steps to control emissions and other greenhouse gases were taxes or cap-and-trade systems; both are considered on command-and-control regulations. The authors consider incentive-based approaches to be more effective and efficient, with increased freedom of choice. There are many examples of regulations and experiments conducted to improve environmental issues, including an apparatus that would glow red or green depending up a consumers’ electrical usage. Providing feedback to consumers would improve information delivery and disclosure.

Freedom

According to Thaler and Sunstein, “libertarian paternalists care about freedom; they are skeptical about approaches that prevent people from going their own way” (p. 199). Section IV covers issues of choice on three controversial areas; education, patients and doctors, and marriage. “Improving School Choices” (Chapter 13) starts with the authors sharing the work of Milton Friedman’s argument that the best way to improve our children’s schools is to

introduce competition. Choice architecture, with regards to education, is creating plans to put parents in a position to make sensible decisions for their children. Examples of schools competing are presented, many relating to school performance issues. Students could transfer to a better school if their current school scored low on certain assessments. However, schools made it difficult for parents to do so, to the point of being discouraging. As with other topics of this book, to have more choices and hope parents make good choices, schools need to put parents in situations to think through their choices and exercise their freedom rather than settling for the default option.

Thaler and Sunstein’s discussion of enabling patients and doctors to make contracts for services, including waiving the right to sue, was very enlightening. They title this chapter “Should Patients be Forced to Buy Lottery Tickets?” (Chapter 14), which is interesting in itself. The purchase of health insurance includes or forces consumers/patients to also purchase the right to sue as a part of the insurance policy. Consumers may be able to choose lower cost health care if given options and are informed about alternatives to gain the best health care for themselves and their family.

“Privatizing Marriage” (Chapter 15) may test you. Thaler and Sunstein propose that marriage be privatized, including the removal of the word *marriage* from any laws and that “marriage licenses would no longer be offered or recognized by any level of government” (p. 217). The removal from laws relates to separation of church and state; government minding its own business and churches doing the same. Thaler and Sunstein want to remove any doubt that the word marriage, as it is now, signifies both an official legal status and a religious one. They suggest a domestic partnership agreement between two people similar to a partnership agreement in the business world. There is also discussion of who needs protection in the agreement, options for child support payments, and whether the term marriage is appropriate in today’s world. Regarding choice architecture, the key is to identify appropriate default rules when people make a commitment to each other clearer sense of rights and obligations and protect the vulnerable (generally women and children).

Extensions and Objections

Section V contains a variety of information including two chapters on 36 specific nudges; one chapter about objections to nudges, and the Notes, Bibliography, and Index.

Some examples of nudges that have direct applications to personal finance include the following:

- *Give More Tomorrow* (*Save More Tomorrow* was mentioned earlier in the review). People want to give more, but due to inertia, give less than they want. The nudge is to ask people whether they want to give a small amount to their favorite charities now, and then commit to increasing donations every year.
- *The Charity Debit Card and tax deductions*. The nudge would be to make it easier for us to deduct our charitable contributions. The Charity Debit Card would be a special debit card issued by banks and only accepted by charities. Any donations would be deducted from your normal account (checking or savings), and the bank sends you a statement at the end of the year with your donations itemized and totaled.
- *The Automatic Tax Return*. Anyone who does not itemize and has no income (such as tips) that is not reported to the IRS would receive a tax return already filled out. The taxpayer would only need to sign and return it, or go to an IRS secured website, and in and click. Taxpayers would need to make changes only if their filing status changed. Other countries are already doing this!
- *Smart meters*. These are meters and thermostats that nudge customers to program heating and cooling more precisely throughout the day, while raising rates during peak afternoon hours.
- *An affordable home energy meter*. A wireless meter that connects to a home's energy use and displays electricity usage in watts or money. Blue glow shows less electricity than normal being used; red glow means the opposite.

Summary

Thaler and Sunstein have provided a framework/model to be applied and used across the spectrum of health, wealth, freedom, and other aspects of life. They back up their discussion of choice architecture with proven research, experiments, and surveys. *Nudge* provides readers with information and guidance to help create an environment where clients, learners, students, and even family members will make decisions to help themselves become healthier, wealthier, and hopefully, wiser.

Recommendation

The authors utilize research from psychology, economics, social sciences, health, and finance to provide readers with the background and framework within which to apply choice architecture in their own company, place of business, and even in the home. Examples are shared from research as well as from the author's own experiences and background.

This reviewer has found this book to be a challenge, not in readability or length, but in making me more aware of how I design teaching environments, materials, and hand-outs for learners. By making choice architecture a priority, learners can be *nudged* to make better decisions for their family's financial future.

Are you a choice architect? Do you have responsibility for organizing the context of how others learn and make decisions? In other words, are you a nudge? This reviewer hopes this review will influence you to read this book. [You are being nudged!]