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## Nudge

### Improving Decisions About Health, Wealth, and Happiness

#### THE SUMMARY IN BRIEF

Every day, we make decisions on topics ranging from personal investments to schools for our children to the meals we eat. Unfortunately, we often choose poorly. *Nudge* invites us to explore how we make those decisions and how we can be led to make better ones. By knowing how people think, we can design choice environments that make it easier for people to choose what is best for themselves, their families and their society.

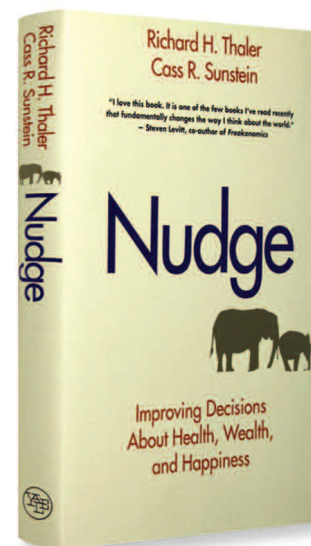
Drawing on decades of cutting-edge behavioral science research, Richard H. Thaler and Cass R. Sunstein offer an insightful new perspective on how to improve the decisions we make in everything we do — from public policy issues, such as health care, to personal decisions, such as saving for retirement. They demonstrate how thoughtful, choice architecture can be established to *nudge* us in beneficial directions, a process they label “libertarian paternalism.”

The libertarian aspect of their 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 so desire. Their approach maintains or increases freedom of choice by making it easy for people to go their own way.

*Nudge* is about choices. By learning about choice architecture, you will be able to successfully nudge people toward the best decisions without restricting their freedom of choice.

#### IN THIS SUMMARY, YOU WILL LEARN:

- How people make the choices they do.
- Why people make bad decisions.
- How government and companies can nudge people in the right direction.
- What you need to know how to design the best possible choice environment.
- When people need a nudge.



by Richard H. Thaler and  
Cass R. Sunstein

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# THE COMPLETE SUMMARY: NUDGE

by Richard H. Thaler and Cass R. Sunstein

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## Introduction

Carolyn is the director of food services for a large city school system. She is in charge of hundreds of schools, and hundreds of thousands of kids eat in her cafeterias every day. One evening, she hatched an interesting idea. Without changing any menus, she would run experiments in her schools to determine whether the way the food is displayed and arranged might influence the choices kids make. In some schools the desserts were placed first, in others last, in still others in a separate line. The location of various food items was varied from one school to another.

Simply by rearranging the cafeteria, Carolyn was able to increase or decrease the consumption of many food items by as much as 25 percent. School children, like adults, can be greatly influenced by small changes in context. The influence can be exercised for better or for worse. For example, Carolyn knows that she can increase consumption of healthy foods and decrease consumption of unhealthy ones.

Carolyn is a *choice architect*. A choice architect has the responsibility for organizing the context in which people make decisions. Although Carolyn is an imaginary person, many real people turn out to be choice architects. If you design the ballot voters use to choose candidates, you are a choice architect. If you are a doctor and must describe the alternative treatments available to a patient, you are a choice architect. If you are a parent, describing possible educational options to your son or daughter, you are a choice architect.

Just as a building architect must eventually build some

particular building, a choice architect like Carolyn must choose a particular arrangement of the food option at lunch, and by so doing she can influence what people eat. She can *nudge*.

### 'Libertarian Paternalism'

If you think that Carolyn should take the opportunity to nudge the kids toward food that is better for them, you would be welcomed into the *libertarian paternalism* movement.

When the term libertarian is used to modify the word paternalism, it simply means liberty-preserving. Libertarian paternalists want to make it easy for people to go their own way; they do not want to burden those who want to exercise their freedom.

Libertarian paternalism is a relatively weak, soft and nonintrusive type of paternalism because choices are not blocked, fenced off or significantly burdened. If people want to smoke cigarettes, eat a lot of candy, choose an unsuitable health care plan or fail to save for retirement, libertarian paternalists will not force them to do otherwise — or even make things hard for them.

Still, the recommended approach counts as paternalistic because private and public choice architects are not merely trying to track or implement people's anticipated choices. Rather, they are self-consciously attempting to move people in directions that will make their lives better. They nudge.

A nudge is any aspect of the choice architecture that alters people's behavior in a predictable way without forbidding any options or significantly changing their



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economic incentives. Putting fruit at eye level counts as a nudge. Banning junk food does not. ●

### Biases and Blunders

Most of us are busy. Our lives are complicated and we can't spend all our time thinking and analyzing everything. When we have to make judgments, we use simple rules of thumb to help us.

#### Rules of Thumb

Although rules of thumb can be very helpful, their use can also lead to systematic biases. This insight, was first developed decades ago by two Israeli psychologists, Amos Tversky and Daniel Kahneman (1974). Their original work identified three heuristics, or rules of thumb: anchoring, availability and representativeness — and the biases that are associated with each.

**Anchoring.** Suppose we are asked to guess the population of Milwaukee. We may not know much about Milwaukee, but let's guess that it is the biggest city in Wisconsin. To guess at its population, you typically start with something you know, which is the population of Chicago, roughly three million. So we might think, Milwaukee is a major city, but clearly not as big as Chicago, so maybe it is one-third the size.

Now consider someone from Green Bay, Wisconsin, who is asked the same question. She also doesn't know the answer, but she does know that Green Bay has about 100,000 people and knows that Milwaukee is larger, so guesses three times larger — 300,000.

The process is called “anchoring and adjustment.” You start with some anchor, the number you know, and adjust in the direction you think is appropriate. The bias occurs because the adjustments are typically insufficient.

Anchors serve as nudges. We can influence the figure you will choose in a particular situation by ever-so-subtly suggesting a starting point for your thought process. When charities ask you for a donation, they typically offer you a range of options. These values are not picked at random, because the options influence the amount of money people decide to donate.

**Availability.** How much should you worry about hurricanes, nuclear power, terrorism, mad cow disease, alligator attacks or avian flu? And how much care should you take in avoiding risks associated with each? In answering questions of this kind, most people use what is called the “availability” heuristic.

They assess the likelihood of risks by asking how read-

ily examples come to mind. If people can easily think of relevant examples, they are far more likely to be frightened and concerned than if they cannot. A risk that is familiar, like that associated with terrorism in the aftermath of 9/11, will be seen as more serious than a risk that is less familiar.

When “availability bias” is at work, both private and public decisions may be improved if judgments can be nudged back in the direction of true probabilities.

**Representativeness.** Another heuristic bears an unwieldy name: “representativeness.” Think of it as the similarity heuristic. The idea is that when asked to judge how likely it is that A belongs to category B, people answer by asking themselves how similar A is to their image or stereotype of B (that is, how “representative” A is of B).

Use of the representativeness heuristic can cause serious misperceptions of patterns in everyday life. When events are determined by chance, such as a sequence of coin tosses, people expect the resulting string of heads and tails to be representative of what they think of as random. Unfortunately, people do not have accurate perceptions of what random sequences look like. When they see the outcomes of random processes, they often detect patterns that they think have great meaning but, in fact, are just due to chance.

#### Optimism and Overconfidence

People are unrealistically optimistic even when the stakes are high. Smokers are aware of the statistical risks, and often even exaggerate them, but most believe that they are less likely (than the average smoker) to be diagnosed with lung cancer and heart disease.

Unrealistic optimism is a pervasive feature of human life; it characterizes most people in most social categories. When they overestimate their personal immunity from harm, people may fail to take sensible preventive steps. If people are running risks because of unrealistic optimism, they might be able to benefit from a nudge.

People hate losses. Roughly speaking, losing something makes you twice as miserable as gaining the same thing makes you happy.

Loss aversion helps produce inertia, meaning a strong desire to stick with your current holdings. If you are reluctant to give up what you have because you do not want to incur losses, then you will turn down trades you might have otherwise made. Loss aversion operates as a kind of cognitive nudge, pressing us not to make changes, even when changes are very much in our interest.

Loss aversion is not the only reason for inertia. For

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lots of reasons, people have a more general tendency to stick with their current situation. Most teachers know that students tend to sit in the same seats in class, even without a seating chart. But status quo bias can occur even when the stakes are much larger, and it can get us into a lot of trouble.

For example, in retirement savings plans, most participants pick an asset allocation and then forget about it. In one study, the median number of changes in the asset allocation of the lifetime of a professor was, believe it or not, zero. Perhaps even more telling, many married participants who were single when they joined the plan still have their mothers listed as their beneficiaries. ●

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### Resisting Temptation

Self-control problems can be illuminated by thinking about an individual as containing two semi-autonomous selves, a far-sighted “Planner” and a myopic “Doer.” The Planner is trying to promote your long-term welfare but must cope with the feelings, mischief and strong will of the Doer, who is exposed to temptations.

In many situations, people put themselves into an “automatic pilot” mode in which they are not actively paying attention to the task at hand. When self-control problems and mindless choosing are combined, the result is a series of bad outcomes for real people.

Millions of Americans still smoke in spite of the evidence that smoking has terrible health consequences, and significantly, the overwhelming majority of smokers say that they would like to quit. Nearly two-thirds of Americans are overweight or obese. Many people never get around to joining their company’s retirement savings plan, even when it is heavily subsidized. Together, these facts suggest that significant numbers of people could benefit from a nudge.

#### Self-Control Strategies

Since people are at least partly aware of their weaknesses, they take steps to engage outside help. We make lists to help us remember what to buy at the grocery store. We buy an alarm clock to help us get up in the morning. We ask friends to stop us from having dessert or to fortify our efforts to quit smoking. In these cases, our Planners are taking steps to control the actions of our Doers, often by trying to change the incentives that Doers face. Unfortunately, Doers are often difficult to rein in and they can foil even the best efforts of Planners.

Alarm clocks and Christmas clubs are external devices people use to solve their self-control problems. Another

way to approach these problems is to adopt internal control systems, otherwise known as “mental accounting.” Mental accounting is the system that households use to evaluate, regulate and process their home budget. Almost all of us use mental accounts, even if we’re not aware that we’re doing so.

The concept is illustrated well by an exchange between the actors Gene Hackman and Dustin Hoffman. Hackman and Hoffman were friends back in their starving-artist days, and Hackman tells the story of visiting Hoffman’s apartment and having his host ask him for a loan. Hackman agreed to the loan, but then they went into Hoffman’s kitchen where several mason jars were lined up on the counter, each containing money. One jar was labeled “rent,” another “utilities” and so forth. Hackman asked why, if Hoffman had so much money in jars, he could possibly need a loan, whereupon Hoffman pointed to the food jar, which was empty.

Most organizations have budgets for various activities and it is always a source of frustration when an important purchase cannot be made because the relevant account is already depleted. The fact that there is unspent money in another account is considered no more relevant than the money sitting in the rent jar on Hoffman’s kitchen counter. ●

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### Following the Herd

Humans are frequently nudged by other humans. Sometimes massive social changes, in markets and politics alike, start with a small social nudge. Humans are not exactly lemmings, but they are easily influenced by the statements and deeds of others.

Understanding how and why social influences work is important in this context for two reasons. First, most people learn from others. This is usually good, of course. Learning from others is how individuals and societies develop. But many of our biggest misconceptions also come from others. When social influences have caused people to have false or biased beliefs, some nudging may help.

The second reason why this topic is important is that one of the most effective ways to nudge (for good or evil) is via social influence. Choice architects need to know how to encourage socially beneficial behavior, and also how to discourage the opposite.

Social influences come in two basic categories. The first involves information. If many people do something or think something, their actions and thoughts convey information about what might be best for you to do or

think. The second involves peer pressure. If you care about what other people think about you then you might go along with the crowd to avoid their wrath or curry their favor.

The bottom line is that humans are easily nudged by other humans. Why? One reason is that we like to conform. ●

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### When Do We Need a Nudge?

For all their virtues, markets often give companies a strong incentive to cater to (and profit from) human frailties, rather than to try to eradicate them or minimize their effects.

Suppose you are told that a group of people will have to make some choices in the near future. You are the choice architect. You are trying to decide how to design the choice environment, what kinds of nudges to offer and how subtle the nudges should be. What do you need to know to design the best possible choice environment? Here are some kinds of situations in which people are least likely to make good choices:

**Benefits Now — Costs Later.** Predictable problems arise when people must make decisions that test their capacity for self-control. Self-control issues are most likely to arise when choices and their consequences are separated in time. At one extreme are what might be called “investment goods,” such as exercise, flossing and dieting. For these goods, the costs are borne immediately, but the benefits are delayed. At the other extreme are what might be called “sinful goods”: smoking, alcohol and jumbo chocolate doughnuts are in this category. We get the pleasure now and suffer the consequences later. Both investment goods and sinful goods are prime candidates for nudges.

**Degree of Difficulty.** We use spellcheckers and spreadsheets to help with hard problems, but many problems are quite difficult, and often there is no easy technology available to help.

**Frequency.** Even hard problems become easier with practice. Unfortunately, some of life’s most important decisions do not come with many opportunities to practice. Most students choose a college only once. Most of us choose a spouse. Few of us get to try many different careers. We get one chance to save for retirement. Generally, the higher the stakes, the less often we are able to practice. Rare, difficult choices are good candidates for nudges.

**Feedback.** Even practice does not make perfect if people lack good opportunities for learning. Learning is most likely if people get immediate, clear feedback after

each try. We usually get feedback only on the options we select, not the ones we reject. Unless people go out of their way to experiment, they may never learn about alternatives to the familiar ones. When feedback does not work, we may benefit from a nudge.

**Knowing What You Like.** It is particularly hard for people to make good decisions when they have trouble translating the choices they face into the experiences they will have. Take the problem of choosing a mutual fund for your retirement portfolio. When people have a hard time predicting how their choices will end up affecting their lives, they have less to gain by numerous options and perhaps even by choosing for themselves. A nudge might be welcomed.

People may need a good nudge most for choices that have delayed effects; those that are difficult, infrequent and offer poor feedback; and those for which the relation between choice and experience is ambiguous.

### Markets: A Mixed Verdict

A natural question is whether free markets can solve people’s problems, even under such circumstances. Often, market competition will do a lot of good. But in some cases, companies have a strong incentive to cater to people’s frailties and to exploit them.

Most of the time, competition ensures that price serves as a good signal of quality. Usually (but not always) the \$50 bottles of wine are better than the \$20 bottles and irrational consumers will not alter the market as long as they do not predominate.

For irrational consumers to be protected there has to be competition. Consider the case of extended warranties on small appliances, typically a bad deal for consumers. Do market forces drive these unduly expensive extended warranties from the market? Or does competition drive the price of the extended warranties down to the expected value of the claims? The answers to these questions are no and no.

You might think that firms could educate people not to buy the warranty, and indeed they might. But why should firms do that? If you are buying something that you shouldn’t, how do I make any money persuading you not to buy it? ●

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### Choice Architecture

Many people will take whatever option requires the least effort, or the path of least resistance. If, for a given choice, there is a default option, then we can expect a large number of people to end up with that option, whether or not it is good for them. These behavioral

tendencies toward doing nothing will be reinforced if the default option comes with some implicit or explicit suggestion that it represents the normal or even the recommended course of action.

Many organizations in both the public and the private sector have discovered the immense power of default options. Remember the idea of automatic renewal for magazine subscriptions? If renewal is automatic, many people will subscribe, for a long time, to magazines they don't read. Note that not all defaults are selected to make the chooser's life easier or better.

### Expect Error

Humans make mistakes. A well-designed system expects its users to err and is as forgiving as possible. Consider that over the years, automobiles have become much friendlier to their operators. If you do not buckle your seat belt, you are buzzed. If you are about to run out of gas, a warning sign appears and you might be beeped. If you need an oil change, your car might tell you. Many cars come with an automatic switch for the headlights that turns them on when you are operating the car and off when you are not, eliminating the possibility of leaving your lights on overnight and draining the battery.

The best way to help people improve their performance is to provide feedback. Well-designed systems tell people when they are doing well and when they are making mistakes. Our laptops warn us to plug in or shut down when the battery is dangerously low. But warning systems have to avoid the problem of offering so many warnings that they are ignored. If our computer constantly nags us about whether we are sure we want to open that attachment, we begin to click "yes" without thinking about it. These warnings are thus rendered useless.

### Understanding 'Mappings'

Some tasks are easy, like choosing a flavor of ice cream; other tasks are hard, like choosing a medical treatment. A good system of choice architecture helps people improve their ability to map and hence to select options that will make them better off.

One way to do this is to make the information about various options more comprehensible, by transforming numerical information into units that translate more readily into actual use.

Take the example of choosing a digital camera. Cameras advertise their megapixels, and the impression created is certainly "the more megapixels the better." What is really problematic for consumers is translating megapixels into what they care about. Is it worth paying

## Save More Tomorrow

Although automatic enrollment is effective at getting new and young workers to enroll sooner than they would have otherwise, participants tend to stick with the default contribution rate, which is typically quite low. To mitigate this problem, consider a program of automatic escalation of contributions: Save More Tomorrow.

This program invites participants to commit themselves, in advance, to a series of contribution increases timed to coincide with pay raises. By synchronizing pay raises and savings increases, participants never see their take-home amounts go down, and they don't view their increased retirement contributions as losses. Once someone joins the program, the saving increases are automatic, using inertia to increase rather than prevent savings.

an additional \$100 to go from four to five megapixels? Suppose instead that manufacturers listed the largest print size recommended for a given camera.

Often people have a problem in mapping products into money. Think about credit cards, mortgages, cell phone calling plans and auto insurance policies, just to name a few. For these and related domains, a very mild form of government regulation, a species of libertarian paternalism, is suggested called RECAP: Record, Evaluate and Compare Alternative Prices. The government would not regulate how much issuers could charge for services, but it would regulate their disclosure practices.

### Structure Complex Choices

People adopt different strategies for making choices depending on the size and complexity of available options. When we face a small number of well-understood alternatives, we tend to examine all the attributes of all the alternatives and then make trade-offs when necessary.

Social research reveals that as the choices become more numerous and/or vary on more dimensions, people are more likely to adopt simplifying strategies. Good choice architecture will provide structure, and structure will affect outcomes.

Many companies, such as Netflix, the mail-order DVD rental company, succeed in part because of immensely helpful choice architecture. Customers looking for a movie to rent can easily search by actor, director, genre and more, and if they rate the movies they

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have watched, they can also get recommendations based on the preferences of other movie lovers with similar tastes, a method called “collaborative filtering.”

Choice architects must think about incentives when they design a system. Sensible architects will put the right incentives on the right people.

Free markets often solve all of the key problems by giving people an incentive to make good products and to sell them at the right price. ●

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### Money

In 2005, the personal savings rate for Americans was negative for the first time since 1932 and 1933 — the Great Depression years. On average, American households spent more than they earned and borrowed more than they saved. Increased borrowing rates were fueled by substantial growth in home equity loans and in credit card debt. For many Americans, savings rates, especially retirement savings, are woefully low, if not zero.

#### Enrollment: Nudging People to Join

What can be done to help? An obvious answer is to change the default rule. As things now stand, the default is nonenrollment; you have to do a little work to get into a retirement program. Forms can be a headache and many employees just put them aside. An alternative is to adopt automatic enrollment. Here’s how it works. When an employee first becomes eligible, he or she receives a form indicating that he or she will be enrolled in the plan (at a specified savings rate and asset allocation), unless he or she actively fills out a form asking to opt out.

An alternative to automatic enrollment is simply to require every employee to make an active decision about whether to join the plan. A related strategy is to simplify the enrollment process. One study tested this idea by analyzing a simplified enrollment form. New employees were handed enrollment cards during orientation with a “yes” box for joining the plan at a 2 percent saving rate and a preselected asset allocation. Employees did not have to spend time choosing a savings rate and asset allocation. As a result, participation rates during the first four months of employment jumped from 9 percent to 34 percent.

#### Credit Markets

Mortgage shopping has now become more complicated. Borrowers can choose from a variety of fixed-rate loans and also numerous “variable rate” loans. Borrowers

might also consider such exotic products as interest-only loans. When markets get more complicated, unsophisticated and uneducated shoppers will be especially disadvantaged by the complexity.

Shopping for a student loan is nearly as complicated as looking for a mortgage. One helpful nudge would be to simplify the financial aid application. The complicated format of these forms can discourage students from applying for financial aid and cause them to seek price direct-to-consumer loans instead.

The credit card is a ubiquitous feature of modern life. The Census Bureau reported that there were more than 1.4 billion credit cards in 2004 — an average of 8.5 cards per cardholder. Currently, 115 million Americans carry a month-to-month credit card debt.

For mortgages, school loans and credit cards, life is far more complicated than it needs to be, and people can be exploited. Often it’s best to ask people to take care of themselves, but when people borrow, standard human frailties can lead to serious hardship. Here, as elsewhere, government should respect freedom of choice; but with a few improvements in choice architecture, people would be far less likely to choose badly. ●

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### Health

Libertarian paternalists see countless opportunities for improving people’s health. People who know obese people are more likely to be obese themselves; weight loss can be contagious, too. Framing matters: people are more likely to engage in self-examinations for skin and breast cancer if they are told not about the reduced risk if they do so, but about the increased risk if they fail to do so.

Doctors are crucial choice architects, and with an understanding of how people think, they could do far more to improve people’s health.

#### Prescription Drugs: Part D for Daunting

The largest overhaul in Medicare’s history, Part D created a half-trillion-dollar federal subsidy for prescription drug coverage. This was no laissez-faire system. The national government imposed a lot of structure. Before consumers could even begin to choose, the government set minimum coverage requirements and approved all private plans.

The system of constrained free choice might seem like a nice example of libertarian paternalism in action. As a health care delivery system, Part D met its planners’

## Summary: NUDGE

expectations reasonably well. As a piece of choice architecture, however, it suffered from a cumbersome design that impeded good decision-making. It offered a menu with lots of choices, which is fine, but it had four major defects:

1. It gave participants little guidance to help them make the best selections from that menu.
2. The default for most seniors was nonenrollment.
3. It chose a default at random for 6 million people who were automatically enrolled, and it actively resisted efforts to match people and plans based on their prescription drug histories.
4. It failed to serve the most vulnerable population, specifically the poor and the poorly educated.

Do not misunderstand. Part D has done a lot of good. But there is plenty of room for better choice architecture. Maximizing choices is not enough to create good policy. The more choices there are, and the more complex the situation, the more important it is to have enlightened choice architecture.

### Saving the Planet

In recent decades, governments all over the world have been taking aggressive steps to protect the environment. Most of the time, governments seeking to protect the environment and to control the harmful health effects of pollution have gone well beyond a nudge, and their steps have not been libertarian. Typically regulators have chosen some kind of command-and-control regulation. Catalytic converters for cars are one example.

More often, government officials do not specify technologies, but require across-the-board reductions in emissions. They might say, for example, on average, all new cars must emit 90 percent less carbon monoxide, on average, than they do now. Philosophically, however, such limitations look uncomfortably similar to Soviet-style five-year plans, in which bureaucrats in Washington announce that millions of people have to change their conduct in the next five years.

When incentives are badly aligned, it is appropriate for government to try to fix the problem by realigning them. In the environmental area, two broad approaches have been proposed.

The first is to impose taxes or penalties on those who pollute. In the domain of climate change, a tax on greenhouse gas emissions is a simple example.

The second approach is called a cap-and-trade system. In such systems, those who pollute are given (or sold) “rights” to pollute in certain amounts and these rights

are then traded in a market. Incentive-based approaches are more efficient and more effective, and they also increase freedom of choice.

Especially when compared with command-and-control systems, economic incentives have a strong libertarian element. Liberty is much greater when people are told, “You can continue your behavior, so long as you pay for the social harm that it does” than when they are told, “You must act exactly as the government says.”

### Objections — Evil Nudgers and Bad Nudges

In offering supposedly helpful nudges, choice architects may have their own agendas. Those who favor one default rule over another may do so because their own economic interests are at stake, as in when companies offer you a special rate for the first month, then automatically reenroll you in the program at a higher rate after the introductory period.

Real architects can have conflicts of interest with their clients as well, but they should not necessarily stop designing buildings. Instead, we need to try to line up incentives when we can and employ monitoring and transparency when we can't.

### The Real Third Way

You have been presented with two major claims. The first is that seemingly small features of social situations can have massive effects on people's behavior; nudges are everywhere, even if we do not see them. Choice architecture, both good and bad, is pervasive and unavoidable, and it greatly affects our decisions.

The second claim is that libertarian paternalism is not an oxymoron. Choice architects can preserve freedom of choice while also nudging people in directions that will improve their lives.

Understanding choice architecture and the power of nudges hopefully will lead others to think of creative ways to improve human lives in other domains. ●

#### RECOMMENDED READING LIST

If you liked *Nudge*, you'll also like:

1. ***The Heart of Change* by John Kotter and Dan Cohen.** Built around eight steps of change first introduced in Kotter's earlier works, this book gives straight advice on successful change.
2. ***The Speed of Trust* by Stephen M.R. Covey.** Trust is central to the success of every relationship. Covey demonstrates the best ways to establish trust or repair it in the event it has been broken.
3. ***The Hands-Off Manager* by Steve Chandler and Duane Black.** Offering an opposing view to *Nudge*, this book postulates that employees need gentle coaching rather than management by force.