

Review of “How Change Happens”

by Cass Sunstein

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This book from the co-author of Nudge (Thaler and Sunstein, 2008) has important lessons for public policy and especially financial policy in an era when doubts about “elites” and their unaccountable power is rising. Sunstein’s book arrives as just the latest in an extensive line of his works considering how we might best combine the free markets that have made us wealthy, with the social justice that makes a materially comfortable life worthwhile (Sunstein, 1997). Those of us who favour free financial markets, as engines of financial wealth and risk management, may wish to heed the concerns Sunstein raises in this and related works.

At its broadest, Sunstein’s subject is the drivers of social change. He frequently illustrates this with reference to the struggle for equal rights by women and blacks. But as finance scholars, we might think of the swings in popularity of financial capital; from angels in the mid-1990s to devils in the late noughties. If the inherent relative merits of women, blacks and financial capitalists have remained broadly the same over time, why has our view, and even our laws, changed so much with respect to these groups? If Universal Banks were a good thing in 1995, why did they seem so bad by 2015? If big CEO bonuses were in vogue in the 1980s, why had the tide already turned by the start of the millennium?

I structure my discussion of the book, largely, around the three chapter themes he adopts:

- (1) the establishment and evolution of social norms, Chapters 1–3;
- (2) nudging, Chapters 4–11; and
- (3) how our chosen political philosophy might be informed by developments in behavioural science, Chapters 12–16.

1. Social norms

Social norms evolve, but we are not clear how or why. Laws work best when supported by social norms, against drunk-driving, or racist abuse. But laws also shape our tastes. So as Sunstein puts it “the unthinkable becomes the unthought” (Sunstein, 2019b, p. 9). But initial conditions are important. What if Rosa Parks just sat at the back of the bus? What if Rose McGowan had just thought “that’s just Harvey”; as so many had before?



Similarly [Roe \(2003\)](#) sees social crises and war determining a nation's corporate governance settlement. So crises are functional in financial markets, but they are also highly contingent. So as others have pointed out where would be now Bear Stearns had been allowed to fail, sending a warning shot to Lehman's Board ([Roberts, 2010](#))?

To judge a social norm about how to dress, speak, properly I look to others in my peer group. Sunstein points out the problem is I then see what others do; but not what they believe. I may inhabit a sexist, or religiously bigoted, society; but I do not know if those I meet truly believe women, or Jews, are inferior. In this environment it is easy for informational cascades to take hold. I may not know any Jews; so received opinion may be all I have to make a judgement about them. Similarly, I do not know any FTSE 100 CEOs, so it hard for me to form a view of them based on first-hand experience.

In adopting the collective view, I should be wary of the difference between expressed and held opinions. My Trumpster/Kipper friend may just tell me how "diversity is our strength" to remain in polite society within the Academy. Indeed private truths, about what wives truly think of their husbands, or citizens their Sovereign, have been the staple of British comedy for centuries ([Kuran, 1995](#); [Kuran and Sunstein, 2000](#)).

With such social dissimulation it is clear "we need to talk". But Sunstein goes on to point out talking maybe not be that helpful. If a bunch of Catholics/Jews, etc. get together to discuss shared interests, problems, it is likely that views shared in a modest form by most in the group will shift towards the most extreme form of their shared view. So Catholics, who do not really understand the value of the Reformation, may drift toward believing Protestants are not real Christians at all. Such group polarisation is now typically parodied amongst our students; with jibes about them being triggered by "micro aggressions" of "invading their (safe) space". Sunstein points out that although we want marginalised groups to organise to represent their interests, as women, or blacks, but we may be dismayed by the "enclaves" produced.

Indeed Sunstein will end his book in Chapter 15, with a discussion of "partyism", the trend of society, and perhaps even workplaces, to be balkanised by shared political/social mental frames. Sunstein points out, that while discrimination on the basis of race is mercifully waning to the margins, discrimination by political affiliation/social awareness is rampant. A distinct danger of this is that whole professional groups, academics or investment bankers, could retreat into echo chambers, where calls for enforced recognition of preferred gender pronouns, or scrapping the failed NHS, becomes the localised norm.

Partyism segments society, but even more viciously it divides, and frustrates our governance. As I write it common to hear the British Prime Minister depicted as a tyrant/fascist and the leader of the opposition described as either a simpleton or a Communist. As Sunstein points out many of our immediate social problems, climate change, care of the increasing number of elderly, frail citizens, require consensus and an intense focus on the facts of the case. While much of our Punch and Judy politics is amusing, it is not helping us get stuff done. A more technocratic, less tribal, process of political deliberation may have something to commend it in these vital matters.

Sunstein points out this reminds us of the importance of inter-enclave dialogue, as well as intra-enclave dialogue. Raising this I wonder how much inter-enclave dialogue is happening between academics of different flavours, or academics and practitioners? If not much, can our academic scribbles survive the evolutionary test so that "Practical men believe themselves exempt from any intellectual influence [. . .] are distilling their frenzy from some academic scribbler a few years back".

This reminds us of the importance of Jefferson's belief that "a little rebellion now and then is a good thing" (Sunstein, 2019b, p. 36). So we might salute Jobs's "crazy ones"; who engage in norm entrepreneurship, setting new social standards, or lifestyle choices. In our own midst such a person was James Bogle, who died earlier this year. Bogle essentially invented index funds, using his Vanguard fund to put many active investors to shame.

If such norm entrepreneurs are rare, we might wonder whether the State has some role in directing social norms in eating, drinking and good business practice. Often norms and the law are compliments. If a friend offers me cannabis I can politely refuse, while reminding them humorously "it's illegal you know".

Here the law has an expressive power, saying something important about values we all share. Local bye-laws against littering, or public consumption of alcohol, may serve this purpose. I do not fear arrest for littering my street, but the law makes a clear statement of the norm that I should not.

This expressive function of the law might also be seen to be embedded in insider trading laws and laws on good governance; implemented via the FRC's Corporate Governance Code in its various incarnations. Often the inability to enforce insider trading laws is seen as a fatal flaw in their working. But they may serve an expressive purpose of articulating a social norm that corporate board members should fulfil their fiduciary duties to their shareholders.

From the economic perspective, insider trading laws are odd because they impede the strong form efficiency of financial markets, allowing even the inside information, known by the select few, to enter into the pricing of assets. It is a victimless crime, punished by the State with a misplaced sense of virtue-signalling (Manne, 1985). But in some sense we are all insider traders' victims through a loss of the social norm of market integrity. Similarly, following the financial crisis many asked if CEOs of major financial institutions were "too big to jail" (Garrett, 2014). But perhaps the intended purpose of much bank regulation/legislation was always more expressive than potentially punitive.

2. Nudging

In the second part of the book, Sunstein turns to the nudges we finance folk know and love him best for. These nudge types include default rules, simplification, using social norms, increasing ease and convenience, eliciting implementation intentions, and precommitment strategies.

For Sunstein it is vital we judge the value of any nudge, or change in architecture, "as judged by themselves". So the State may deeply wish I drank 21 units of alcohol a week and flossed twice daily. But it is not their liver or teeth to choose. In short, we must beware of nudging degenerating into stealth bullying. Otherwise we reach the sad fate of Winston in Orwell's 1984, who can finally state "He had won the victory over himself. He loved big brother".

Part of the danger of privileging nudgers over nudgees is that both share a common humanity with its innate flaws (Sunstein, 2019b, p. 93). Somewhere short of this intimidatory prospect lies a whole range of nudges that help us address self-control, such as automatic enrolment in pensions schemes. But Sunstein recognises that the individual is the presumptive controller of their own fate and discusses experimental evidence he has conducted with others which shows that most of us value, and are thus willing to pay for, retaining that control (Bobadilla-Suarez *et al.*, 2017).

Freedom to choose without coercion, or deception, is an integral part of the classical liberal ethic. For Mill, Hayek and so many more the individual knows their own interests best and so can decide. Yet Sunstein points to "tyranny of choice" this can bring. Indeed

many of us have a wardrobe full of white shirts and dark trousers precisely to avoid the “what to wear?” choice each morning.

Sunstein points out that unbidden choice can act as a sort of “mental tax, cognitive to be sure [and] likely to be small [yet it] might well be unwelcome” (Sunstein, 2019b, p. 67). Under this tyranny of choice, the State may need to decide what happens if one refuses to, or cannot, choose.

This is the sort of tragic choice faced by those engaged in palliative care, would I choose to continue living in my current reduced state, even if a treatment option exists to facilitate that? Sunstein explains the dilemma:

If people choose not to choose, or if they would make that choice if asked, it is an insult to their autonomy to force them to choose. And if people like to choose a default option deprives them of their choice. (Sunstein, 2019b, p. 125)

We see these solutions at work regularly in the work of the Behavioural Insights Team (BIT) and more generally in shaping regulatory policy regarding financial products, online abuse (Halpern, 2015; Costa and Halpern, 2019; Katy *et al.*, 2019) and much more. Some may object to the State structuring of citizen’s choice via nudging and choice architecture (Sugden, 2009). But, as Sunstein points out, if the State does not nudge my attitude to eating and smoking, alcohol and tobacco manufacturers certainly will. If tobacco companies lure young men into smoking, by implying it is a manly thing to do, we cannot be outraged by the State pointing out the fact that smokers increase their possibility of impotence. “Nature nudges” as Sunstein states it (Sunstein, 2019b, p. 115), by giving me loving/abusive, sporty/sedentary, parents who form my mind and habits. So the true question is who nudges and how? Not whether we should have our daily choices structured for us and nudged which choice to make.

In a seismic shift in pensions regulation, the UK Government in April 2015 ended the requirement of some 13 million defined-contribution savers to purchase lifetime annuities upon retirement. In a review of these changes in December 2017 the Financial Conduct Authority found amongst other things (FCA, 2017):

- There are weak competitive pressures and low levels of switching – most consumers choose the “path of least resistance”, accepting drawdown from their current pension provider without shopping around.
- One in three consumers who have gone into drawdown recently are unaware of where their money was invested.
- Some providers were “defaulting” consumers into cash, or cash-like assets, but holding cash is highly unlikely to be suited for someone planning to draw down their pension pot over a longer period.

2.1 Developing a philosophical justification for nudging and shoving

Freedom to choose without coercion, or deception, is an integral part of the classical ethic. For Mill, Hayek and so many more, the individual knows their own interest best and so can decide their own fate best. Thus Hayek states:

The awareness of our irremediable ignorance of most of what is known to somebody [who is a chooser] is the chief basis of the argument for liberty”. (Sunstein, 2019b, p. 123)

Thus the classical argument for personal choice comes out of both an awareness of our nobility and fragility. It is the latter which suggests a liberal paternalism might be both an attractive and socially needed adjustment to unalloyed individual liberty.

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We see these solutions at work regularly in the work of the Behavioural Insights Team (BIT) and more generally in shaping regulatory policy regarding financial products, online abuse (Halpern, 2015; Costa and Halpern, 2019; King *et al.*, 2019) and much more. Some may object to the State structuring of citizen’s choice via nudging and choice architecture (Sugden, 2009). But, as Sunstein points out, if the State does not nudge my attitude to eating, smoking, alcohol and tobacco, then manufacturers/advertisers will. So the true question is who nudges and how? Not whether we should have our daily choices structured for us and nudged which choice to make.

In a helpful engagement with his critics, like Robert Sugden, Sunstein devotes Chapter 7 to why nudges fail. One response is just to give up and accept some people are drunks, obese, poor in old age or whatever their un-nudged fate might be. It is not libertarian paternalism, if we cannot cherish individual liberty as a guiding, if not supreme, value. But as Hayek elsewhere stated:

To advocate any—clear of social order is today an almost certain way to incur the stigma of being an impractical doctrinaire. (Hayek, 1948, p. 1)

Professor Sunstein, as his prior record as Administrator of the White House Office of Information and Regulatory Affairs, OIRA, in the recent Obama administration suggests, is nothing is not a practical man. Sunstein (2013) describes that key period of his life, which informs much of the discussion in the present book. Sunstein is a consequentialist, if not quite a utilitarian, judging the desirability of a social intervention by its consequences, rather than clear principles. Later Sunstein reflects on the relationship between moral laws and consequentialist reasoning, in one of the most fascinating parts of the book I felt.

For Sunstein nudging is an evidence-based pragmatic art, full of unintended consequences and measures that should in all reason work, but just do not. So a good nudge is a nudge which matches the “behavioural scissors” (Simon, 1990) of cognition and context, reflecting an ecological rationality of local, rather than universal, application.

Part of the reason why the classical liberal preference for supporting individual choice is incomplete is that within each of us lies more than one decision maker. As Thaler and Shefrin (1981) made clear our mind is inhabited by both a “planner” and a “doer”. Whose will gets executed depends on the internal battle for self-command, which no amount of respect for personal autonomy can resolve. After all, which person is choosing? The planner or doer is not yet clear.

Furthermore, the means of preference elicitation seems to impact the choice made. So I may merrily refuse all black/female candidates for a job on the basis that “they are not right for us”. But when I must choose between a highly qualified black/female candidate and less qualified white male one the source of my prejudice might become obvious to others; and perhaps even for the first time to myself. So isolated and joint decisions can produce differing decisions, as Sunstein makes clear in Chapter 11 of his book. It is not clear which method of preference elicitation consistently produces better results, from the Chooser’s standpoint. Decisions made in isolation, give us no idea of content, so pharmaceutical startups are risky, but are they more/less risky than mining, for example.

Certainly joint evaluations are almost designed to induce manipulation, focusing on a car's ability to cruise at 85 mph in a town where reaching 40 mph is mostly a dream. While standard finance has encouraged investors to focus on systematic risk the financial crash of 2008 reminds us that an accumulation of total risk, systemic and diversifiable, can be threatening to investors too. The financial system cannot insure itself, leaving the put option to the taxpayer. Because the financial system is not a closed one, it must be insured by the public, which manifested itself in a form of grotesque "socialism for the rich"; as bank after bank was rescued at the public expense in 2008.

3. Excursions in how philosophy and morality shape the law

In the final part of the book, Sunstein looks at some of the issues that have pre-occupied him because his nudging expertise led him to be asked to join the Obama Administration. With that vantage point he gives some advice on what sort of information should be revealed to the public by government.

Sunstein distinguishes between output disclosures, of the top ten polluters in each state, companies with the most work-based fatalities, etc. and input disclosures, of how policies were agreed, who said what to who, who threatened to resign, told who else they are a moron/clown/charlatan, etc.

Not surprisingly the anger the financial crisis produced put pressure on politicians to be more transparent and Sunstein studies some of the consequences of this. One central legal doctrine driving the response to reforming the banks is the "precautionary principle". This legal doctrine is then applied to major threats to social well-being and suggests the:

Precautionary measures [to prevent the harm envisaged] should be taken even if some cause and effect relationships are not established scientifically. In this context the proponent of the activity, rather than the public, should bear the burden of proof. (Sunstein, 2019b, p. 203)

So if my second-floor flat is drowning in water from my ceiling I do not have to prove anything to get the inhabitant of third floor flat, above, to switch off their water. It is this very principle which underlies much of the thrust towards green renewal, Extinction Rebellion, etc. Are we really going to wait until our kids are gasping for breath before we act on carbon emissions?

The scientific consensus that global warming is man-made is strong; but not utterly overwhelming. But we choose to act now out of an excess of caution (perhaps). The problem with this approach is that, with respect to global warming, it rather assumes Nature is benevolent and bountiful for Mankind, perhaps that it even was created for us. But much of nature seems almost targeted against our interest, the ice age, the oncoming asteroid strike.

We cannot assume natural processes are desirable from the perspective of humanity. Who would seriously decry the triumphs over nature, of indoor plumbing, penicillin and many other advances in our modern life? Equally interventions in modern life are full of unintended consequences. Thalidomide, intended to cure morning sickness in mothers, created horrendous abnormalities in users' children, for example.

So while the natural order cannot be assumed to be benevolent to humanity its disruption cannot be either. Hence the precautionary principle's advice, to beware changes to the prevailing order, is rendered incoherent in practice. This reminds of much of the discussion in the Turner Review of the oversight of the Financial Services Authority, as was, in the run up to the 2007/8 financial collapse (Turner, 2009).

The FSA had assumed that the market was its own best healer, with bad financial practice simply leading to a loss of clients, making sharp practice self-limiting. In the wake

of the crisis, regulatory authority has been enhanced. But this ignores the degree to which the State creates the financial crises it is called upon to solve (Roberts, 2010). Thus the precautionary principle lacks coherence in Sunstein's view. This is because it ignores the fact both the observed, prevailing, order can be dysfunctional, as can equally any correction to constrain its inherent dangers.

The "dictum do no evil" does not tell me what to do, if anything at all. A central idea here is that of resilience in any naturally "grown", as opposed to made, social order, as outlined by Hayek (1973). An evolved/grown social order, like our British unwritten constitution, contains its own stabilisers. Thus the nausea I feel after drinking too much is my body asserting its own control upon being poisoned. And financial markets contain such automatic stabilisers which State intervention can only serve to dull. Thus we might ask what was the real mistake, letting Lehman's fail 2008, or under-writing the bail out of Bear Stearns, by J.P. Morgan, earlier that year?

In Chapter 14 of the book, Sunstein turns away from what the law can/does do to what is right/virtues to do. Sunstein discusses moral heuristics stating:

Heuristics play a pervasive role in moral, political and legal judgements and that they sometimes produce significant mistakes. (Sunstein, 2019b, p. 2015).

This is because simple rules work so well in most contexts. A rule like "do unto others as you would have them do for you" may work badly in a particular context, when working with an incorrigible swindler, for example. A heuristic tool in an investor's/regulators "adaptive toolbox" must be finely tuned to the context into which it was deployed.

Thus the "cheap money" policy of the Fed/ECB, which seemed so wise in early 2000, or late 2008, looked more hazardous, of not downright reckless by early 2007, or perhaps even today. Crucially Sunstein advances an idea that in the same way as Gigerenzer and Todd (1999) advance "simple rules that make us smart" we might also surmise a rulebook, set of commandments, for "simple rules that make us good" (Sunstein, 2019b, p. 224).

I gladly leave discussion of these rules to my moral superiors. But it is illuminating for finance scholars to consider one heuristic that Sunstein discusses. This is the "outrage heuristic", first discussed by Kahneman and Frederick (2002). This is the notion that in deciding on how to respond to an action we are guided not so much by its consequences as the moral offense/outrage it causes. This may account for what some see as a self-defeating antagonism against the huge rewards paid to senior executives, especially in banks (Gaibaix and Landier, 2008). Bebchuk and Fried (2004) document a clear role for "outrage" in constraining managerial pay. But we might wonder whether this outrage reflects the deployment of an outrage heuristic, embedding its own predictable bias?

Towards the end of his book, in Chapter 15, Sunstein turns to the central issue of what a good/right set of morals is or where such a rulebook might come from? Obviously, this is a very personal choice and Sunstein avoids preaching in this regard. But he does draw a useful distinction between two types of moral reasoning. These are:

- (1) deontological/rules based, and
- (2) consequentialist moral reasoning. Sunstein identifies himself clearly with the latter path of moral reasoning, consistent with being author of a forthcoming book on cost-benefit analysis (Sunstein, 2019c) and a former policy advisor.

Although not arguing for the superiority of consequentialist reasoning, Sunstein points out its association with reflective, calculative, system 2 (Kahneman, 2011), patterns of thought, as opposed to the "hot cognition" of system 1 thought. While many of the most vile, debased, monsters of history, Hitler, Pol Pot, have been very calculated in their actions, we would

generally hope sustained, reasoned thought would improve the quality of our choices; including those requiring moral fibre. Over many years Gerd Gigerenzer and the “fast and frugal reasoning” school of scholarship emphasises the potential superiority of my gut-feeling that cannibalism, torture or incest, are “just–wrong”(Gigerenzer, 2007).

Yet interestingly Sunstein points out that when we have time to think, and are prodded to do so, we seem more likely to exercise consequentialist moral judgements. This suggests default, system 1, reflex, patterns of moral reasoning may embed predictable problems. Thus Sunstein argues deontological/rules-based reasoning should:

Be seen as a heuristic. consistent with a growing body of behavioral and neuroscientific research, which generally finds that deontological judgements are rooted in automatic, emotional processing. Deontology may be a moral heuristic, in the sense that it may be a mental short-cut for the right moral analysis. (Sunstein, 2019b, p. 244)

It is thus clear we should want company management, regulators, to have the time and space to engage in a deliberative, calculative, system 2 thought process in making important decisions with moral consequences, say redundancies, or health and safety policy. But it is equally clear we cannot guarantee that this will ensure they will make more moral decisions.

4. Overview: how change happens from a classical and ecological rationality perspective

Sunstein’s book is an important contribution from a central figure in the implementation of behavioural insights into financial and economic policy. The importance of this work is assured, but I felt less sure about how it will be interpreted. In many respects, I wondered if the book reflected a belief that deploying heuristics induces a bias that makes the decisions made unwise, or damaging, to the chooser. Thus gut feeling, system 1, thought was largely presumed to be inferior. In discussing moral heuristics, Sunstein is exceptionally clear that system 1/heuristic-driven thought cannot be assumed to be inferior. Sunstein simply notes that when given time to reflect we often choose a more calculative, system 2 pattern of moral choice. But elsewhere, in considering ordinary purchases, health-related decisions, the presumably heuristic-driven, system 1 choice is presumed by Sunstein to be an imperfect choice. I wonder if this underplayed the ability of an adaptive toolbox of, financial, decision-making to effectively guide social and economic choices. This would not undermine much of Sunstein’s call to make financial, and other, decisions, more transparent because “most of us can use a little help” (Sunstein, 2013, p. 9). But the choice presumed to be best for us; towards which we are nudged, should not just be one shown to “optimal” in a psychological lab. Rather it should be one shown to have been adopted successfully by a large group of comparable choosers. In short, the default choice should be known to exhibit both ecological as well as the classical, rationality of our standard decision-making textbooks.

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