



Economics in Context

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Designed for use with the Global Development And Environment Institute's *In Context* textbooks

The Use of Behavioral Economics to Increase Government Revenue

One important lesson from behavioral economics is that the way issues are framed to people can have a significant influence on their decisions. Over the last few years government officials have begun to use insights from behavioral economics to increase public revenues.

Since 2013, the Behavioral Insights Unit in Australia has been designing experiments to test the effectiveness of various government proposals. For example, one experiment sought to increase the payment of delinquent taxes. Proposed changes to the payment notices included telling taxpayers that “more than eight out of 10 people pay their land tax on time, making you one of a small minority who has required us to take further action.” Other changes included making the color of the text red and changing the words “amount owed” to “you owe.”

In each experiment, one group of people gets the proposed change, while another group (called the control group) continues with the current approach. Then government officials can empirically test whether the change had any significant effect. The Behavioral Insights Unit has already been credited with positive impacts such as raising an extra \$10 million from drivers' fines and saving \$11 million in public health expenditures.

A similar group was created in the United Kingdom in 2010. Known as the Nudge unit, after the 2008 book of the same name, it has developed methods to increase organ donations, encourage people to give to charity, increase the portion of people who pay their taxes on time, and increase the payment of court fines.

David Halpern, director of the

Nudge unit, sees the use of behavioral economics by government as a “potential game changer.”

“If we keep doing this and get lots of incremental improvements - a few per cent here and a few per cent there - you can transform the delivery of services,” he said. “The efficiency gains just waiting there are absolutely enormous.”

Harvard professor and leading behavioral economist David Laibson agrees that numerous practical applications of nudges remain to be discovered.

“What we need now are armies of people who are trained in taking this knowledge and spreading it out to other areas of human behavior,” he says. “There’s a limitless set of ways we can tweak things and get small efficiency improvements each time.”

Sources:

Wade, Matt. 2014. “Politics of Pushing: Behavioural Economics a Revenue Game-Changer,” *Sydney Morning Herald* (Australia), June 7, 2014

Wright, Oliver. 2014. “How the Government's Successful Behaviour Insights Team has had a Profound Effect on Whitehall,” *The Independent*, February 9, 2014.

Note: This update specifically relates to *Microeconomics in Context* Chapter 7 and *Principles of Economics in Context* Chapter 8.

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