

2021
~~2020~~ Yuji Ijiri Lecture

Principles, Rules, and Norms

The Principles vs. Rules Debate: A Primary Dimension

Degree of reliance on individual judgement

More judgement \Rightarrow more relevant

Less judgement \Rightarrow more reliable

The Principles vs. Rules Debate: Another Dimension

Nature of enforcement mechanism

Institutions – contracts, litigation, regulatory

Norms – cultural, social, conscience

Some Working Definitions

Principles vs. Rules

A spectrum – pure principle to pure rule.

Pure principle: articulates the objective that should determine acceptable behavior.

Pure rule: clear guidance (i.e., necessary and sufficient conditions) for acceptable behavior.

Principles vs. Rules: An Example

Principle: Don't drive too fast.

Rule:



Norms

“[W]hat is it which prompts the generous, upon all occasions, and the mean upon many, to sacrifice their own interests to the greater interests of others It is reason, principle, conscience, the inhabitant of the breast, the man within, the great judge and arbiter of our conduct.” [Adam Smith]

When in Rome, live as the Romans do; when elsewhere, live as they live elsewhere. [St. Ambrose]

Norms

Informal mechanisms that enforce notions of acceptable behavior.

Enforcement Mechanism:

feelings of guilt – internal

wired to fit in – internal

social judgement/punishment – external

Norms, to some extent, established by behaviors taken, which in turn, are a function of the norms.

Principles

Attributes

more reliance on judgement
greater reliance on norms

Why greater reliance on norms?

less objective & verifiable
=> institutional mechanisms harder
to implement

Rules

Attributes

less reliance on judgement

greater reliance on institutions

Why greater reliance on institutions?

objectivity & verifiability

undermines norm for principled behavior

Rules Undermine Norms

Employing rules (may) undermine norms for the principle.

Why?

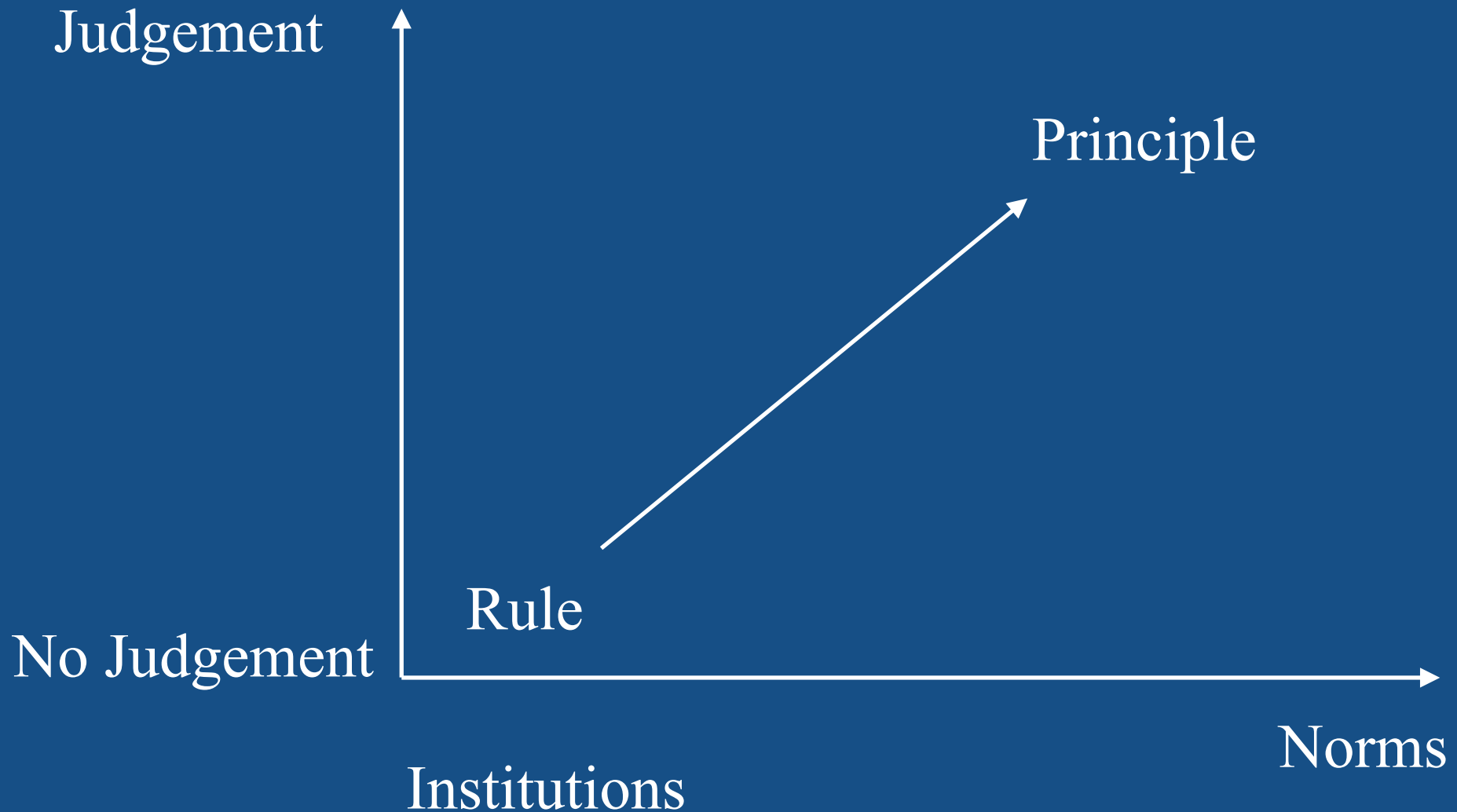
Rules reframe the decision

induce ethical fading

eliminate intrinsic motivations

alter what is socially acceptable

Principles vs. Rules: Two Dimensions of Choice



The Research Question

How does the nature of the enforcement mechanisms influence the relative impacts of principles and rules?

A Little Bit of Modeling

Will use a really simple illustrative model

Illustrative model contrasts extremes

Pure principle that is enforced solely by norms

Pure rule that is enforced solely by institutions

Observations should (hopefully) apply to settings where more principles based systems rely to a greater extent on norms than more rules based systems rely to a greater extent on institutions.

Rules are not the Principle

A rule should support an underlying principle.

Rules, however, are rarely perfectly congruent with the underlying principle.

Sometimes by design – adherence to rule forces a violation of the principle

Sometimes by choice – one can satisfy the rule in a manner that violates the principle

Incongruence is one consequence of employing a rule.

A Little Bit of Modeling

Continuum of individuals indexed over $[0,1]$.

Individuals choose one of two actions, one that aligns with some principle, $a = 1$, and one that fails to align with that principle, $a = 0$.

An individual i 's payoff is $\int_0^1 a_t dt + bi(1 - a) - C(a)$

where

$\int_0^1 a_t dt$ is proportion of individuals who are expected to choose $a = 1$

$bi(1 - a)$ is benefit i gets from choosing $a = 0$, $b \in (0,1)$.

$C(a)$ is cost of action taken, $C(1) = 0$ and $C(0) \geq 0$.

A Little Bit of Modeling

Behaving in a principled manner generates a public good.

Individuals with higher i get a greater benefit from being unprincipled.

All individuals would prefer to commit to being principled because $b < 1$.

Informal (norm) and formal (regulatory) mechanisms provide incentives for behaving in a principled manner by imposing costs for being unprincipled, $C(0) > 0$.

Standard is a Principle

Scenario 1: Standard is a pure principle.

Only the norm influences behavior

$$C(0) = c + s \int_0^1 a_t dt$$

where $s \in (0, b)$ and $c \in (0, b - s)$

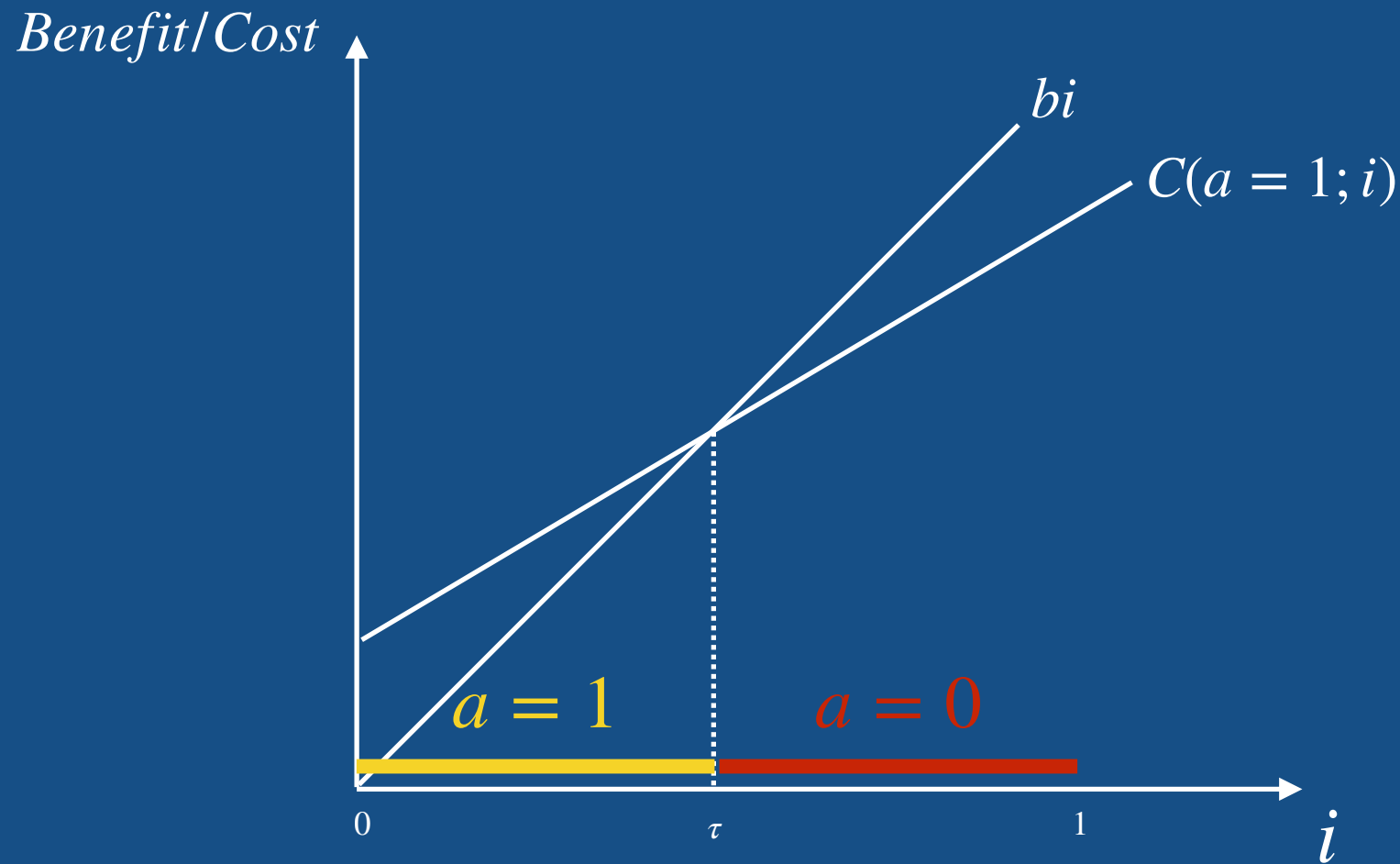
Norm is endogenous. The cost of behaving in an unprincipled manner is increasing in the proportion of individuals who behave in a principled manner.

c can be thought of as personal conscience

s can be thought of as social influence of principled behavior

Standard is a Principle

Scenario 1: Equilibrium is characterized by a threshold i, τ



$$\tau = \frac{c}{b - s}$$

Standard is a Principle

Proportion of individuals who take the principled action, $\tau = \frac{c}{b-s}$, is decreasing in b , is increasing in c , and is increasing in s .

Intuition:

greater benefit from unprincipled action \Rightarrow more of it

greater cost for unprincipled action \Rightarrow less of it

greater social influence of principled behavior increases cost of unprincipled behavior \Rightarrow less of it

Standard is a Rule

Scenario 2: Standard is a pure rule.

With probability q individual can satisfy the rule even if they choose $a = 0$.

If individual can only satisfy rule if $a = 1$ then $C(0) = \lambda$, where $\lambda > 0$.

If individual can satisfy rule with $a = 0$, then $C(0) = 0$.

Standard is a Rule

Key features of Scenario 2

$\lambda > 0$ reflects the cost of deviating from the rule under the formal mechanism (e.g., litigation)

q captures degree of congruency with the rule – higher q implies lower degree of congruency.

Standard is a Rule

Scenario 2 Equilibrium

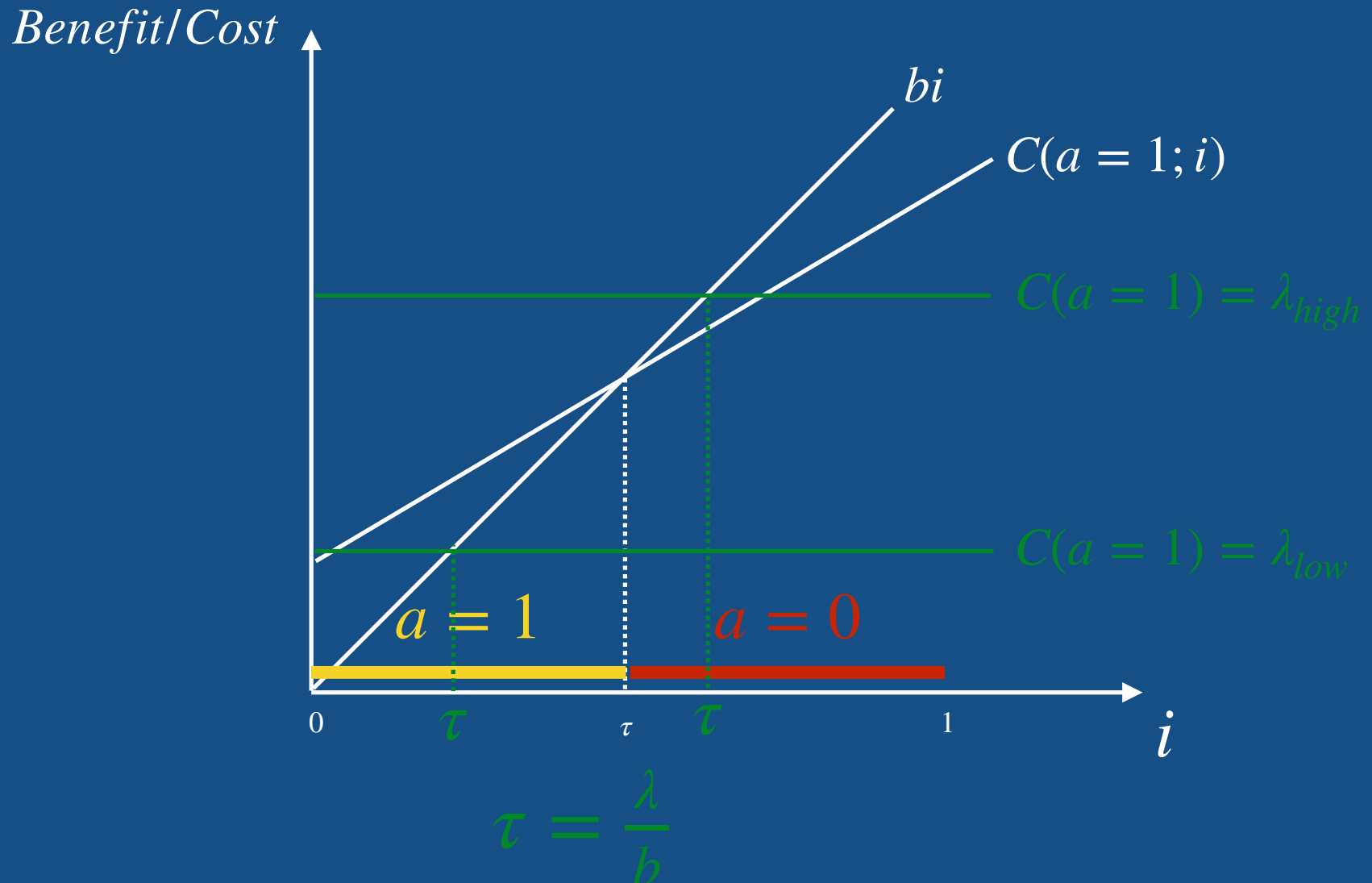
Those who can satisfy the rule and still choose the unprincipled action, $a = 0$, choose $a = 0$.

The behavior of those who can satisfy the rule only if they adhere to the rule is again characterized by the threshold.

That threshold exceeds the Scenario 1 threshold if and only if the formal mechanism cost, λ , dominates the informal mechanism cost, $C(1) = c + s \int_0^1 a_t dt$.

Standard is a Rule

Scenario 2: Threshold i, τ , for individuals who can satisfy the rule only by choosing $a = 1$.



Standard is the Rule

Proportion of individuals who take the principled action increasing in λ and decreasing in q .

Intuition:

greater rule violation cost \Rightarrow less unprincipled action

rule incongruent with principle \Rightarrow more unprincipled action

Principle vs Rule

If the objective is to maximize principled behavior, then principle dominates a rule if the norm is more effective at promoting principled behavior:

norm is strong – c is large

rule is weak – λ is small – or rule is not congruent – q is high

Principles will be employed in entities, organizations, countries, in which norms are strong. When norms are weak, then we might see rules.

Principle vs Rule

If the objective is to maximize principled behavior, then principle dominates a rule if the benefit, b , is not too large:

Why? Small benefits of unprincipled behavior make the norm stronger due to social influence of principled behavior.

Principles will be employed in entities, organizations, countries, in which the benefits of unprincipled behavior are not too large.

Suggestive of cyclical behaviors if benefits move cyclically.

Some Extensions

What choice maximizes ex ante welfare (i.e., representative individual welfare before their index/type is knowns)?

What choice will prevail when the choice is determined via a vote of the individuals?

How do norms evolve and how might that influence the principle vs. rules choice over time?

If benefits/costs/population attributes are unknown but learned by experience/observation, how does that influence the principle vs. rules choice over time?

Summary

Two dimensions to principles vs rules debate:

Judgement/discretion

Nature of enforcement

Principles-based standards => norms

Rules-based standards => institutions

Principles-based standards dominate when:

norms are relatively strong

institutions relatively weak

rules are incongruent