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A Model of a Rule of Law and a Rule of Man

Implications for the Design of Institutions

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Abstract

Findings of cross-cultural psychology suggest that different approaches to rule enforcement have cultural roots. Individualist societies have established a rule of law, in which rules prevail; collectivist societies have a rule of man, which allows discretionary rule enforcement, which, in turn, is recognized as an obstacle to sustained increases in productive long-term investment in developing countries. This paper presents a model that offers a unified framework to explain rule enforcement as social optimization processes in both individualist and collectivist societies and, on this basis, highlights the essential differences between a rule of law and a rule man (i.e., between rules and discretion). The paper uses this framework to show that cross-country variations in rule enforcement are explained to a considerable extent by cultural values. The paper then uses the framework to show how the *imported* multi-stage rule enforcement institutions based on separation of powers in vertically-oriented collectivist societies, unlike in the individualist societies from which they originate, might not ensure as low a degree of discretion as intended. Finally, the paper uses these results to explore practical ideas that would help collectivist societies benefit from rule enforcement with low discretion.

Keywords: rule of law, rule of man, collectivism, discretion, enforcement, individualism, institutions, rules

JEL classification: K00, O17

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1 Introduction

One of the under-researched topics in economics, particularly in its analysis of institutions and institutional change, is how collectivism and individualism—two different systems of values—affect institutions.[1] These two systems of values are different. The following two passages by Rawls and the government of Singapore describe well the essence of the differences:

> Each member of society is thought to have an inviolability founded on justice … which even the welfare of every one else cannot override. … Justice denies that the loss of freedom for some is made right by a greater good shared by others (Rawls 1999: 24-5).

> Nations before [ethnic] community and society above self … Consensus instead of contention … (Government of Singapore, quoted in Huntington 1996: 319).

Collectivism here refers to cultural values, not a political ideology. A society may be driven by collectivist values, without collectivizing production. Among a variety of different behavioural implications of these sets of values are those for inter-group relations and use of rules. Research by Hofstede (1997) and other cross-cultural and social psychologists suggests that collectivist societies tend to experience (i) strong inter-group rivalry (or factionalism) and (ii) a high degree of discretion in rule enforcement, much more so than in individualist societies.

Their studies note that collectivist societies have developed a rule of man; individualist societies, a rule of law.[2] The two value systems have different ideals for governance:

> It is in vain to say that enlightened statesmen will be able to adjust these clashing interests, and render them all subservient to the public goods. Enlightened statesmen will not always be at the helm (Hamilton 1787).

> Confucianism traced back the ordering of a national life to the regulation of the family life and the regulation of the family life to the cultivation of the personal life (Lin Yutang 1938: 21).

The former stresses the importance of rules, the latter highlights the importance of enlightened leaders.

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1 Different behavioural implications of individualist and collectivist cultural values are well established in cross-cultural and social psychology. Their implications, however, are not widely analysed or discussed in economists' research. Neoclassical economics, in general, assumes that human beings are rational individualists. Hayek (1948) has provided an analysis of the implications of individualism for market economic order and efficiency, but not a comparative analysis of individualism, on the one hand, and collectivism, on the other, the latter as it exists in the non-western civilizations in conjunction with a formal market order. New institutional economists have criticized neoclassical economics for its inadequate usefulness as tools to analyse long-term changes in the developing world (e.g., North 1994). Greif (1994) is among a handful of economists who have explicitly compared the implications of these two cultural values for the manner in which societies organize their institutions.

2 See, for example, Hofstede (1997), and Berry *et al.* (1992).

Both of these consequences of cultural collectivism—inter-group conflicts and discretionary rule enforcement—can have significant negative effects on how a society develops sound institutions.[3] In their interactions, rival groups in a collectivist society, by trying to promote their factional interests, end up undermining society's chances to promote encompassing interests, thus harming their own interests. This is a standard result for games of prisoners' dilemma (PD). Many economic and political reforms have elements of PD games. Rival groups in a collectivist society, by choosing—to promote their own interests—*defection* rather than *cooperation*, damage their collective interests and thus their own interests. While both individualist and collectivist individuals and groups face PD games, collectivist values can intensify inter-group conflicts (see Chu 2004).

Cross-cultural psychologists point out that culturally collectivist societies tend to be hierarchical (i.e., have a large power distance, or are authoritarian), in which leaders and other rule enforcers with paternalist ideals tend to use a high degree of discretion in interpreting and enforcing rules. This often leads to unintended consequences by reducing the predictability and transparency of rules. Rules in this context are formal rules as analysed in new institutional economics, which defines institutions as rules of the game and as comprising both formal and informal rules.

More recent research in social psychology has suggested that the power distance dimension is independent of the individualism-collectivism dimension. Therefore, both individualist and collectivist societies may have various degrees of horizontal and vertical orientation, thus having different degrees of power distance.

While cross-cultural psychologists' results, based on observations, surveys and statistical analysis, are insightful, they do not offer formal models, which can enrich the understanding and discussion of the analytical results. This paper (i) presents a formal framework to analyse rule enforcement and highlight how rules and discretion arise, (ii) uses cross-country statistical data and the analytical framework to test the differences between rules-based and discretion-based enforcement, and (iii) reviews some practical experiments aimed at reducing the degree of discretion in rule enforcement in the context of the analytical framework.

Rules in this paper, as in new institutional economics, comprise both formal rules (e.g., laws, policies, and regulations) and informal rules (e.g., customs, conventions and norms). They are not merely laws. Therefore, rules in this paper are broader than laws, and rule-making agencies are broader than the legislative branch.

2 Vertical and horizontal individualism and collectivism

Cross-cultural psychologists highlight behavioural implications of a number of dimensions of culture.[4] As noted, individualist and collectivist cultures engender different values and behavioural norms in some respects. Individualist societies value

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3 The ideas in this note, in part, are based on the results reported in Chu (2003).

4 See Chu (2004, 2003) for further details.

the interest of the individual, compared with that of the group, while collectivist societies value the interest of the group, compared with that of the individual. Individualism is widespread in countries of western civilization; collectivism in many of the rest. While individualism-collectivism is a matter of degree, that it is an obvious distinction is firmly established in psychology. For example, Feldman (2001: 475) states:

> Are you often influenced by the moods of your neighbours? Do you think people should take their parents' advice in determining their career plans? ... If you answer yes to questions such as these, you may hold a view of the world that is dissimilar from that of most people in the dominant North American culture …

A large/small power distance, another cultural dimension, makes formal and informal institutions more/less hierarchical. In this regard, research in cross-cultural and social psychology offers two strands of results:

a) Hofstede (1997) has noted that a collectivist society tends to be vertically oriented and have a large power distance—a tendency for members of a society to accept inequality—whereas an individualist society tends to be horizontally oriented and have a small power distance, but noting that there are exceptions. Hofstede's research suggests that, some among western countries, particularly France and Belgium, while individualist, are characterized by a relatively large power distance, while most other individualist countries have a relatively small power distance. Collectivist countries tend to be characterized by a large power distance.

b) Recently, however, researchers note that different societies can have four different value orientations: horizontal and vertical individualism (H-I and V-I) and horizontal and vertical collectivism (H-C and I-C).[5] The results of these recent studies point to the possibility for some of individualist and collectivist societies to be vertically and horizontally oriented. Vertical orientation, more so than horizontal orientation, tends to tolerate unequal outcomes in the distribution of power and income. In individualist societies, vertical orientation manifests itself by having people accept unequal outcomes, for example, in income distribution, as in the US, if they result from, for example, market rules. In contrast, northern European countries tend to tolerate less of these outcomes and use redistributive government policies to promote a greater degree of equity. In collectivist societies, vertical orientation manifests itself by having groups tolerate domination by authoritarian leaders. While leaders receive more rewards than the rest in a group, they are responsible for safeguarding the welfare of those they lead. In contrast, some groups (e.g., a small community) in a collectivist society do not have any hierarchy, and their members interact as equals.

In a world of societies characterized by these four value orientations, the individualism-collectivism distinction determines whether a society has a rule of law (rules) or a rule of man (discretion), but rule enforcement may also be horizontal or vertical, depending

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5 For example, Gannon (2001); Nelson and Shavitt (2002).

on the extent to which the authorities or rule enforcers are more or less equally or unequally distributed.[6]

Are the systems of rules and discretion really different? A certain degree of discretion is an inevitable phenomenon that accompanies rule enforcement in any society. That different societies enforce rules differently, however, is quite obvious from casual observations. As shown later in this paper, that the wide range of degrees of discretion is related to societies' values is statistically supported. The following examples of what discretion means in practice are drawn and synthesized from a number of episodes in collectivist societies, with some modifications, but without altering the essential facts:

a) A prime minister breaks law to pursue the administration's campaign promise and claims that the action was aimed at 'promoting national interests'.

b) After indicting politicians for accepting illegal campaign contributions from large corporations, prosecutors decide not to indict corporation chiefs who made illegal contributions because, in their view, prosecuting a large number of business executives would harm the national economy.

c) Shortly after prosecutors have indicted and jailed senior officers in a campaign for receiving a large amount of illegal campaign contributions, a defeated candidate in a parliamentary election issues an apology to the voters on behalf of the campaign and suggests that as head of the campaign, s/he, not the subordinates, should be indicted and jailed. To this assertion, the prosecutors respond by saying that they have no evidence that implicates the candidate in soliciting illegal contributions.

d) A finance minister violates existing rules and decides to grant tax exemptions to selected corporations 'to promote exports'.

e) Faced with scattered evidence of many companies' significant under-reporting of taxable incomes in a region, tax administration officials decide not to press for audits of the companies in the region because the region's economy is down.

f) Local police do not stop cars for breaking traffic regulations by crossing a red light because there are so many of them.

3 A model of rule enforcement

A high degree of discretion in rule enforcement can have significant negative implications for productive economic activities and, therefore, for economic growth. Research has shown that, for allocative efficiency and sustained growth, rules should not only be efficient, but also be enforced with minimal discretion. Discretionary rule enforcement would obviously make efficient rules inefficient and unpredictable. This gives rise to two questions: (i) How can one contrast the differences between *discretion*

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6 Why have individualist societies developed a rule of law and collectivist societies a rule of man is an interesting question. This paper, however, does not address this question.

and *rules* in rule enforcement analytically and test the differences empirically across countries? (ii) If discretionary rule enforcement is an inevitable result of collectivist values, and if discretion is an obstacle to achieving allocative efficiency and growth, how does a collectivist society move toward *nondiscretionary rule enforcement*? What are key elements of a rule enforcement system that would have small chances for discretion?

This section presents a model that explains how a society enforces rules and how it reflects values in rule enforcement processes. The model can highlight how individualist and collectivist values shape rule enforcement processes and how vertical and horizontal orientations affect rule enforcement outcomes. The paper uses the model to show the essential differences between *rules* and *discretion* and uses cross-country data on values and rules to test the hypothesis that values are indeed associated with rules.

In line with Hofstede's original findings, this paper bases its empirical analysis on the premise that collectivist societies tend to be vertically oriented. The theoretical model presented in the paper, however, is general and flexible enough to show, in a unified framework, how collectivist and individualist values and horizontal and vertical orientations shape rule enforcement outcomes. This feature of the model is useful to highlight how vertically oriented collectivist values are particularly responsible for a high degree of discretion and what institutional features would be needed to reduce discretion.

3.1 Rules versus discretion

An analytical approach to highlighting the differences between rules and discretion may proceed along the following lines:

A rule and the outcome of its enforcement

Let the outcome of a formal rule, as it is enforced in a society, be represented by Equation (1).[7]

$$y^{o}_{it} = a + bx_{it} + e_{it} \qquad (1)$$

In Equation (1), the rule determines the relationship between y_{it} and x_{it} for individual i (i = 1,2, 3, …, I)—the ith member of a group of agents who are required to observe the

7 Rules versus discretion may be relevant for how society enforces informal rules, but is more relevant for enforcement of formal rules. The model here, therefore, assumes that rules are formal rules. The 'rules versus discretion' question discussed in this paper refers to different approaches to enforcing a rule for different individuals and is, in some respects, different from and, in some other respects, similar to the 'rules versus discretion' question in macroeconomic policy. The question in the context of macroeconomic policy concerns implications for macroeconomic aggregates, such as aggregate income and overall price. The question in this paper concerns implications for efficiency and equity for different individuals or organizations. The two questions share some similarities, however. For example, a predictable countercyclical policy rule may not be effective. Similarly, certain rules and a predictable discretionary enforcement of rules may engender agents' effort to evade the rules' negative impact on them. This is, however, the maximum extent of similarity between the two.

rule—and for time t, but the relationship holds exactly only in a special case where $e_{it} = 0$, in which case the rule is enforced exactly.[8]

In this context, the value of y_{it}, say, $y^*_{it} = a + bx_{it}$, defined by the rule may be considered to be an optimal value of y_{it} on some grounds (e.g., on efficiency and/or fairness grounds) arrived at via a social optimization process, independent of who is in charge of rule enforcement. Significant deviations from this rule imply inefficiency and/or inequity in some sense. Focusing on the enforcement aspect of rules, this paper addresses neither why they are optimal, nor how the society makes rules;[9] it addresses only how the society enforces formal rules that have been established.

Equation (1) may have a number of practical interpretations:[10]

a) With a binary dependent variable (i.e., 1 or 0), embedded into, say, an appropriate probit function, it may represent how a highway police officer enforces a speed limit (e.g., to stop or not to stop a speeding car?); in this case, i represents the ith of the cars that come into a police officer's view on a highway. Or it may represent how a public prosecutor's office enforces a campaign financing law; it has to determine whether the seriousness of a violation warrants an indictment.

b) With a = 0 and b = a positive fraction of 1, it may be a flat-rate corporate income tax rule,[11] where i represents the ith taxpayer.

c) It may also be a sentencing rule that relates the seriousness of a crime to the duration of imprisonment. In this case, i represents the ith defendant being sentenced for a crime.

In general, in all societies, including individualist ones, for a variety of reasons, the outcome of rule enforcement differs through time and among the agents required to

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8 Note that the rule may include special treatment of different individuals for special circumstances. For example, an individual income tax law may include a provision that exempts poor families and those living in an area hit by a natural disaster from filing their tax returns. It may also include rules aimed at dealing with a variety of well-identifiable contingencies that are not predictable for specific taxpayers.

9 To a large extent, the whole body of literature concerning economic policy, including macroeconomic and microeconomic policy, optimal taxation, public expenditure policy, addresses this question.

10 Note that not all discretionary deviations of the outcome from a *de jure* rule is symmetric. For example, speed limits as enforced by a police officer in a discretionary manner will only exceed the legal limit (e.g., 90km/hr). In this case, u_{it} and e_{it} will only be positive, and will have nonzero means. On the contrary, tax payments under discretionary tax administration cannot normally exceed *de jure* tax obligations, unless the enforcer is truly an arbitrary despot. In some other cases, however, deviations may be either positive or negative. For example, a sentencing rule may define a norm around which a positive or a negative deviation may be allowed, although the rule may stipulate a ceiling. Even a ceiling rule (e.g., a speed limit) may intend to allow a certain deviation in practice. For example, a *de facto* limit (designated for enforcement purpose) of a *de jure* speed limit of 90 km/hr may be 100 km/hr, around which police officers are allowed to exercise some discretion. In this case, u_{it} and e_{it} may be either positive or negative, although their mean still may not be zero.

11 x_{it} would be the taxable income of the ith corporation.

observe it. Rule enforcers in a collectivist society are particularly discretionary. Possible reasons for discretion include the following:[12]

a) Fundamentally, values in a collectivist society tend to attach importance to ruler's (or enforcer's) judgement in comparison to the rules. Particularly in a collectivist society with vertical orientation, rule enforcers, who have authority, also tend to be authoritarian. A collectivist society does not necessarily view rulers' discretion as negatively as an individualist one does. The society tends to tolerate enforcers' discretion and accept or even demand enlightened enforcers' discretion.

b) There are a number of possible other overlapping reasons for discretion. Each of the following cases will give rise to discretion in both collectivist and individualist societies, but more so in collectivist societies, where a rule of man prevails, than in individualist societies, where a rule of law prevails.

   i) Enforcing rules requires enforcement costs. It is in general not possible to catch all speeding cars, tax evaders, regulation violators, or other lawbreakers. A tax administration office does not have the resources to audit all the tax returns. Under a rule of law, however, greater efforts and resources will be spent on enforcing rules faithfully than under a rule of man. Many formal rules (e.g., constitutions, tax laws, election laws, etc.) in the culturally collectivist developing world have been 'imported' from the developed world.[13] These imported formal rules may not always be securely nested in the informal norms in the developing world. This discrepancy between formal rules and informal norms tends to engender high enforcement costs and discretion.[14]

   ii) Enforcer's principles may not be in line with the existing rule. The enforcer may not personally endorse the intentions of a rule. A country's president may not endorse a certain provision of an election law enacted by the legislature that may be dominated by an opposition party. It may have been enacted during the term of his or her predecessor or, as often is the case, may have been 'imported' from another country. Changing the provision of the law, keeping it and not enforcing it, and enforcing it in a discretionary manner have different political benefits and costs. Faced with such a law, a president in a country with a well-established rule of

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12 See O'Connor (2004) for a characterization of restrained discretion under a rule of law as a rule enforcer's judgement, choice, discernment, liberty, and license. Discussing police discretion, O'Connor offers three causes of discretion: factors related to the offender, situation, and system.

13 An obvious example is the introduction of a formal land title system in a rural Kenyan community, where land traditionally had been communally owned and used. A modern formal system of property rights did not work well because it clashed with traditional values and norms (Ensminger 1997). Many formal rules in the developing world (constitutions, VAT laws, budget laws, etc.) quite often have been designed by or in consultation with western experts, who have made their best to alter the rules to function effectively in an alien environment, but may not be successful all the time.

14 Alien, off-the-shelf, colonial rules uniformly introduced by a heterogeneous set of small societies with diverse indigenous rules would surely have high u's and e's in general and when they are enforced by local enforcers in particular. In the US, the enforcement problem resulting from the lack of compatibility between the formal institutions that emerged from the Constitutional Convention and the informal norms of the south was so severe that the tension could be resolved only with a violent war.

law may try to change the provision, but still will be obligated to enforce the provision faithfully until it is amended or revised. A president in a society where a rule of man is practised may simply choose to enforce it in a discretionary manner.

iii) Finally, corruption matters. Research has shown that a system of discretionary rule enforcement gives rise to corruption. And corruption may engender discretion.

Given a rule, its enforcement in any society is a process of interactions among a number of interested parties, which may include:

a) those (e.g., police officers, tax administrators, prosecutors, judges, or tyrants) who are directly in charge of enforcing the rule (i.e., primary enforcers),

b) those (e.g., automobile drivers, taxpayers, criminals, and citizens) who are required to observe it, and

c) others (e.g., jurors, defence attorneys, the public, the press, and NGOs and other pressure groups).

The outcome of rule enforcement is the end result of interactions—some taking longer than the others—among these parties, some obviously having more inputs or influences than others in the process.

In a strictly rules-based society, e_{it}, in principle, could be zero (no exception or discretion), although this is not a realistic case in practice. In a society that enforces rules with a high degree of discretion, e_{it} would be large. In a one-man tyranny, e_{it} in all substantive cases would largely represent the tyrant's intentions, whims, and interests.[15]

Rule enforcer's view of how the rule should be enforced

An important feature of discretionary rule enforcement under a rule of man is the important role of the individuals (or the groups of individuals in a leadership position with authority) in charge of interpreting and enforcing rules. In a world of vertical collectivism, paternalistic role expected from them and a large power distance in a hierarchical political and social structure allow the rule enforcers to use discretion more than in rules-based individualist societies.

To show this process formally, let y^*_{it} and y^{**}_{it} be the values of y_{it}, respectively, (i) dictated by the rule itself and (ii) considered appropriate collectively by the enforcers in a rule enforcement stage: e.g., police officer(s) in the case of highway patrol, tax administrator(s) for the enforcement of tax laws, or law enforcement official(s) in general.[16] One may contrast the two cases as follows:

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15 In this case, depending on circumstances, either (i) the rule itself may entirely reflect the tyrant's view, and both u_{it} and e_{it} may be zero or (ii) there may not be a rule, and u_{it} and e_{it} may be arbitrarily determined by an unprincipled tyrant (a and b = 0).

16 As shown later, rule enforcement may be a multi-stage process. There will be different primary enforcers. For simplicity, the discussion here assumes only one rule enforcer. This assumption will be later relaxed.

rule: $y^*_{it} = a + bx_{it}$ (2)

rule enforcers' intention: $y^{**}_{it} = a + bx_{it} + u_{it}$ (3)

In Equation (3), u_{it} reflects the degree of the deviation (in what direction and to what extent) that, in the view of the rule enforcer(s), the outcome of the enforcement of a rule should differ from the outcome dictated by the rule for an agent i required to observe the rule. In Equation (3), u_{it} may either reflect either the individual view of a sole enforcer or the collective view of enforcers (a) above.[17] Starting with this, a rule enforcement process yields the final outcome (y^o_{it}) of the process and the final deviation (e_{it}). Before presenting a model of this process, it is necessary to discuss the nature of u_{it} and e_{it}.

Thus, in a simple case, a traffic police officer may be the sole enforcer of a speed limit. Even in this case, however, the officer not only forms his or her own view (u_{it}), but also chooses to issue, or not issue, a ticket (i.e., determines e_{it}) by internalizing the social optimization process. There may also be a simple administrative hearing, to which the driver caught for speeding may choose to take the case. This would involve other enforcers. In another case, the prime minister and the minister of finance in a country get involved in granting discretionary tax allowances to a firm. In still other case, the president, the minister of justice, and the attorney general, collectively, but as a hierarchy, may decide whether to indict a prominent politician in a politically-sensitive criminal case.

An interesting, under-researched source of a nonzero u_{it} and e_{it} is cultural collectivism, which tolerates rule enforcers' discretion and, in particular, authoritarianism and paternalism that are often found in a world of vertical collectivism. An authoritarian, paternalistic rule enforcer may put, or may be allowed to put, his or her view *above* the rule, not necessarily as a result of sinister intentions (although these are widespread), but of what he or she believes to be good intentions.

Note the difference between e_{it} and u_{it}. The former reflects the outcome of rule enforcement; the latter the intentions of the rule enforcers, who in general are in a leadership position. In a world of vertical collectivism, rule enforcers have authority, often tolerated by the members of society and, thus. inadequately checked and balanced, even in societies that have established democratic political institutions, quite often imported from abroad.

A main difference between a rule of law and a rule of man is that the variances of e's in the former are smaller than the variances of e's in the latter. This hypothesis will be formally formulated and will be tested later in this paper. Whether the variances of u's are necessarily smaller in the former than the latter is not immediately obvious. On the one hand, individualist values imply diverse opinions and views among individuals and thus may allow a variety of views on how a rule should be enforced. On the other hand, a culture of discretion may allow member of a collectivist society to have a larger u.

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[17] The deviation u may reflect the views of all enforcers when there are more than one. Thus, in a criminal case, u would reflect collective judgement of a prosecutor and a judge, while e reflects the final outcome of the rule enforcement process. Prosecutors and judges may have similar u's in a routine criminal case even in a collectivist society, but may have sharply different u's in a politically sensitive, controversial case. The value of u in such a case will reflect an average of u's of all rule enforcers.

Therefore, there is no reason to believe that u's would be larger in a collectivist society, where discretionary rule enforcement is widespread, than in an individualist society, where rules-based rule enforcement is well established.

A president, a judge, or a tax administrator in a rules-based, individualist society may have a personal or professional view that implies as large u's in the enforcement of a country's constitution, criminal law, or tax law as his or her counterpart in a discretion-based, collectivist society. The difference between a rules-based society and a discretion-based society is that the system (a tradition of a rule of law, based on individualist values and a system of checks and balances) in the former ensures small e's (but not necessarily small u's), while this is not the case in the latter.[18]

While there is no presumption that the variances of u's should differ between individualist and collectivist worlds, the variances of u's may differ between legal professionals and the public in general, or between judicial branch personnel (e.g., judges), who are trained law enforcement experts, and others who participate in law enforcement as members of members of a jury or of a pressure group.

3.2 Rule enforcement as a social optimization process

How does a society (e.g., an individualist one), given a large u_{it}, ends up with an outcome that implies a small e_{it}? How does a society (e.g., a collectivist one) end up with an outcome that implies a large e_{it}?

Objective function

To model a rule enforcement process, one can postulate that a society, through interactions among different groups and individuals, tries to minimize the *social costs* arising from two factors: by how much the final outcome deviates from (i) the rule and (ii) the intentions of the rule enforcer (in a simple case of one enforcer). Furthermore, one can also postulate that the cost function, which encapsulates the society's shared values, is quadratic with respect to the two factors:

$$\text{social cost} \quad C_t = \Sigma_i(1-\theta)(y^o_{it} - y^*_{it})^2 + \Sigma_i\theta(y^o_{it} - y^{**}_{it})^2 \qquad (4)$$

for each t.[19]

The difference, $y^o_{it} - y^*_{it}$, for agents, i = 1, 2, …, I, who are required to observed a rule, represents by how much the outcome of rule enforcement deviates from what the rule intends, and the difference, $y^o_{it} - y^{**}_{it}$, represents by how much the outcome of rule enforcement deviates from the outcome desired by the rule enforcer. The model

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18 For example, during the 1960 presidential campaign, John F. Kennedy said that, as President, he would uphold the US laws even if they are not in line with his Catholic faith. Similarly, during a Senate confirmation hearing, John Ashcroft promised that, as the Attorney General, he would enforce the US laws even if they were not in line with his conservative view. That Kennedy was elected and that Ashcroft was confirmed indicate that US non-Catholic voters and Democratic Senators (particularly liberal ones) did not believe that Kennedy's and Ashcroft's personal views would significantly interfere in their law enforcement, respectively, as President and as Attorney General.

19 An alternative way to set up the optimization problem would be set it up to minimize: $C_t = \Sigma_i(1-\theta)e_{it}^2 + \Sigma_i\theta(e_{it} - u_{it})^2$ with respect to e_{it}. The solution would be the same.

postulates that the weights a society assigns to these two factors are determined by the society's values. More specifically, θ ranges between two unrealistic extremes: 0 (pure collectivism, implying extreme discretion) and 1 (pure individualism, implying pure rules):

$$\theta = 1 \text{ (collectivism)}$$
$$= 0 \text{ (individualism)}$$

Optimization

In the model, through checks and balances, a society collectively chooses an outcome of rule enforcement for each i and t, by using y^{o}_{it} as the instrument to minimize C. For each t, the society, with a group of primary and other rule enforcers working on its behalf, determines the values of I instruments, y^{o}_{it}, i = 1, 2, …, I, to minimize C. The solution, for each i and each t, will be as follows:

$$y^{o}_{it} = (1-\theta)y^{*}_{it} + \theta y^{**}_{it} \quad (5)$$

It is a fairly straightforward solution, with two special cases: (i) For a collectivist society under a pure rule of man, with θ = 1 (a maximum degree of discretion), Equation (5) becomes $y^{o}_{it} = y^{**}_{it}$. The outcome reflects the rule enforcer's discretion to its fullest extent. (ii) For an individualist society under a pure rule of law, with $\theta = 0$ (no discretion), Equation (5) becomes $y^{o}_{it} = y^{*}_{it}$. In this case, the outcome is pure rules.

The model highlights the essential difference between a rule of law and a rule of man. A rule of law (or rules-based rule enforcement) is a system in which the rule enforcer's rule enforcement activities are bound by a tradition of placing the rule *above* the rule enforcer's discretion (Madison's vision). A rule of man is a system in which the rule enforcers tend to put their views above the rule either because they feel that their deviations tend to promote public interests or because they want to promote their own personal gains. An extreme case would be the case of 'I am the law'.

3.3 Extensions—a model of multi-stage rule enforcement

This model, while highlighting the essential differences between rules and discretion, is too simple to capture rule enforcement in practice. It presumes that rule enforcement is a one-step process that involves one enforcer or one group of enforcers. There are cases that can be represented by this simple model. In many cases in reality, however, the enforcement of a tax law or a criminal justice system directly involves many individuals and/or groups in more than one step.

Rule enforcement in practice

For example, a dispute arising from regulatory enforcement may proceed as follows:

a) The regulatory officials in charge of judging the case would decide whether it should be resolved administratively or be brought for criminal prosecution.

b) If the administrators decide to proceed for prosecution, the prosecutors would decide whether the case should be brought to the court.

c) The court would be in charge of the trial. Judges (and juries) would be involved. The case might go to higher courts. In a federal system of government, the case might go through local, provincial, and federal courts.

In each stage, each of the rule enforcers (e.g., regulators, prosecutors, and/or judges) would form their views that can be represented by Equation (3). In another example, death sentence cases may go to the office of president or to provincial chief executive (e.g., a state governor in the United States).

The final outcome in each step will be shaped by a mixture of rule enforcers' convictions and social values. In rules-based societies, rule enforcers, even with large u_{it}, tie their hands, voluntarily or through a system of checks and balances embedded into the rule enforcement system that reflects their shared values, and allows the final outcomes to be faithful to the rules. They do not necessarily change their u_{it}.

If the rule enforcer in each of the above stages is a group (e.g., tax administrator, prosecutor, and judge), rather than individuals, u_{it} will reflect the collective view (e.g., a weighted average) of the group, which would produce a formal or informal leader.

This simple model lends itself to some theoretical extensions and empirical tests. A theoretical extension may proceed as follows:

An extended model

The model may incorporate some of the elements listed in the preceding section to highlight the essential features of discretionary rule enforcement in practice. For example, one may wish to build a more elaborate model to reflect the realistic features of multi-stage rule enforcement processes: Rule enforcement in each stage involves enforcers and a collective θ. The values of u and θ, in principle, may vary through successive stages. In *each* stage, the rule enforcer (or enforcers) forms his or her u, and the optimization, based on a value of θ, will yield an outcome (e and, therefore, y^o). As rule enforcement goes through successive stages, the outcome may change as follows:

First stage. The enforcer's discretion is as follows:

$$y^{**}_{1it} = y^*_{it} + u_{1it} \quad (6)$$

The first-stage optimization yields the following outcome:

$$\begin{aligned} y^o_{1it} &= (1-\theta_1)y^*_{it} + \theta_1 y^{**}_{1it} \quad (7) \\ &= y^*_{it} + \theta_1 u_{1it} \\ &= y^*_{it} + e_{1it} \end{aligned}$$

where θ_1 is the value of θ assumed for the first-stage optimization[20] and

$$e_{1it} = \theta_1 u_{1it}$$

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20 Note that θ reflects shared values in a society, but may vary across individuals. The essential difference between individualist and collectivist societies is that members of the former tend to have the values of θ closer to 0 than the members of the latter, who tend to have those closer to 1.

This result needs some elaboration. This paper argues that, in a rule enforcement case in which individualist and collectivist societies have identical rules, rule enforcers under a rule of law (i.e., in the former) and under a rule of man (i.e., in the latter) behave differently. The values of u's, as well as e's, would obviously differ among enforcers within these societies, as well as between the societies. The essential difference between a rule of law and a rule of man is that the variances of e's, reflecting the outcomes of social optimization processes, would be smaller in the former than in the latter, whereas the variances of u's would not necessarily differ between the societies. The following hypothetical example illustrates this point:

A junior police officer, in the middle of the night, catches a drunken driver, who turns out to be their boss, the chief of a small precinct in a metropolitan police department. The chief's car had a near-collision with another car, driven by a mutual friend. The chief, with perfect career records in the department and in line for a promotion shortly, got drunk after having severely reprimanded another police officer with a strong professional record for a rare, but severe misjudgement.

Suppose two junior police officers in two different societies confronted this case. Suppose traffic rules in both societies required the officers to issue two tickets to the chiefs on two counts, drunken *and* reckless driving. This means that x_{it} is sufficiently large to yield the value of y^{o}_{1i} to trigger 1 (to issue a ticket), not 0 (no ticket) on both counts. The model predicts that the officer under a rule of law would be likely to issue two tickets, but the officer under a rule of man might not issue a ticket at all or issue only one ticket, for example, for drunken driving, but not for reckless driving.

That is, in the context of the model, the police officers would internalize the optimization processes in their respective societies, ending up with different verdicts, even if they might have begun the rule enforcement processes with either similarly large initial positive u's, reflecting their judgement that the case is serious enough, or large negative u's (for not issuing a ticket), reflecting a number of mitigating factors for their respective chiefs (the unblemished records, difficult decision with regard to his subordinate, no injuries or property damage, etc.). The two police officers would be guided by different values in their professional judgement and would possibly face different informal and formal sanctions for their actions. The former might expect sanctions for not issuing two tickets, the latter sanctions in an opposite direction for being too harsh to his boss with unblemished record. In this case, when they faced institutionalized second-stage enforcement procedures, they would expect different outcomes from each other, the former a rules-based outcome, the latter an outcome more sympathetic to the precinct chief. This might also affect their courses of action.

Second stage. The rule enforcer's discretion will be

$$\begin{aligned} y^{**}_{2it} &= y^{*}_{it} + \delta_1 e_{1it} + (1-\delta_1)\, u_{2it} \\ &= y^{*}_{it} + \delta_1 \theta_1 u_{1it} + (1-\delta_1)\, u_{2it} \end{aligned} \qquad (8)$$

Equation (8) assumes that the second-stage enforcer's preferred deviation from the rule is a weighted average of his or her deviation (u_{2it}) and the deviation ($\theta_1 u_{1it}$) resulting as the outcome of the first-stage optimization. This formulation reflects the practice in both individualist and collectivist worlds. For example, prosecutors, when appealing their case to a higher court, will inevitably reflect on the lower court verdict.

To illustrate, one can continue to use the case of precinct police chiefs in two different societies in the preceding example. Suppose both chiefs decided to appeal to their respective internal tribunals, claiming that he should be treated more leniently because of all the mitigating factors.[21] Suppose the respective police departments selected, for the tribunals, senior officers to represent the junior officers who handled the case in the preceding stage and other senior officers to preside over the tribunals. In each of the two precincts in two different societies, the junior officer and the senior officers would have their own views, which would yield u_2 and $\delta_1\theta_1u_1 + (1-\delta_1)\ u_2$, drawing on the junior officer's verdict θ_1u_1 and their shared δ_1. The final outcome would reflect not necessarily their own views, but their own view of what is acceptable.

Criminal cases involving prosecutors would follow similar stages. There would be a first-stage enforcement process involving the enforcers (prosecutors, judges), who would form u_1, and others (a defendant, defence attorneys, pressure groups), who would contribute to the final first-stage verdict (e_1). When either side decides to appeal the verdict, there would be a new group of (most likely) more senior enforcers (a group of senior prosecutors, but possibly including all or some of the prosecutors involved in the first-stage enforcement process) who, together with other second-stage enforcers, would form a new u_2, and so forth.

The second-stage outcome would be determined as a result of optimization in the second stage:

$$\begin{aligned} y^{o}_{2it} &= (1-\theta_2)y^{*}_{it} + \theta_2\, y^{**}_{2it} \qquad (9)\\ &= (1-\theta_2)y^{*}_{it} + \theta_2[y^{*}_{it} + \delta_1\theta_1u_{1it} + (1-\delta_1)\ u_{2it}] \\ &= y^{*}_{it} + \delta_1\theta_1\ \theta_2u_{1it} + (1-\delta_1)\theta_2u_{2it} \\ &= y^{*}_{it} + e_{2it} \end{aligned}$$

where

$$e_{2it} = \delta_1\theta_1\ \theta_2u_{1it} + (1-\delta_1)\theta_2u_{2it}$$

The value of δ would range between 0 (in a vertically-oriented society) and 0.5 (horizontally-oriented society).

Third-stage. If the case goes through one additional step, the outcome will be:

$$y^{o}_{3it} = y^{*}_{it} + \delta_1\delta_2\ \theta_1\theta_2\ \theta_3\ u_{1it} + (1-\delta_1)\delta_2\ \theta_2\theta_3\ u_{2it} + (1-\delta_2)\theta_3u_{3it} \qquad (10)$$

The outcome of rule enforcement in a multi-stage rule enforcement system reflects θ's, δ's, and u's in successive stages. In particular, the outcome depends on the index of collectivism-individualism (θ) and the index of vertical-horizontal orientation (δ). The following are four special cases for possible outcomes at the Sth step (s = S):

a) Pure rules

i) $\theta = 0$, $\delta = 0.5$ horizontal orientation (a small power distance)

$y^{o}_{Sit} = y^{*}_{it}$

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[21] Here the junior officer in the collectivist society is assumed to have issued one ticket.

ii) $\theta = 0, \delta = 0$ vertical orientation (a large power distance)

$y^{o}_{Sit} = y^{*}_{it}$

b) Maximum discretion

i) $\theta = 1, \delta = 0.5$ horizontal orientation

$y^{o}_{Sit} = y^{*}_{it} +$ weighted average of u_{Sit}, u_{S-1it}, u_{S-2it}, …., the weights starting with 0.5 for the last-stage enforcer, but declining exponentially

ii) $\theta = 1, \delta = 0$ vertical orientation

$y^{o}_{Sit} = y^{*}_{it} + u_{Sit}$

In a pure rules-oriented (individualist) society, the outcome of rule enforcement reflects rules regardless of whether the society is horizontally oriented or vertically oriented. In a purely discretion-based (collectivist) society, horizontal orientation and vertical orientation make a difference. In the former, the discretion of the enforcers in successive rule enforcement stages matters; in the latter, the discretion of only the last stage enforcer matters.[22]

Table 1 illustrates the results of multi-stage rule enforcement simulated for four different combinations: $\theta = 0.3, 0.7$ and $\delta = 0.5, 0.1$. Main features of the results, which yield some useful suggestions for designing a rule enforcement system, include the following:

a) Multi-stage rule enforcement tends to reduce, but does not eliminate discretion in rule enforcement outcomes in a collectivist society;

b) Independence of judgement of rule enforcers in a hierarchy of rule enforcement helps reduce the degree of discretion (the difference between the standard deviations of e's in columns A and B);

c) Horizontal orientation tends to reduce the degree of discretion particularly when rule enforcers in successive stages form their views *independently*.

Some of these results are inevitable results of cultural values. Collectivism tends to promote uniformity in attitude and values, consensus, and harmony, compared with diversity in attitude and values and contention. Rule enforcers with collectivist values at different rule enforcement stages may not be independent of each other in forming their views. This may be more pronounced in a vertically-oriented collectivist world than in an individualist world. For example, lower-stage rule enforcers in a hierarchical society may develop capacity to 'read' the minds of higher-level rule enforcers. The outcome of their rule enforcement may already reflect the view of higher-level enforcers even before the case arrives at the latter's office.

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22 Note that a pure discretion-based enforcement in this paper means that the outcome of rule enforcement reflects the rule enforcers' intentions unaltered, not that rules are totally disregarded.

Table 1
Degree of discretion in multi-step rule enforcement
under horizontal and vertical individualism and collectivism

	H 0.50							V 0.10						
						Degree of discretion							Degree of discretion	
						A	B						A	B
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(1)	(2)	(3)	(4)	(5)	(6)	(7)
S=1														
	u1	u2	u3					u1	u2	u3				
I 0.30	0.30					0.30	0.30	0.30					0.30	0.30
C 0.70	0.70					0.70	0.70	0.70					0.70	0.70
S=2														
	u1	u2	u3					u1	u2	u3				
I 0.30	0.05	0.15				0.20	0.16	0.01	0.27				0.28	0.27
C 0.70	0.25	0.35				0.60	0.43	0.05	0.63				0.68	0.63
S=3														
	u1	u2	u3					u1	u2	u3				
I 0.30	0.01	0.02	0.15			0.18	0.15	0.00	0.01	0.27			0.28	0.27
C 0.70	0.09	0.12	0.35			0.56	0.38	0.00	0.04	0.63			0.68	0.63
S=4														
	u1	u2	u3	u4				u1	u2	u3	u4			
I 0.30	0.00	0.00	0.02	0.15		0.18	0.15	0.00	0.00	0.01	0.27		0.28	0.27
C 0.70	0.03	0.04	0.12	0.35		0.55	0.37	0.00	0.00	0.04	0.63		0.68	0.63
S=5														
	u1	u2	u3	u4	u5			u1	u2	u3	u4	u5		
I 0.30	0.00	0.00	0.00	0.02	0.15	0.18	0.15	0.00	0.00	0.00	0.01	0.27	0.28	0.27
C 0.70	0.01	0.02	0.04	0.12	0.35	0.54	0.37	0.00	0.00	0.00	0.04	0.63	0.68	0.63

Notes:

I = individualism; C = collectivism; H = horizontal orientation; V = vertical orientation; The numbers are coefficients of, respectively, u1, u2, u3, ….

The outcome of rule enforcement, as described in Equations (7), (9), and (10) may be extended to cases of S = 4, … as follows:

$y^{o}_{1it} = y^{*}_{it} + \theta_1 u_{1it}$

$y^{o}_{2it} = y^{*}_{it} + \theta_2\theta_1\delta_1 u_{1it} + \theta_2(1-\delta_1)u_{2it}$

$y^{o}_{3it} = y^{*}_{it} + \theta_3\theta_2\theta_1\delta_2\delta_1 u_{1it} + \theta_3\theta_2\delta_2(1-\delta_1)u_{2it} + \theta_3(1-\delta_2)u_{3itS}$

$y^{o}_{4t} = y^{*}_{it} + \theta_4\theta_3\theta_2\theta_1\delta_3\delta_2\delta_1 u_{1it} + \theta_4\theta_3\theta_2\ \delta_3\delta_2(1-\delta_1)u_{2it} + \theta_4\theta_3\delta_3(1-\delta_2)\ u_{3it} + \theta_4(1-\delta_3)u_{4it}$

If θ_j's and δ_j's do not vary with j's ($\theta_j = \theta$ and $\delta_j = \delta$), the above expressions will be simplified as follows:

$y^{o}_{1it} = y^{*}_{it} + \theta u_{1it}$

$y^{o}_{2it} = y^{*}_{it} + \theta^2\delta u_{1it} + \theta(1-\delta)\ u_{2it}$

$y^{o}_{3it} = y^{*}_{it} + \theta^3\delta^2 u_{1it} + \theta^2\delta(1-\delta)u_{2it} + \theta(1-\delta)u_{3it}$

The table reports, in columns (1)-(5), the coefficients for u's for θ = 0.3 and 0.7 and δ = 0.5 and 0.1. The table also reports, in columns (6)-(7), the standard deviations of e_s's (or θu_1, $\theta^2\delta u_1+(1-\delta)u_2$, …) (s = 1,2,…) for two cases in which: (A) u_s's are identical (i.e., $u_1 = u_2 = u_3$ …) and (B) u_s's are independent. Both are not realistic in their pure form, but can highlight two contrasting cases: In the first case, rule enforcers in different stages have identical views; in the second case, rule enforcers' views are totally uncorrelated. In the first case, rule enforcers in different stages form their views in unison. In the second, they form their views independently, not influenced by each other. The standard deviations of e_s's under these two extreme assumptions can highlight the extent to which the outcome of rule enforcement deviates from the rule itself.

On the basis of the assumption that the standard deviations of u's are the same for all s = 1, 2, .., S (i.e., $\sigma_{u1} = \sigma_{u2} = \sigma_{u3}$ … $= \sigma_u$), the results in columns (6)-(7) may be derived as follows for two cases a and b below, by using s =3 for illustration: (notes continue)

Notes to Table 1 (con't)

$y^{o}_{3it} = y^{*}_{it} + \theta^3\delta^2 u_{1it} + \theta^2\delta(1-\delta)u_{2it} + \theta(1-\delta)u_{3it}$

a) If $u_{1it} = u_{2it} = u_{3it} = u$ (the case in which the views of rule enforcers' views are identical in all steps of rule enforcement).

$y^{o}_{3it} = y^{*}_{it} + \theta^3\delta^2 u + \theta^2\delta(1-\delta)u + \theta(1-\delta)u$

$y^{*}_{it} + [\theta^3\delta^2 + \theta^2\delta(1-\delta) + \theta(1-\delta)]u$

In this case,

$[E(y^{o}_{3it} - y^{*}_{it})^2]^{0.5} = [\theta^3\delta^2 + \theta^2\delta(1-\delta) + \theta(1-\delta)]\,[E(u)^2]^{0.5} = [\theta^3\delta^2 + \theta^2\delta(1-\delta) + \theta(1-\delta)]\sigma_u$

Column (6) reports the coefficient $\theta^3\delta^2 + \theta^2\delta(1-\delta) + \theta(1-\delta)$ in each of the four cases.

b) If u_{1it}, u_{2it}, and u_{3it} (views of rule enforcers in various rule enforcement stages) are stochastically independent, i.e., $E(u_{sit}u_{vjt}) = \sigma_{usv} = 0$, for all s and v, not equal to each other.

$[E(y^{o}_{3it} - y^{*}_{it})^2]^{0.5} = [(\theta^3\delta^2)^2 + (\theta^2\delta(1-\delta))^2 + (\theta(1-\delta))^2]^{0.5}\,[E(u)^2]^{0.5} =$

$[(\theta^3\delta^2)^2 + (\theta^2\delta(1-\delta))^2 + (\theta(1-\delta))^2]^{0.5}\sigma_u$

Column (7) reports the coefficient $[(\theta^3\delta^2)^2 + (\theta^2\delta(1-\delta))^2 + (\theta(1-\delta))^2]^{0.5}$ in each of the four cases.

Some of these results can provide useful suggestions for designing a rule enforcement system that restraints discretion in a collectivist society. For example, an increase in the number of stages will tend to reduce the degree of discretion, although the results in Table 1 indicate that the reduction in the degree of discretion tapers off rapidly after the second stage. Moreover, there can be institutional arrangements to make the outcomes of rule enforcement in different rule enforcement stages more independent. Such an effort in a hierarchical society should require elaborate arrangements aimed at institutionally protecting the independent judgement and independence of lower-stage rule enforcers.

Relationship of the model to other models addressing discretion

The existing studies on rules, in the tradition of studies of crimes by Becker (1968), generally focus on economic factors that affect rational individual agents reacting to existing rules. Many recent studies analyse the relationship between discretion and corruption. These studies point to rule enforcers' opportunities to exercise discretion as a source of corruption. At the same time, these studies also note that given a chance, government officials might try to create opportunities to use discretion. A model along these lines has been aimed at establishing the factors that determine u_{it}.

The model in this paper, however, is aimed at identifying a broader set of factors that give rise to discretion in rule enforcement. It is not interested in finding out how u's are determined for individual agents who are required to observe rules, but how societal values in different countries, over time, determine the magnitudes of the variances of the rule enforcement outcomes (see Tanzi 1998, for a discussion of a range of factors, including cultural aspects, of corruption).

The existing models tend to recognize the possibilities to reduce discretion with proper short-run incentives or punishments, such as competitive wages for government officials and effective punishment for illegal acts. The model in this paper, however, suggests that the phenomenon of discretion in rule enforcement is much more deeply ingrained in a culture. Short-run solutions relying on models taking into account largely pecuniary factors to promote nondiscretion may not reach the heart of the problem. An

extensive study of corruption in the tax administration authorities in Tanzania and Uganda notes 'cultural logics' of corruption (Fjeldstad, Kolstad and Lange 2003).

4 Values and rules: cross-country tests

The model presented in the preceding section provides a basis for empirically testing whether collectivism does engender discretion. To this end, a statistical test may proceed as follows: Suppose one wants to use the model to test the hypothesis that values indeed shape the outcome of rule enforcement. One can use Equations (7), (9), (10), … to formulate testable equations.

a) For the case of S =1, subtract y^*_{it} from both sides of Equation (7) to obtain

$$y^o_{1it} - y^*_{it} = \theta(y^{**}_{1it} - y^*_{it}) \quad (11)$$

or

$$e_{1it} = \theta u_{1it}$$

By assuming that e_{it} and u_{it} both have zero mean,[23] squaring both sides of the equation, taking their expected values, and obtaining their square roots, one obtains

$$[E(e^2)]^{1/2} = \theta E[(u^2)]^{1/2} \quad (12)$$

or $\sigma_e = \theta\sigma_u$

or $\sigma_e = \sigma_u\theta$

In carrying out these operations, one assumes that e and u are random variables over the space of all i's and that θ, which is the same for all rule enforcers in a country, is a constant. This assumption does not strictly reflect the world as described in the preceding sections, which have stated that θ's may vary across individuals in a society. Since θ's reflect *shared* social values, however, this assumption, which was abandoned for theoretical analysis, is useful and not unreasonable for statistical analysis, considering that variation of θ's should be relatively small within a society, in comparison with across societies.

b) Deriving a testable equation for a multi-stage rule enforcement is somewhat more elaborate, but yields an equation in the form of Equation (12). For example, using Equation (9) for illustration to formulate an equation for S = 2, where s = 1, 2, …, S denotes rule enforcement stages, subtract y^*_{it} from both sides of Equation (9) to obtain

$$y^o_{2it} - y^*_{it} = \delta_1\theta_1\theta_2 u_{1it} + (1-\delta_1)\theta_2 u_{2it} \quad (13)$$

or $e_{2it} = \delta_1\theta_1\theta_2 u_{1it} + (1-\delta_1)\theta_2 u_{2it}$

Assume that $\theta_1 = \theta_2 = \theta$, which reflects shared values in a society and that u_{1it} and u_{2it} have a same variance, σ_u^2; denote their coefficient of correlation as ρ_{u12}; and simplify the notation by denoting $\delta_1 = \delta$. Then the variance σ_e^2 and the standard deviation σ_e of e_{it} can be shown to be

$$\sigma_e^2 = [\theta^4\delta^2 + (1-\delta)^2\theta^2 + \theta^3\delta(1-\delta)\rho_{u12}]\sigma_u^2 \quad (14)$$

---

23 The test does not depend crucially on this assumption, which can be relaxed.

and

$$\sigma_e = \sigma_u[\theta^4\delta^2 + (1-\delta)^2\theta^2 + \theta^3\delta(1-\delta)\rho_{u12}]^{0.5}$$

As in Equation (12), assume that σ_u is a constant, but

$$\sigma_e \text{ and } [\theta^4\delta^2 + (1-\delta)^2\theta^2 + \theta^3\delta(1-\delta)\rho_{u12}]^{0.5}$$

vary across countries, as discussed in the preceding sections. The former reflects the outcome of rule enforcement, which in turn reflects different degrees of discretion in different societies; the latter can be shown to vary between 0 and 1 and may be proxied by θ under the following conditions, which are reasonably realistic:

i) ρ_{u12} moves approximately linearly in line with θ, which ranges between 1 (collectivist) and 0 (individualist), allowing one to write $\rho_{u12} = \theta$ (approximately),

ii) $\theta = 1-2\delta$, with δ, a power distance index ranging between 0 (maximal power distance or vertical orientation) and 0.5 (minimal power distance or horizontal orientation). In accordance with Hofstede's findings, power distance is positively correlated with collectivism.

In (i) above, the assumption that ρ_{u12} is a (linear) positive function of θ means that individualist values allow the independence of opinions among rule enforcers, whereas collectivist values promote uniformity of opinions.

Under these conditions, both

$$\theta^4\delta^2 + (1-\delta)^2\theta^2 + \theta^3\delta(1-\delta)\rho_{u12}$$

and

$$[\theta^4\delta^2 + (1-\delta)^2\theta^2 + \theta^3\delta(1-\delta)\rho_{u12}]^{0.5}$$

range between 0 (when $\theta = 0$) and 1(when $\theta = 1$), and

$$[\theta^4\delta^2 + (1-\delta)^2\theta^2 + \theta^3\delta(1-\delta)\rho_{u12}]^{0.5}$$

mimics θ. Thus, Equation (14),

$$\sigma_e = \sigma_u[\theta^4\delta^2 + (1-\delta)^2\theta^2 + \theta^3\delta(1-\delta)\rho_{u12}]^{0.5}$$

may be approximated by Equation (12), which is also a testable equation for S = 2.[24]

Equation (12) suggests that the degree of discretion in the outcome of rule enforcement (σ_e) is determined by θ (society's collectivist tendency, i.e., to what extent, it practices a

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24 Let $\tau = [\theta^4\delta^2 + (1-\delta)^2\theta^2 + \theta^3\delta(1-\delta)\rho_{u12}]^{0.5}$. Simulations (i.e., calculating the values of τ for various values of θ in the range between 0 and 1, with the assumption that $\theta = 1-2\delta$, suggest that θ is related to τ approximately as in $\theta = -m + n\tau$, where m is an increasing function of the number of stages. The second form of Equation (14) may be written as $\sigma_e = \tau\sigma_u = [m/n + (1/n)\theta]\sigma_u = (\sigma_u m/n) + (\sigma_u /n)\theta$, which is in the form of Equation (15).

rule of man) and the degree of discretion desired by rule enforcers (σ_u). For a given σ_u, a large θ (a fraction close to 1) in a collectivist society would make the degree of discretion in rule enforcement outcomes relatively large, but a small θ (close to 0) in an individualist society would make the degree of discretion in the outcome of rule enforcement relatively small.

Suppose one wants to use the model to test whether different θ_j's (where j is the country subscript) in different countries affect σ_{ej}, the degree of discretion reflecting the outcomes of rule enforcement in different countries with different degrees of collectivist values. To this end, one can compile data on σ_{ej} for specific rules in a sample of countries.

a) For example, to analyse how a corporate tax law is enforced, one can collect data on the actual tax payments (y^o) of individual corporations (these payments would reflect discretionary exemptions, etc.) and compare them with their legal tax obligations (y^*),[25] taking into account legally recognized adjustments to them. The variances for the countries of the differences between the two amounts for different corporations could form a set of data on σ_{ej}, which can be regressed on a set of data on θ_j for the sample countries.[26]

b) To test cross-country differences of how judges observe a sentencing rule, one can compile data on judges' sentences (e.g., the lengths of prison terms) for a convicted crime (e.g., murder) committed in similar circumstances and compare them with the sentences suggested in the sentencing rule (or guidelines). These data, if compiled across countries, would form a basis for cross-country comparison of degrees of discretion.

c) A test may also be based on aggregate data. Measures of overall degree of discretion across countries may be regressed on measures of individualism-collectivism (see below).

This approach will yield an estimate of σ_u. If, contrary to the assumed stability (or constancy in a special case) of σ_e's cross countries, σ_e's vary widely (relative to the variation of θ_j) across countries, the estimation may not yield a high goodness of fit.

This paper uses cross-country data on indices of the rule of law, judicial independence, and soundness of property rights, as published annually in the World Economic Forum's *Global Competitiveness Report*s. These indices, based on opinion surveys, can be alternative proxies for a measure of discretion. Chu (2003) reports the econometric results for an equation similar to Equation (15). In addition to the rule of law equation (Equation (15a) below), this paper reports results for two more equations (Equations (15b) and (15c) below):

$$h_j = g_0 + g_1 z_j \qquad (15)$$

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25 The point of getting these data is to highlight the differences between legal tax obligations and actual payments reflecting discretion. While these data may not be easy to collect, proxies may be obtained.

26 The difference between y^o and y^* may be difficult to compile in practice, since tax administrators would have all the formal justifications for arriving at y^o. Unless a researcher can rely on professional experts to determine the amount of y^* corresponding to each y^o, one can use an opinion survey on the extent of discretion in the administration of the corporate income tax law.

where

h_j = ranging between 1 (least effective) and 6 (most effective) and defined, for Equations (15a), (15b), and (15c), as follows:

a) Equation (15a): index of the rule of law, i.e., an average of the World Economic Forum (WEF 2000-01) indices of predictability of rules, judicial independence, and integrity of property rights,

b) Equation (15b): index of judicial independence, i.e., WEF (2001-02) index of judicial independence; and

c) Equation (15c): index of soundness of property rights, i.e., WEF (2001-02) index of the soundness of property rights

z_j = ranging between 0 (least individualist) and 100 (most individualist),

which are defined to be inversely related to σ_{ej} (which increases as the degree of discretion rises and as h_j declines) and θ_j (which reaches 1 with an extreme collectivism and rises as z_j falls),[27] and

g_0, g_1 = coefficients

The series used for θ are drawn form Hofstede's measure of individualism-collectivism. The data on h's and θ's are two different data sets, constructed independently and compiled independently at different times and on the opinions of different respondents.

The estimation results are as follows:

a)	h_j =	3.659	+	$0.034z_j$	adj. $R^2 = 0.581$
		(15.22)		(7.60)	
b)	h_j =	3.117	+	$0.041z_j$	adj. $R^2 = 0.556$
		(9.790)		(6.98)	
c)	h_j =	4.437		$0.023z_j$	adj. $R^2 = 0.497$
		(21.53)		(6.21)	

The estimation results are unambiguous—the degree of individualism affects the decree of rules-based system of law. The h and z data are independently compiled. That they have such a robust statistical correlation cannot be chance results.

5 Institutional arrangements for nondiscretionary rule enforcement

An aim of democratic institutions is to separate *law-making* functions from *law-enforcement* functions and to establish checks and balance between the two. This

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[27] Therefore, both Equations (12) and (15) should yield a positive estimate of the coefficient for the right-hand variable. That is, in Equation (12), a higher index of collectivism (θ) causes a higher degree of discretion (σ_e). In Equation (15), a higher index of individualism (z_j) causes a higher index of the rule of law, judicial independence, and soundness of property rights (h_j), which means a lower degree of discretion. The two equations, based on the dependent and explanatory variables constructed differently, explain a same causal relationship.

enhances nondiscretionary law enforcement. More generally, since rules (including laws, policies, government decrees) are broader in scope than laws, separation of *rule making* and *rule enforcing* and making the process of rule enforcement not subject to political and other interferences would be necessary for nondiscretionary rule enforcement. A government can demonstrate a commitment to rules by enforcing the rules consistently and *non*discretionarily by subjecting itself to 'a set of rules that do not permit leeway for violating commitments' (North and Weingast 1996: 803). This very condition is not easy to fulfil in a collectivist society. As shown in an earlier section, however, adding a limited number of layers of rule enforcement stages and making them autonomous and independent, in principle, would be helpful.

5.1 Role of a multi-stage rule enforcement system with separation of powers

Both separation of powers and multi-stage rule enforcement tend to reduce chances of discretion. In the context of Equation (10), if the first- and the second-stage enforcement procedures take place in the executive branch, a multi-stage rule enforcement could mean a separate formation of u_{1it} and u_{2it}; separation of powers could mean a separate formation of u_{3it} from either u_{1it} or u_{2it}. The principles of separation of powers may be used not only *between* different branches of government, but also *within* a government branch.

Two-stage rule enforcement

Equation (10) could be the final outcome of two-stage rule enforcement in the executive branch and one-stage rule enforcement in the judicial branch:

$$\begin{aligned} y^{o}_{3it} &= y^{*}_{it} + \theta_3\, \delta_2\, [\delta_1\, \theta_1\theta_2 u_{1it} + (1-\delta_1)\theta_2 u_{2it}] + \theta_3[(1-\delta_2)u_{3it}] \\ &= y^{*}_{it} + e_{3it} \end{aligned} \qquad (10)$$

The degree of discretion $\delta_1\theta_1\theta_2 u_{1it} + (1-\delta_1)\theta_2 u_{2it}$ in the first set of brackets represents the rule enforcement outcome in the executive branch (i.e., e_{2it}); e_{3it} represents the final outcome that emerges at the end of the judicial process.

Effects of a two-stage, compared with a one-stage, rule enforcement system in the executive branch may be shown by comparing the following two terms in the first set of brackets [ ] in Equation (10):

$$\text{i)} \quad \theta_1 u_{1it} \qquad (16)$$

$$\text{ii)} \quad \delta_1\theta_1\theta_2 u_{1it} + (1-\delta_1)\theta_2 u_{2it}$$

with their respective variances as

$$\text{i)} \quad \theta_1^2 \sigma_{u1}^2 \qquad (17)$$

$$\text{ii)} \quad \delta_1^2\theta_1^2\theta_2^2\, \sigma_{u1}^2 + (1-\delta_1)^2\theta_2^2\sigma_{u2}^2 + \delta_1(1-\delta_1)\theta_1\theta_2^2\, \sigma_{u12}$$

where σ_{u1}^2, σ_{u2}^2, and σ_{u12}, respectively, are the variances of u_{1it} and u_{2it} and the covariance between u_{1it} and u_{2it}.

There are a number of cases of interest with regard to the implications of different rule enforcement systems in a collectivist society (i.e., where θ's are large and close to 1):

a) If it is horizontally orientated (e.g., with $\delta_1 = 0.5$), the degrees of discretion of the final outcome will reflect the views of the rule enforcers in both stages, with a smaller weight for the degree of discretion in the first stage than that for the degree of discretion in the second stage. If it is vertically orientated ($\delta_1 = 1$), however, the degree of discretion will reflect only that of the second-stage enforcer, who will have a more authority than the first-stage enforcer.

b) For the outcome of a two-stage rule enforcement system to be less discretionary than that of a one-stage rule enforcement system, the second variance should be smaller than the first variance in Equation (17). On the simplifying assumption that $\sigma_{u1}^2 = \sigma_{u2}^2 = \sigma_u^2$ and that (to drop the unnecessary subscript) $\delta_1 = \delta$, this condition becomes the following inequality:

$$[(1-\delta) + (1-\delta\theta^2)] - (1-\delta)\theta\rho_{u12} > 0 \qquad (18)$$

where ρ_{u12} = correlation coefficient between u_1 and u_2.

This result is important for highlighting the role of a multi-stage rule enforcement system. In Equation (18), which is an inequality, the left-hand side ranges between 1 (when $\delta = 0$, $\theta = 1$, and $\rho_{u12} = 1$, implying, respectively, vertical orientation, collectivism, and uniform views) and 1.5 (when $\delta = 0.5$, $\theta = 0$, and $\rho_{u12} = 0$, implying horizontal orientation, individualism, and independence of views). The parameters $1-\delta$, θ, and ρ_{u12} cannot exceed 1 even in the most extreme case of collectivism (vertical orientation, and group thinking) among rule enforcers. Even in this most extreme case, the inequality is satisfied, and a two-stage rule enforcement system would yield a smaller degree of discretion than a one-stage system does.

The result also indicates, however, that, under the assumed conditions, adding a second-layer of rule enforcement stage would reduce the degree of discretion more in individualist societies with horizontal orientation than in collectivist societies with vertical orientation. A reduced degree of collectivism, of vertical orientation, and of unity of views among rule enforcers would further reduce the degree of discretion. But these are cultural parameters and not independent of each other. For example, for a collectivist society to reduce ρ_{u12} close to zero without a cultural evolution would not be easy, although some institutional arrangements could help the society achieve some reduction in ρ_{u12}. Note also that a gradual reduction in ρ_{u12} resulting from changes in values would bring about a greater degree of horizontal orientation (i.e., an increase in δ toward 0.5). This interdependence does not allow one to assess the effect of a reduction in ρ_{u12} under a ceteris paribus condition.

Adding a second layer of enforcement, however, could *increase* the degree of discretion when, contrary to the assumption for the preceding conclusion, σ_{u1}^2 and σ_{u2}^2 are different and σ_{u2}^2 is significantly larger than σ_{u1}^2.

Separation of powers in rule enforcement

How does separation of powers contribute to a reduction in the degree of discretion? Let's go back to Equation (10):

$$\begin{aligned} y^o_{3it} &= y^*_{it} + \theta_3\delta_2[\delta_1\theta_1\theta_2 u_{1it} + (1-\delta_1)\theta_2 u_{2it}] + \theta_3[(1-\delta_2)u_{3it}] \qquad (10) \\ &= y^*_{it} + \theta_3\delta_2 e_{2it} + \theta_3[(1-\delta_2)u_{3it}] = y^*_{it} + e_{3it} \end{aligned}$$

Suppose the executive branch brings the case with an outcome y^{o}_{2it} to the judicial branch. In the model, a group of third-stage enforcers, including a judge or a group of judges, form the value of u_3 in the process of trial. The final outcome of the trial (e_3) would emerge from optimization involving these enforcers, defence lawyers, a jury, and pressure groups if it is a criminal case.

The degree of discretion in the outcome of rule enforcement under a system of separation of powers between the executive branch and a judicial branch may be compared with that in the executive branch outcome. This can be achieved by comparing the variances of the following two terms:

$$\delta_1\theta_1\theta_2 u_{1it} + (1-\delta_1)\theta_2 u_{2it} = e_{2it} \quad (19)$$

$$\theta_3\delta_2[\delta_1\theta_1\theta_2 u_{1it} + (1-\delta_1)\theta_2 u_{2it}] + \theta_3[(1-\delta_2)u_{3it}] = \theta_3\delta_2 e_{2it} + \theta_3[(1-\delta_2)u_{3it}] = e_{3it}$$

Similar in its form to the case of two-stage rule enforcement, the relevant inequality will be:

$$(1-\theta_3^2\delta_2^2)\sigma_{e2}^2 - \theta_3^2(1-\delta_2)^2\sigma_{u3}^2 - \theta_3^2\delta_2(1-\delta_2)\sigma_{eu} > 0 \quad (20)$$

where:

σ_{e2}^2, σ_{u3}^2, and σ_{eu}

are, respectively, the variances of e_2 and u_3 and their covariance. On the basis of a simplification (to drop subscripts and to use σ_{e2}^2 to denote the variance of e of the executive branch and $k\sigma^2$ to denote the variance of u of the judicial branch):

$$\theta_3 = \theta,\ \delta_2 = \delta,\ \sigma_{u3}^2 = k\sigma_{e2}^2 = k\sigma^2$$

where $k = \sigma_{u3}^2/\sigma_{e2}^2$ is the ratio between the degrees of discretion of the judicial branch and the executive branch, the inequality will take the following form:

$$[1-(1+k)\theta^2\delta^2-\theta^2(1-2\delta)k]\sigma^2 - \theta^2\delta(1-\delta)^2\sigma_{eu} > 0 \quad (21)$$

which can be rewritten as:

$$[1-\theta^2\delta^2-\theta^2(1-\delta)^2k]\sigma^2 - \theta^2\delta(1-\delta)^2\sigma_{eu} > 0 \quad (22)$$

The contribution of the judicial branch to a reduction in discretion works through two terms:

$\theta^2(1-2\delta)k$ and

$\theta^2\delta(1-\delta)^2\sigma_{eu}$

In the former, $\theta^2(1-2\delta)k$, a smallest possible k (e.g., a number close to zero), that is, a strict constructionist approach to rule enforcement of the judicial branch will maximize the value of the first term (which should be positive in this case) in Equation (22). In the latter, $\theta^2\delta(1-\delta)^2\sigma_{eu}$, the separation of powers (and checks and balances) means that the judicial branch should be prepared to offset the executive branch's undue discretion. This judicial role implies a negative value for σ_{eu}, which will make $\theta^2\delta(1-\delta)^2\sigma_{eu}$ negative and will enhance chances for the inequality in Equation (22) to be satisfied.

Vertical orientation means, however, that separation of powers may not be *de facto* effective for important political cases, although *de jure* institutions promise its effectiveness, particularly when a collectivist country has a powerful president or prime minister who towers over the judicial branch.

Conditions for multi-stage rule enforcement to succeed in reducing discretion are a negative $\theta\rho_{u12}$ and a negative σ_{eu}—the conditions not easy to satisfy with group-thinking tendencies in collectivist societies.

5.2 Institutions for nondiscretionary rule enforcement: lessons of practice experiences

This section assesses the ideas discussed in Chu (2003) in the context of the formal analytical results shown earlier in this paper.

In a collectivist culture, nondiscretionary rule implementation has deep cultural roots. Threats to *non*discretionary rule implementation often come not only from the political party in power, but also from other social groups to which members of different government branches have regional or tribal ties.[28] These informal ties weaken checks and balances intended in formal separation-of-powers principles. Rule implementation is also undermined by the fact that functions of the executive branch often encompass both rule making and rule implementing. Finance ministries—politicians in many cases—not only *formulate* rules (e.g., tax policy, budget, and regulatory measures), but also often *implement* them, although, in a formal sense, the real authority for their legislation belongs to the legislative branch. This makes it difficult to establish rule enforcement as a nonpoliticized function.

Nondiscretionary rule enforcement: principles

To ensure *non*discretionary rule implementation, the relations of rule-implementing agencies might be redefined vis-à-vis their rule-making counterparts. The following are a number of principles to this end:

a) Establish important rule-implementing functions as nonpoliticized, professional, and technical activities, separate from rule making. While neither possible in all cases nor easy, it seems feasible to isolate a set of critical *rule-implementing* functions, such as those of (i) public prosecutors, (ii) tax administrators, (iii) regulators (e.g., in charge of antitrust, banking supervision), and (iv) budget implementers. While a rule-making agency should cooperate with a rule-implementing agency, it appears not essential for them to be part of a same agency.[29] Separating rule enforcing functions (e.g., tax administration,

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[28] Public choice theory suggests that an independent civil service can make it difficult for an elected government to pursue promised policies. (See for example Tullock 1987.) In countries with a collectivist culture, however, an excessive loyalty of bureaucrats to elected politicians can be a source of discretion in rule implementation.

[29] Separating rule making and rule implementing is a dimension that differs from seeking accountability through institutional pluralism, which involves decentralizing administrative functions through devolution, deconcentration, and delegation to lower levels of government and private sector partners. (See Cohen and Peterson 1999.)

budget execution) from rule-making ones (tax legislation, tax policy formulation, budget formulation) is essential to make them technical and not politicized. While it is necessary to strip rule-making agencies of rule enforcing functions, it is also critical to ensure that rule enforcing agencies do not interfere in rule making, which is essentially political. These two functions should be separate to the extent possible. When they are not separate, it is not possible to have a professional, technical head for rule enforcing functions. Contrary to this principle, many countries mix policy formulation functions with policy implementation functions under one head. Quite often, tax collection functions (enforcing tax laws) are under the control of the minister of finance, who is in charge of tax policy formation, which is a political function.

b) Ensure checks and balances. These can be achieved by multi-stage enforcement and also by separation of powers in some cases. In a society dominated by collectivist values and a large power distance, tax administrators may be unduly loyal to those who appoint them. As head of tax collection agency, a minister of finance—a political appointee—would find it difficult to resist political pressure. Autonomous, nonpoliticized tax administration agencies would have greater chances of resisting the political pressure to use discretion in their administration of a tax policy regime.

The preceding analysis shows why individualist societies have been able to develop a rule enforcement system that does not give rise to a high degree of discretion by using multi-stage rule enforcement and separation of powers. The analysis also shows how vertically-oriented collectivist societies might not be able to achieve a similarly low degree of discretion from a same formal multi-stage rule enforcement system. To benefit from these formal arrangements, the latter societies would have to add other features. It is not easy to specify such additional features in general terms. The following ideas, however, would be worthwhile to explore:[30]

a) Additional features should be aimed at minimizing chances for domination by higher-stage rule enforcers in vertically-oriented collectivist societies. Any features to this end would be easier to introduce into the system than to practice. The degree of difficulties would vary between routine rule enforcement activities at relatively lower levels and politically sensitive rule enforcement activities at higher levels. One possible idea would be to require a second-stage enforcement, if there is to be one, to be charged by an official to whom the first-stage primary enforcer does not normally report. For example, a tax official in the B region, with no personal ties with those involved in the first-stage proceedings, would handle the second-stage proceedings required for a tax case in the A region.

b) Additional features should also be aimed at minimizing the effects of group thinking. The analysis suggests that two independent views of two groups of two individuals are likely to contribute more effectively to a reduction in

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30 These ideas are obviously abstract and need to be developed into a detailed and concrete proposal. More importantly, for practical adoption, these ideas require 'institutional entrepreneurs', as discussed in Chu (2004).

discretion than one view that emerges from a group of four individuals. A jury system as it is practised in individualist countries, if introduced without additional features, might not be as effective as in collectivist countries, where members of a jury would deliberate on a case not as equals who speak their minds, but would tend to seek a *cohesive* group judgement. In such a case, rather than relying on one jury of 12 individuals, a modified system might rely on two juries, with six individuals each, to judge on a case independently, with either the final verdict to be made by, say, a presiding judge, or the final guilt verdict to require two independent guilt verdicts of the two juries.

It is important, however, to hold autonomous rule-implementing agencies accountable. It is not easy to determine the degree to which central government rule-implementing agencies (e.g., prosecutors, tax administrators, regulators) chosen to be autonomous should be independent of those in charge of rule making. Should they be independent of ministers, the prime minister, or the president? Different countries would have different circumstances. A question is whether the possibility of rule-implementing officials' abuse of autonomy is relatively more tolerable than the rule making elected officials' abuse of power for their own political gains.

Country experiences: an overview

Separating rule making from rule implementing has received attention both in countries with an individualist culture and in those with a collectivist culture:

a) Many countries have a professional civil service, although its effectiveness varies across countries. The United States introduced the Civil Service Commission, now the Office of Personnel Management, in 1883 to replace the 'spoils system' with a 'merit system'.

b) New Zealand's public expenditure management system is based on separating the role of ministers, who are responsible for policymaking, from the role of departmental chief executives, who are in charge of policy implementation (Scott 1996 and Lee 1995). This system may not work well in a collectivist culture, in which rule makers are likely to be a source of discretionary rule implementation.[31] The basic approach, however, with some modifications, can be considered for developing countries.

c) In the new programme budget system in Brazil, a culturally collectivist country, a programme manager, who is in charge of implementing a budgeted programme, does not report to the line ministers who control the budgetary resources that are used as inputs for the programme. This system adds a layer of checks and balances in the process of budget execution, in addition to the one provided by parliamentary oversight.

d) A number of developed and developing countries have foreign nationals as heads of key policy implementing agencies (e.g., tax collection agency). A

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31 See Bale and Dale (1998) for the demanding conditions that must be satisfied for a successful New Zealand-type reform: (i) a consistent, comprehensive conceptual model, (ii) a clear performance definition, and (iii) a focus on what government does best. Schick (1998) suggests that a successful New Zealand-type reform should follow basic reforms to strengthen rules-based government.

number of African countries have established independent revenue authorities mandated with tax collection. Some have gone further, by inviting foreign rule enforcers, who are less likely to have personal ties with domestic interest groups.

e) Some others have used foreign commercial firms for certain aspects of customs administration (e.g., pre-shipment inspections). To an extent, these are aimed at enhancing *non*discretionary implementation of rules (e.g., tax laws, customs laws) by mandating those without ties to domestic interest groups to implement rules.[32]

Rule enforcement functions as technical services

Once a country establishes rule enforcing as well-defined activities separate from rule making, the country has a variety of approaches to reducing discretion in carrying out them. A government might consider unusual approaches, such as outsourcing some of these activities to private sector organizations and even to foreign organizations. Fiscal transparency requires that government clearly delineate the demarcation between the spheres of government and the rest of the economy. Conventional wisdom suggests that rule enforcing activities are governmental functions. However, a range of what used to be governmental functions or activities are now outsourced to private agents. For example, government does not necessarily purchase and distribute foodstuff to the designated recipients of the government social assistance programme that distributes food to the poor.

Government must set the objectives of the programme, but does not have to deliver food to the poor. Similarly, government may outsource the operation of prisons to private agents. While government designs these programmes and set their objectives, it may outsource the well-defined activities involved in service delivery. Traditional wisdom is to consider public sector activities as sovereign, not subject to outsourcing to foreign agents, while private sectors, such as banking, manufacturing, and retailing can open up to foreign investment. Rule enforcing activities in the public sector, when they can be clearly delineated, can become technical functions that may be outsourced to either domestic or foreign agents whoever can carry out the functions most effectively at lowest possible costs. Inviting a foreign national without local ties to head a rule enforcing agency clearly is an idea that may be tried more extensively.[33]

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32 In a somewhat different context, but on the basis of similar principles, the Korean national soccer team improved its performance by hiring a foreign coach, who did not have local ties to interest groups, which had hampered the team's effective functioning, by interfering in the team's management.

33 The asset of foreign rule implementers is their independence from domestic interest groups. Such an asset is useful not only for enforcing typical tax laws, regulations, and formulated budget, but also implementing some aspects of an agreed reform plan, in which domestic vested interest groups (e.g., not only specific industries, but also different ministries) might have divergent interests. As Addison (2003) suggests, foreign donors, in these cases, could help a country avoid getting stuck in a 'partial reform equilibrium'.

Government functions as a set of transactions

New institutional economics has given a new meaning to the firm as an organization. The new meaning allows economists to see what a firm does as a set of transactions, some of which the firm will continue to keep and the others it will outsource. If government functions are viewed as a set of transactions, guided by same principles in some respects as those governing markets and by different principles in some other respects, it is easy to see some rule enforcement functions may be outsourced. The following is a brief assessment of the Ugandan experience in this regard.

Uganda Revenue Authority

During the 1980s-90s, a number of African countries, including Ghana, Kenya, Uganda, and Tanzania, established national revenue authorities. An aim was to allow them to enforce tax laws as semi-autonomous agencies separate from the civil service, with higher remuneration and, thus with less incentives for corruption.

Uganda established the Uganda Revenue Authority (URA) in 1991 to enhance autonomy of tax collection. In 2001, the URA hired a foreign national, on a three-year contract, as its head (2001-04). Making the URA a semi-autonomous rule enforcement organization and appointing a foreign national to head the organization was a promising experiment. A contract with a clear set of result-oriented performance criteria would ensure how the outcome would be evaluated.

The URA has remained separate from the Ugandan civil service, and its staff has enjoyed higher salaries than the civil service. While there has been initial confusion, the URA has move into tax administration (rule enforcement) and away from tax policy formulation (rule making). This movement has been in line with the suggestions in this paper.

The experiment, however, has ended, perhaps prematurely, in the midst of confusion and controversies. The URA has not renewed the three-year contract with the expatriate commissioner-general, with some of the objectives remaining unfulfilled, in the view of the departing commissioner-general. The authorities are silent on how they view the outcome of the experiment and why the contract has not been renewed. Some assessments of this innovative experiment are available, although they are not focused on how successful the experiment was for nondiscretionary rule enforcement. While a thorough analysis of this experience in this regard would be useful, some of its initial lessons may be drawn.

The URA has focused more on mobilizing revenue than on nondiscretionary rule enforcement. This revenue objective is clear in its mission statement, compared with, for example, that of the US International Revenue Service.[34]

URA's mission:

> Maximizing central government tax revenue while optimizing resources utilization by ensuring a fair and equitable tax administration with a highly motivated and professional staff.

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34 Their respective homepages: www.ugrevenue.com and www.irs.gov.

US IRS's mission:

> Provide America's taxpayers top quality service by helping them understand and meet their tax responsibilities and by applying the tax law with integrity and fairness to all.

The URA's focus on revenue maximization and fairness as a public policy aim is understandable. Its focus on reducing corruption, while not explicit in its mission statement, is also a crucial objective. It may also be true that in Uganda, a most effective way to maximizing revenue mobilization and reducing corruption is to promote rules-based tax administration and to reduce discretion.

Revenue maximization, however, should be a policy objective—an objective that should be sought by rule-making government bodies. The role of URA as a rule enforcing agency should be to enforce tax laws as precisely, fairly, and efficiently as possible.

A number of reports on the URA experience have suggested that URA's revenue performances have been mixed: with a successful beginning, its revenue collections have since stagnated amid accusations of corruption. The URA management has prepared a corporate plan 2002/03-2006/07, aimed at raising the tax-to-GDP ratio from 11-12 per cent at present to 24 per cent in 2006/07.

The departing Commissioner-General, while suggesting that at present the URA has a potential of achieving 16 per cent of GDP, has noted that corruption is much more widely ingrained throughout URA than initially suggested. This assessment is in line with the findings that corruption and discretionary tax administration have cultural roots.[35]

More fundamentally, the experience of rule enforcement in Africa in general and tax administration in particular, seems to suggest culturally-conditioned discrepancies between *de jure* rules and *de facto* rules. The following conclusion of a study reinforces the new institutional economics' finding that imported formal institutions may not work as intended when they are not nested securely in hospitable informal norms.

> In Europe … the norms of the public service and the legal definitions of corruption correspond or harmonize, even if only appropriately, with the predominant socio-cultural logics. In Africa, on the contrary, there is a glaring discrepancy. As a result, the functioning of the administrative apparatus, entirely copied from the European pattern is a schizophrenic type. In law, official functioning, and budget, it is totally Western. In practice, it is otherwise, traversed by logics in drastic contradiction with the original model.[36]

These findings stress the need to have a broader approach to understanding and improving institutions in general and rule enforcement in particular.

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35 See Section 7 on 'Patronage and the 'cultural logics' of corruption', in Fjeldstad, Kolstad and Lange (2003).

36 Olivier de Sardan (1999), quoted in Fjeldstad, Kolstad and Lange (2003); Therkildsen (2003).

6 Summary and conclusions

Discretion in rule enforcement in collectivist societies is a problem that these societies must confront to enhance their economic performances. It is not easy to make progress in this regard because discretion has cultural roots and because cultural values change slowly.

This paper has presented a simple model that may be used to improve the understanding of how rule enforcement works in collectivist societies, where a rule of man is widespread, in comparison with how it works in individualist societies, where a rule of law tends to prevail. The paper has used the model to test the hypothesis that collectivist societies tend to be discretionary in rule enforcement in comparison with individualist societies. The test based on cross-country data supports the hypothesis.

The analytical results show the importance of individualist values (which discourage group thinking and uniformity of judgement)—as a source of low discretion—underpinning rule enforcement processes in countries where a rule of law prevails. The model shows exactly how separation of powers and multi-stage rule enforcement can reduce discretion. It also shows that, in the framework of the model in the paper, the number of stages does not have to be larger than two or three.

The paper suggests that a collectivist country can reduce discretion by establishing rule enforcement as a separate process from rule making, by ensuring the independence of rule enforcement from political and other interferences, and by instituting a proper multi-stage rule enforcement system. Establishing key rule enforcement activities as separate functions is not only feasible, but is also essential to keep them from political and other interference. Since rule-making activities are, and should be, political by their nature, having a system in which rule making and rule enforcing belong to a same agency headed by a same person would inevitably give rise to chances of political interference and chances of discretion in rule enforcing.

The paper uses the analytical framework to assess experiences aimed at establishing nondiscretionary rule enforcement systems, including the establishment of a nonpoliticized civil service, a result-oriented budget system, a programme budget, and a semi-autonomous revenue authority. Some countries with collectivist orientation are experimenting with independent revenue authorities mandated with revenue collection and headed by a foreign national. Considering that political pressure of vested interest groups who have personal ties with rule enforcers often are a primary source of discretion in rule enforcement in collectivist societies, a foreign national, with no personal ties with domestic interest groups and working with contracts with well-designed performance criteria, is less likely to be receptive to such pressure. These scattered experiments should be studied more thoroughly.

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