



## **The Convergence of Rules and Standards**

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**January 2001**

**RPP-2001-07**

### **Regulatory Policy Program**

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## **Citation**

This paper may be cited as: Schauer, Frederick. 2001. "The Convergence of Rules and Standards." Regulatory Policy Program Working Paper RPP-2001-07. Cambridge, MA: Center for Business and Government, John F. Kennedy School of Government, Harvard University. Comments may be directed to the author at John F. Kennedy School of Government, Harvard University, 79 JFK Street, Cambridge, MA 02138; Email [fred\\_schauer@harvard.edu](mailto:fred_schauer@harvard.edu).

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## The Convergence of Rules and Standards

Frederick Schauer<sup>1</sup>

Regulatory directives are an omnipresent feature of our social existence. Sergeants order privates to stand guard. Parents tell their children to be home by ten. The Commonwealth of Massachusetts says that drivers must drive at a speed no more than 65 miles per hour on the Massachusetts Turnpike, but the State of Montana until recently told drivers in that state only that they should drive at a “reasonable speed.” Congress instructs the Securities and Exchange Commission to make “rules and regulations governing registration statements and prospectuses,”<sup>2</sup> and the Securities and Exchange Commission then directs registrants to file “three copies of the complete registration statement”<sup>3</sup> on “good quality, unglazed, white paper no larger than 8½ x 11 inches in size, . . .”<sup>4</sup>

The directives that we observe in these and countless other instances come in various forms. The directives may be canonically inscribed, as with the provisions of the

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<sup>1</sup>Frank Stanton Professor of the First Amendment and Academic Dean, John F. Kennedy School of Government, Harvard University. Earlier versions of this paper were presented at the Association of American Law Schools Workshop on Administrative Law, at the Kennedy School of Government’s Seminar on New Directions in Regulation, and as a faculty colloquium at the Emory University College of Law. I am grateful for the comments of Mattias Kumm, Mark Miller, Cary Coglianese, and Richard Zeckhauser.

<sup>2</sup>Securities Act of 1933, §19(a).

<sup>3</sup>Rules and Regulations Under the Securities Act of 1933, Rule 402(a), 17 C.F.R. 230.402(a).

<sup>4</sup>Rules and Regulations Under the Securities Act of 1933, Rule 403(a), 17 C.F.R. 230.403(a).

Constitution, Acts of Congress and the rules of administrative agencies, or they may simply be announced, as with the typical command or instruction from a parent to a child or from a superior to a subordinate. The directives may be precise, as with “Speed Limit 65,” “All Workers Must Wear Hardhats that Meet the Specifications of OSHA Regulation 42.865(b),” and “No Person may be convicted of Treason unless on the Testimony of two Witnesses to the same overt Act,”<sup>5</sup> or they may be vague, as with “Drive Carefully,” “Award custody based on the best interests of the child,” and “[t]he right of the people to be secure . . . against unreasonable searches and seizures . . . shall not be violated.”<sup>6</sup> Directives may be enforced by frequent monitoring and inspections, as with the normal practices of the Occupational Safety and Health Administration, the Environmental Protection Agency, and the officials of the National Football League, or they may be enforced by the threat of ex post punishment, as with the laws against murder, rape, burglary, and littering. Enforcement of legal directives may take place through civil liability, as with most of American products liability law and much of American securities and antitrust regulation, or through the criminal law, as with the prohibitions on pickpocketing, child molestation, and price-fixing.

Through all of these permutations in regulatory strategy, a frequently heard theme is that the degree of specificity of the directive is a valuable tool in allocating decision-making authority among the rule-maker, the rule-follower, the rule-interpreter, and the rule-enforcer. Specific rules (“Speed Limit 65”) allow the rule-maker to make many of the decisions (and thus to determine the outcomes) in advance, and vaguer, less specific, rules, conventionally called “standards” (“Drive Carefully”), allow the rule-maker to delegate these decisions (and the determination of outcomes) to the rule-enforcer, the rule-interpreter, or the rule-subject, or all of them. According to the accepted wisdom, managing the degree of specificity of regulatory directives is an important instrument for controlling the amount of discretion that can be exercised by someone other than the original designer of the regulatory regime.

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<sup>5</sup>U.S. Const., Art III, §3, cl. 1.

<sup>6</sup>U.S. Const., amend. IV.

Implicit in the standard picture is a view about the importance of the form that a directive may take. Manipulating the form of the directive, so the conventional wisdom assumes, is a good way of managing discretion in a regulatory environment (including but not limited to courts) at the level of institutional design. That such manipulation is possible presupposes that the form of the directive selected by the designer or issuer of the directive makes a difference, and it makes a difference because the form of the directive is resistant to the preferences of those who are expected to interpret, enforce, and follow those directives.

But what if the form of a directive is less resistant than we have imagined? What if directives, regardless of the form in which they are set forth, may themselves be subject to modification in the hands of the very people or institutions they are intended to control and constrain? If this is so, then the choice of form of the directive may be less of a tool of regulatory strategy than is commonly supposed. The possibility that selecting the form of regulatory directives may be a less effective tool than is often imagined is the primary issue I seek to raise in this paper, guided and motivated by a specific reason for believing that the possibility I have just suggested is not only a logical possibility, but is an empirical reality as well. To use the accepted terminology, I want to suggest that the choice between rules and standards, the choice between specific and vague directives, may not make nearly as much of a difference as is ordinarily assumed. And this is not because there is no difference between rules and standards. There is a difference, but there may also be reason to believe that the adaptive behavior of decision-makers will push rules towards standards, and push standards towards rules. This is the phenomenon I call convergence, and it is the phenomenon whose logical contours and empirical occurrence provides the focus of the paper. If I am right in what I argue here, then much that we have previously thought about the distinction between rules and standards, and much that we have previously thought about the potential for choosing between them to serve regulatory or adjudicative goals, will need to be rethought.

1. Rules and Standards - The Conventional Wisdom

For the sake of familiarity, I will continue to refer to the distinction between specific and vague rules as the distinction between rules (specific) and standards (vague). The distinction has a moderately wide currency in legal theory,<sup>7</sup> and is no less problematic than other similar distinctions. Ronald Dworkin draws a related distinction between rules (like the Statute of Wills at issue in Riggs v. Palmer<sup>8</sup>) and principles (like the “no man may profit from his own wrong” principle at issue in the same case),<sup>9</sup> but Dworkin has a curious view about the non-overrideability of rules and the necessary overrideability of principles that confusingly conflates the dimension of specificity with the dimension of stringency.<sup>10</sup> Some theorists distinguish rules and norms,<sup>11</sup> but to many a norm is defined by the conditions of its emergence rather than by its form,<sup>12</sup> an issue that

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<sup>7</sup>See Larry Alexander and Emily Sherwin, The Deceptive Nature of Rules, 142 U. Pa. L. Rev. 1191 (1994); Alan Chen, Shadow Law: Reasonable Unreasonableness, Habeas Theory, and the Nature of Legal Rules, 2 Buff. Crim. L. Rev. 535 (1999); Louis Kaplow, Rules Versus Standards: An Economic Analysis, 42 Duke L.J. 557 (1992); Duncan M. Kennedy, Form and Substance in Private Law Adjudication, 89 Harv. L. Rev. 1685 (1976); Pierre Schlag, Rules and Standards, 33 UCLA L. Rev. 379 (1985); Kathleen M. Sullivan, The Supreme Court, 1991 Term - The Justices of Rules and Standards, 106 Harv. L. Rev. 22 (1976).

<sup>8</sup>22 N.E. 188 (N.Y. 1890).

<sup>9</sup>Ronald Dworkin, Taking Rights Seriously (1977).

<sup>10</sup>Dworkin claims that rules are both specific and applicable in an all-or-nothing fashion, while principles are non-specific and have the dimension of “weight.” But vague standards are sometimes non-overrideable (as with the Golden Rule), and specific rules (like speed limits) can sometimes be overridden in exigent circumstances. Dworkin mistakenly assumes that the sound distinction between the general and the specific is congruent with the equally sound distinction between the overrideable (*prima facie*) and the absolute, but we have no reason to believe that this congruence exists, either conceptually or empirically. See Frederick Schauer, Playing By the Rules: A Philosophical Examination of Rule-Based Decision-Making in Law and in Life (Oxford: Clarendon Press, 1991), pp. 12-14; Joseph Raz, “Legal Principles and the Limits of Law,” Yale Law Journal, vol. 81 (1972), pp. 823-54; Colin Tapper, “A Note on Principles,” Modern Law Review, vol. 34 (1971), pp. 628-34.

<sup>11</sup>George C. Christie, Law, Norms and Authority (London: Gerald Duckworth and Co., 1982).

<sup>12</sup>Edna Ullman-Margalit, The Emergence of Norms (Oxford: Clarendon Press,

is of little concern in this context. So although the distinction between rules and standards is not free of difficulties,<sup>13</sup> it will serve moderately well for our purposes here.

Under the conventional picture of the distinction between rules and standards, a rule is quite specific, as with “Speed Limit 55,” as with most of the provisions of the Internal Revenue Code, and as with some of the criminal procedure provisions of the Constitution of the Republic of South Africa, one of which provides that:

“Every person arrested for the alleged commission of an offence shall . . . have the right as soon as it is reasonably possible, but not later than 48 hours after the arrest or, if the said period of 48 hours expires outside ordinary court hours or on a day which is not a court day, the first court day after such expiry, to be brought before an ordinary court of law and to be charged or to be informed of the reason for his or her further detention, failing which he or she shall be entitled to be released.<sup>14</sup>

No rule, of course, can be infinitely specific. Neither our world nor our language can provide an airtight seal against unimagined or unimaginable contingencies, a phenomenon that has for centuries or longer been a staple of literature. Shakespeare teased us with “No man of woman born.”<sup>15</sup> The philosopher J.L. Austin asked us to

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1977).

<sup>13</sup>Foremost among them is the way in which the distinction might be taken to suggest that rules are more constraining than standards without reference to the decisions that might otherwise be taken by some decision-maker. For a decision-maker inclined always to give custody to the mother, a directive to make those decisions “in the best interests of the child” might be quite constraining, cutting off a high proportion of otherwise eligible outcomes. Conversely, “Speed Limit 90” would for most of us not be especially constraining, and might even be less constraining than “Drive With Extreme Caution.” To say that a rule is more constraining than a standard makes sense only against a background of a stipulated equivalence of antecedent preferences for the rule-follower, and only against a background of rough equivalence between the substantive content of the rule and the center of gravity of the substantive content of the standard.

<sup>14</sup>Republic of South Africa Constitution, chapter III, §25(b)(2).

<sup>15</sup>Macbeth, Act IV, scene I, line 79.

imagine what we would do when confronted with an “exploding goldfinch.”<sup>16</sup> And of course the unimagined or unprovided-for case has pervaded legal theory for centuries. As long ago as the 16<sup>th</sup> century Samuel Pufendorf asked us to imagine what would happen if we were to prosecute a surgeon performing emergency surgery under an anti-dueling law prohibiting “letting blood in the streets.”<sup>17</sup> More recently, and equally famously, Lon Fuller relied heavily on examples like the respectable but tired commuter prosecuted under a “No Sleeping in the Railway Station” enactment for nodding off while waiting for his train,<sup>18</sup> the starving explorers prosecuted for murder for conducting a lottery to determine which of their number the others should consume,<sup>19</sup> and the military truck incorporated into a war memorial which might have been deemed to violate the “No Vehicles in the Park” rule.<sup>20</sup> As H.L.A. Hart put it, all rules necessarily have a core of settled meaning surrounded by a penumbra of uncertainty.<sup>21</sup>

Yet although the penumbra of uncertainty is ineliminable, the comparative specificity of numerous rules is quite apparent. While there are circumstances in which I could imagine contesting the Internal Revenue Service over an interpretation of the fringes of the April 15<sup>th</sup> filing deadline, it would be implausible to imagine that in the normal course of things I could argue that May 3<sup>rd</sup> falls within the deadline. If the deadline were to be specified simply as “as soon as reasonably possible after the close of the tax year,” I could imagine making a case for May 3, and I could also imagine the

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<sup>16</sup>J.L. Austin, “Other Minds,” in Philosophical Papers, 3d. ed., J.O. Urmson & G.J. Warnock, eds. (Oxford: Oxford University Press, 1979), pp. 76-116.

<sup>17</sup>S. Pufendorf, De Jure Naturae et Gentium Libri Octo, quoted in *United States v. Kirby*, 74 U.S. (7 Wall.) 482, 487 (1968).

<sup>18</sup>Lon L. Fuller, Positivism and Fidelity to Law - A Reply to Professor Hart, 71 Harv. L. Rev. 630, 664 (1958).

<sup>19</sup>Lon L. Fuller, The Case of the Speluncean Explorers, 62 Harv. L. Rev. 616 (1949).

<sup>20</sup>Lon L. Fuller, Positivism and Fidelity to Law, supra note 19, at 663.

<sup>21</sup>H.L.A. Hart, The Concept of Law (Oxford: Clarendon Press, 1961).

Internal Revenue Service making the case that February 1 was late, but both of these positions are, in almost all imaginable cases, precluded by the specificity of the April 15<sup>th</sup> rule.

In contrast to rules, therefore, what are commonly referred to as “standards” make few of the decisions at the rule-making level, and leave most of them to be made at the point and time of application to some concrete set of facts. Famously, the Constitution of the United States contains numerous standards. Unlike the highly specific criminal procedure provisions of the Constitution of South Africa, the criminal procedure provisions of the United States Constitution contain elements such as “unreasonable searches and seizures,” “due process of law,” “speedy and public trial,” “excessive bail,” and “cruel and unusual punishments.” Other parts of the Constitution purport to prohibit the “establishment of religion” and “abridging the freedom of speech,” and guarantee “the privileges and immunities of citizens of the United States” and “the equal protection of the laws.” Similarly, the most common directive to judges in custody disputes instructs the judges to make the decision that is “in the best interests of the child,” and the text of the Sherman Antitrust Act prohibits “contracts, combinations, and conspiracies in restraint of trade.”

Just as rules are not infinitely specific, nor are standards infinitely vague. “In the best interests of the child” is likely more constraining of the decision-maker than “the decision that is best, all things considered,” a prohibition on “unreasonable searches and seizures” and “excessive bail” has more content than a requirement of “justice” in criminal prosecutions, and the prohibitions of the Sherman Act have more content than would a mandate to ensure “fairness” in all business dealings. Still, the maximum amount of specificity can be thought of as representing one end of a scale, and the maximum amount of vagueness can be thought of as representing the other. Conventionally, the directives that are on the specific end of the scale are referred to as “rules” and the directives that are on the vague end of the scale are referred to as “standards.” And although there will of course be difficult intermediate cases, the existence of such cases no more undercuts the distinction between rules and standards

than does the existence of dusk undercut the distinction between night and day.

The choice of rules over standards, or vice versa, is often thought to be an important part of the regulatory arsenal. One reason for this, less important for my purposes here, is that rules made in advance tend to be blunt instruments, grouping the virtually infinite variation in the human experience under easily accessible headings. “Speed Limit 55” may dampen important variations in driving ability, traffic, weather, and road conditions, but people are still on notice as to what is required. Consequently, it is often thought that rules bring the virtues of predictability and mechanical application at some cost to the possibility of producing the optimal result or the maximum amount of justice in the individual case, and that standards increase the likelihood of case-based optimization, but at some cost to the possibility of predicting in advance what the result is likely to be.<sup>22</sup>

More importantly, at least in this paper, is that rules are commonly thought to be the instruments of constraining discretion, while standards, conversely, are thought to be the instruments of granting discretion. A judge who is instructed to reach the decision that is “in the best interests of the child” still has considerable discretion in making her decision, while a judge who by contrast is instructed to award custody to the mother in all cases in which the mother has not previously been convicted by an American court of a felony is being asked to make a decision that could in most cases be made by a clerk, or even by a computer. A soldier who is ordered to “guard the fort” has more discretion than one who has orders to stand in a particular place for a particular period of time, and an inspector of the Environmental Protection Agency who is charged with ensuring “clean air” has more discretion than one who must determine whether the emissions of a specified chemical at a specified manufacturing facility are above a specific and pre-determined numerical maximum.

As a result of this distinction between granting and constraining discretion, an

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<sup>22</sup>For an exhaustive analysis, see Schauer, Playing By the Rules, op. cit.

important question of regulatory strategy has often been thought to be the question of how much discretion the rule-maker should give to others, regardless of whether those others are rule-appliers such as inspectors or police officers, or rule-interpreters such as judges, or rule-followers such as members of the public whose behavior is constrained by the directive. If the rule-maker (in a different sense of “rule”) wishes to grant considerable discretion, she will use standards, and if she wants to constrain that discretion, she will employ rules. The decision to employ rules rather than standards, or vice versa, or the decision to employ more and less rule-based approaches, is thus ordinarily thought to be one of the important tools in the regulatory toolbox.

## II The Avoidance of Rules

Implicit in this conventional picture, however, is a view about the distinction between rules and standards that may when applied not accurately depict our empirical and normative reality. The alternative picture I wish to offer, and eventually (but not here) test, is what I will call the convergence hypothesis. According to the convergence hypothesis, rule-appliers, rule-interpreters, rule-enforcers, and rule-followers all have available to them, even under a regime of crisp rules, a battery of rule-avoiding devices. The effect of the availability of these rule-avoiding devices is to grant to the rule-appliers, rule-interpreters, rule-enforcers, and even rule-followers more discretion in practice than the crispness of the rule itself would indicate. Conversely, rule-appliers, rule-interpreters, rule-enforcers, and rule-followers who are given open-ended standards will to satisfy their own preferences for certainty and simplicity frequently supplement those standards with relatively determinate heuristic rules, the consequence of which is that standards may produce less case-by-case discretion than the open-ended nature of the standard itself would have suggested. And insofar as the degree of recourse to rule-avoiding devices is directly correlated with the determinacy of the rules, and insofar as the degree of recourse to self-imposed heuristic rules is directly correlated with the indeterminacy of standards, we can expect to see a phenomenon in which the rules tend towards standards, and the standards tend towards rules. This is the phenomenon I label “convergence,” and

this is the phenomenon I hope in this paper to elaborate at greater length.

Consider first the possibility that rules will tend towards standards, and in this connection consider the various ways in which even the most specific rules may be avoided. One way is for the rule-enforcer or rule-interpreter to engraft an exception to the rule at the moment of its application.<sup>23</sup> If a faculty's rules require all of its members to have doctoral degrees, and if an extraordinarily successful candidate embarked on what has become a prize-winning academic career before completing his dissertation, the faculty might be willing, when faced with this candidate, and even when there is no apparent authorization for making an exception, to create an exception in just this case, the faculty promising to itself that it will never again, are almost never again, make an exception to its rules. Thus, insofar as even facially exception-less rules are understood in a decision-making environment to be permissibly open to the creation of ad hoc exceptions when the exception-less rule confronts a case not envisaged by the rule itself, and in which the rule would generate would appear at the time to be an erroneous result, what looks at first glance like a crisp and rigid rule is in practice less crisp and less rigid than we might suspect, and is in practice more granting of discretion than the literal formulation of the rule itself would appear to indicate.<sup>24</sup>

The creation of ad hoc exceptions is not the only strategy of rule-avoidance. Another is to take any rule to be subject to a "reasonableness" qualification. The Delaney Clause, a statutory section famous in the American literature on statutory interpretation, appears on its face to prohibit the use as food additives of all substances that produce any increase in the likelihood of cancer, but some would say that this absolute prohibition on substances that increase the likelihood by only a minuscule amount is so unreasonable that it should not be interpreted as literally written.<sup>25</sup> To the extent that rule-enforcers

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<sup>23</sup>See Alfred C. Aman, Jr., Administrative Equity: An Analysis of Exceptions to Administrative Rules, 1982 Duke L.J. 277.

<sup>24</sup>See Frederick Schauer, Exceptions, 58 U. Chi. L. Rev. 871 (1991).

<sup>25</sup>Cass R. Sunstein, "Interpreting Statutes in the Regulatory State," Harvard Law Review, vol. 103 (December 1989), pp. 405-508, at p. 423.

and rule-interpreters may permissibly enforce or interpret rules so as to avoid an unreasonable application, and to the extent that there is a wide understanding of what may count as an “unreasonable” application,<sup>26</sup> then the implicit authorization to rule-enforcers and rule-interpreters to test the rules against a reasonableness standard turns out to grant the rule-enforcers and rule-interpreters a quite wide range of discretion.

A third strategy of rule-avoidance is to take even the most specific rule to be subject to override by various considerations external to the rule itself. When the police officer who stops me for driving at 75 in a 55 miles per hour zone sees that I have an injured person in the car and that I am heading for the hospital, he is likely to take the emergency, even if nowhere specified in the rules he is charged to enforce, as overriding the rules that he is assigned to enforce and that I am ordered to obey. When the Supreme Court of the United States announces that even the facially non-overrideable mandates of equal protection of the laws may be overridden in cases of “compelling interest,”<sup>27</sup> it is similarly recognizing that in some legal environments it is permissible to treat all rules as subject to override in exigent circumstances even if the possibility and permissibility of override is nowhere mentioned in the formal law.<sup>28</sup>

Fourth, rule-enforcers and rule-interpreters will often depart from the specificity of a rule in order to rely on its less specific purpose. Now it is not always the case that the purpose (or justification, or rationale) behind a rule is less specific than the rule itself. Sometimes the rationale may be based on a concrete example, and a less concrete rule is

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<sup>26</sup>This is crucial. There is a large distinction between the view that only true absurdities may count as unreasonable, as in the traditional “Golden Rule” of statutory construction, and the view that a wide range of sub-optimal applications and policies may legitimately be considered to be unreasonable. See Frederick Schauer, The Practice and Problems of Plain Meaning, 45 Vand. L. Rev. 715 (1992).

<sup>27</sup>*Korematsu v. United States*, 323 U.S. 214 (1944). See also *Loving v. Virginia*, 388 U.S. 1 (1967); *City of Richmond v. J.A. Croson Co.*, 488 U.S. 469 (1989).

<sup>28</sup>See Frederick Schauer, Can Rights Be Abused?, 29 Phil. Q. 229 (1981).

written in order to make the rule itself broader than the concrete example that inspired it.<sup>29</sup> More commonly, however, specific rules embody less specific purposes, as when, canonically, the “No Vehicles in the Park” rule is written in order to instantiate a more general purpose of achieving quiet and decorum in public parks. But when in such cases the rule-enforcer or rule-interpreter is permitted to expand (noisy non-vehicles) or contract (non-noisy vehicles) the rule by reference to its purpose, it turns out that the purpose and not the rule is doing the work.<sup>30</sup> When this happens, it is fair to conclude that the recourse to purpose is still another way of avoiding the crispness and determinacy often associated with rules themselves.

This catalog of rule-avoiding strategies is illustrative and not exhaustive. There are others, and my point is only that in various circumstances we can imagine a rule-enforcer, rule-interpreter, or rule-applier using one or more of these rule-avoiding strategies or devices to ameliorate what might otherwise be the stringent effect of a rule in a particular case. Insofar as these strategies or devices are available, it then turns out that what might otherwise look like a discretion-constraining rule is in practice more of a discretion-permitting standard. Insofar as any or all of the various rule-avoiding strategies are permissible, an issue to which I will turn presently, rules may resemble standards, or be made to operate as standards, more than may be apparent from the face of the rule.

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<sup>29</sup>Perhaps a good example is the way in which the Equal Protection Clause of the Fourteenth Amendment makes no reference to race or color.

<sup>30</sup>See Frederick Schauer, Formalism, 97 Yale L.J. 509 (1988).

### III The Concretization of Standards

Now consider the opposite phenomenon, under which broad and vague standards may in practice come to operate in more rule-like fashion. Standards appear to many people to have an uncomfortable vagueness about them. They leave discretion, to be sure, but they give little guidance, and require even a discretion-appreciating rule applier to engage in a broader range of calculations and assessments in each case than she might wish. Not every decision-maker wishes this freedom,<sup>31</sup> and not every decision-maker has the time, the energy, or the inclination to engage in the “from the ground up” process that unconstrained discretion and unspecified standards require.

As a consequence of the numerous reasons of time, energy, and psychology that would lead nominally unconstrained decision-makers to constrain themselves more than others would wish to constrain them, it is possible that rule-enforcers, rule-interpreters, and rule-appliers, even if they in theory enjoy the considerable discretion granted to them, will supplement the standards with more specific “guidelines” or “rules of thumb” that in practice have all of the characteristics of rules. When faced with the vagueness of the Sherman Antitrust Act, American courts have developed a series of “per se rules,” such as the rule against price-fixing and the rule prohibiting tying arrangements, that provided guidance and that limited discretion far more than would have been the case with direct application of the vague language of the Sherman Act to each individual case.<sup>32</sup> Similarly, the Supreme Court’s decision in Miranda v. Arizona<sup>33</sup> specifies

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<sup>31</sup>See, among numerous explorations of the circumstances in which freedom may be seen by people to be a mixed blessing, Fyodor Dostoevsky, *The Grand Inquisitor*, in *Notes from Underground and Grand Inquisitor* (Ralph E. Matlaw ed. 1960).

<sup>32</sup>See, e.g., *Palmer v. BRG of Georgia, Inc.*, 498 U.S. 46, 49 (1990); *Broadcast Music, Inc. v. CBS*, 441 U.S. 1, 7-8 (1979); *Klor’s, Inc. v. Broadway-Hale Stores*, 359 U.S. 212 (1959); *Northern Pacific Railroad Co. v. United States*, 356 U.S. 1, 5 (1958); *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150 (1940).

<sup>33</sup>384 U.S. 436 (1966).

essentially the exact language that police officers should use when interrogating a suspect, and the Court's frequent use of three- (and sometimes four-) part tests in freedom of speech<sup>34</sup> and freedom of religion<sup>35</sup> cases exemplifies an urge to make things more concrete, more specific, and more rule-like than the standard-like constitutional text would otherwise suggest. In practice, the Constitution of the United States and the Sherman Act are far more affairs of rules than one would think by looking only at the primary texts.<sup>36</sup>

Standards may come to resemble rules in less direct ways as well. When a court says that a vague standard incorporates the common law, or incorporates a statute, it is in effect importing a specific rule from outside of the non-specific standard in order to make the non-specific standard more specific. When Justice Hugo Black maintained that the quite non-specific Due Process Clause of the Fourteenth Amendment incorporated by reference all and only the (relatively) more specific guarantees of the Bill of Rights,<sup>37</sup> he was indulging his own preference for specificity by finding something more specific that ameliorated his discomfort with the less specific standard he had been asked to interpret. And when American courts hold that a legislative remedy containing no statute of limitations is to be understood as importing the statute of limitations from a similar cause of action it is again using something external to a standard to make the standard come to resemble a rule.

Standards also come to resemble rules when decisions made under standards are taken as having precedential effect for future decisions under the same standard. When

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<sup>34</sup>See *Central Hudson Gas & Elec. Co. v. Public Service Commission*, 447 U.S. 557 (1980); *United States v. O'Brien*, 391 U.S. 367 (1968).

<sup>35</sup>*Lemon v. Kurtzman*, 403 U.S. 602 (1971).

<sup>36</sup>Whether this is a good thing is deeply contested. Compare Morton J. Horwitz, Foreword: The Constitution of Change: Legal Fundamentality Without Fundamentalism, 107 Harv. L. Rev. 30 (1993), with Frederick Schauer, Opinions as Rules, xx U. Chi. L. Rev. xxx (1995).

<sup>37</sup>See *Adamson v. California*, 332 U.S. 46 (1947 (Black, J., dissenting)).

standards are truly the devices of maximal discretion, decisions under those standards would not constrain future decisions, because constraint by precedent is itself a form of constraint by rule.<sup>38</sup> But when standards are supplemented by precedential constraint, that constraint serves to convert the standard into a standard instantiated by the decisions under it, and this instantiation, insofar as it has precedential weight, makes the standard more like a rule. Just as rules may in practice come to resemble standards, so too, therefore, may standards come to resemble rules.

#### IV The Potential for Convergence

Implicit in all of the foregoing is the possibility, and I describe it so far only as a possibility, of what I call convergence. If the adaptive behavior of rule-appliers, rule-followers, rule-enforcers, and rule-interpreters can make rules more standard-like than they appear, and can also make standards more rule-like than they appear, then the possibility is open that rule-appliers, rule-followers, rule-enforcers, and rule-interpreters would approach (although probably not reach) the same point on the rule-standards continuum regardless of whether they were given rules or standards as their starting raw material.<sup>39</sup> The convergence hypothesis offers as a hypothesis that this convergence, this gravitation towards the same degree of rule-ness (or standard-ness, if you will), regardless of the starting point, will occur, and that this will produce a world in which the choice between rules and standards makes far less difference<sup>40</sup> than is generally supposed to be the case. And if this is so, then it may be that the tool of regulatory specificity as a way of managing discretion is less a part of the toolbox of regulatory strategy and institutional design than has historically been thought to be the case.

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<sup>38</sup>See Larry Alexander, Constrained By Precedent, 63 S. Cal. L. Rev. 1 (1989); Frederick Schauer, Precedent, 39 Stan.L. Rev. 571 (1987).

<sup>39</sup>The parallels with the Coase Theorem are obvious.

<sup>40</sup>That it makes no difference at all can probably not be established.

But although the possibility I describe appears plausible, is there any reason to believe that the convergence hypothesis is true? One such reason starts with the fact that there are identifiable differences among legal cultures in views about the desirability and rigidity of rules. In some legal cultures, it is generally understood that rules should be read literally, that the appliers and interpreters of rules should not be empowered to modify the rules at the point of application, that judges should interpret rules according to their ordinary meaning except in the most egregious cases, and that the virtues of specificity and predictability are more important, especially within the legal system, than the virtues of flexibility in the face of changing or unforeseen circumstances. In these societies, the devices of rule-amelioration are either absent or scorned.

In other legal systems, by contrast, the virtues of ruleness and formality are less apparent, and it is widely accepted that reaching the correct outcome in the individual case is more important than the virtues brought by rigid obedience to specific rules. In these societies, the rule-ameliorating devices, rather than being scorned, are celebrated, and rule-interpreters, rule-enforcers, and rule-appliers who refuse to employ these devices are typically castigated as “mechanistic,” “formalistic,” and the like.

As should be apparent, there is a widespread view, supported by some moderately serious research,<sup>41</sup> that the United States is the best example of the latter, and that most other advanced legal systems are closer to the former than is the United States. Indeed, an anecdotal example of this is provided by a book entitled A Common Law for the Age of Statutes,<sup>42</sup> in which Guido Calabresi argued that judges have (or should have) the power to update obsolete statutes, even at some affront to the language of those statutes, if updating would make the statutes better able to handle current problems not imagined at the time of drafting. The important thing about this book is not whether it is right or wrong, descriptively or prescriptively. Rather, it is that the author, at the time of writing

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<sup>41</sup>See P.S. Atiyah and R.S. Summers, Form and Substance in Anglo-American Law: A Comparative Study in Legal Reasoning, Legal Theory and Legal Institutions (Oxford: Clarendon Press, 1987).

<sup>42</sup>Cambridge, Massachusetts: Harvard University Press, 1982.

Professor of Law at the Yale Law School, is now a judge of the United States Court of Appeals for the Second Circuit. Even holding the nomination and confirmation procedures constant, it is hardly unlikely that in numerous countries throughout the world writing a book with this message would have been a permanent disqualification from the judiciary, yet that is plainly not the case in the United States.

For present purposes, my characterization of the United States, or any other legal culture for that matter, is relatively unimportant. What is important is the idea that if countries can vary in their legal cultures' attitudes about the appropriate degree of ruleness, then it would not be surprising to discover that within a legal culture there were prevailing views, independent of the goals and substance of particular rules or regulatory schemes, about where on the rules-standards continuum it would be good to wind up. In other words, it may well be the case that rule-appliers, rule-enforcers, and rule-interpreters within a given legal (or regulatory) culture would have a set of background beliefs about the extent to which rules as opposed to standards are a good thing, and thus a set of background beliefs about the desirability of making standards more specific, and rules more flexible. Consequently, it would be plausible to imagine that rule-enforcers, rule-interpreters, and rule-appliers, when confronted with a rule, would try to make it conform to their background views about flexibility, and when confronted with a standard would try to make it conform to their background views about the appropriate degree of rigidity, specificity, and inflexibility.

## V Insider Trading and the Possibility of Convergence

That which is logically possible and empirically plausible is still not necessarily true. In this final section of the paper I want to describe an inquiry designed to examine empirically the possibility that the convergence hypothesis might be confirmed.

Ideally, it would be desirable, within a given legal culture, to be able to examine a rule and a standard in order to determine whether the standard had been made more rule-

like in application, and the rule more standard-like in application. And, ideally, it would be desirable to try to do this with substantively equivalent statutes, in order to exclude the possibility that rule-interpreters would think that rules are appropriate for one form of regulation and standards appropriate for another. But since it would be hard to imagine why any legal culture would have two different types of directives for the same problem, it is obvious that this optimal case study is not going to be found.

In the United States, however, we do have a paired set of legal directives that might work as a plausible substitute. Consider first Section 16b of the Securities and Exchange Act of 1934.<sup>43</sup> In order to deal with the particular form of insider trading known as “short-swing profits,” this provision, designed to “prevent[] the unfair use of information which may have been obtained by [a] beneficial owner, director, or officer by reason of his relationship to the issuer,” requires individuals in these categories to disgorge to the company any profits made by virtue of a purchase and sale or sale and purchase of the company’s securities within a six-month period. For our purposes here, what is most important about this provision is its stark rule-like quality. Described even in the 1934 congressional hearings that led to its passage as a “crude rule of thumb,”<sup>44</sup> this provision defines short-swing profits as a profit made as a result of a purchase and sale or sale and purchase “within any period of less than six months . . . irrespective of any intention on the part of such beneficial owner, director, or officer in entering into such transaction of holding the security purchased or of not repurchasing the security sold for a period exceeding six months.” Moreover, the provision applies to all officers, all directors, and anyone “who is directly or indirectly the beneficial owner of more than 10 per centum of any class of any [registered] security.” According to the language of Section 16b, all officers, directors, and 10 per cent owners are prohibited from taking profits in a period of less than six months, regardless of actual insider knowledge, and regardless of intent. If the owner of 9.9% of the stock, not being an officer or director,

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<sup>43</sup>15 U.S.C. §78p(b).

<sup>44</sup>See Thomas Lee Hazen, The Law of Securities Regulation (St. Paul, Minnesota: West Publishing Company, 1985), p. 414.

trades on inside information with the intention of capitalizing on the ignorance of others, there is no violation. So too if an officer, director, or 10 per cent owner buys and sells or sells and buys in six months and one day. And if the owner of 10.1% of the stock, having no inside information, buys and sells or sells and buys in a period of one day less than six months, the statute is violated.

Now consider a quite different provision designed also to deal with the problem of insider trading, Rule 10b-5 of the Securities and Exchange Commission,<sup>45</sup> promulgated pursuant to Section 10b of the Securities and Exchange Act of 1934. This provision, although intended to deal with problems not dissimilar to the problems at which Section 16b is aimed, is drafted in a quite different way. One of its three brief operative provisions makes it unlawful “to employ any device, scheme, or artifice to defraud,” and another makes it unlawful “to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person.” Even the remaining provision is not much more specific, making it unlawful “to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading.” Just as Section 16b is moderately close to the rules end of the rules-standards continuum, Rule 10b-5 is just as close to the standards end.

If the standard picture of the consequences of choosing rules over standards, or vice versa, were correct, we would expect under Section 16(b) to see not much litigation, and to see decisions by both the primary interpreter (the Securities and Exchange Commission) and the courts that tracked the mechanistic nature of the statute. And we would expect to see decisions under Rule 10b-5 that were largely case-specific, much like the largely case-specific decisions we see under something like the “best interests of the child” standard.

It turns out, however, that just the opposite is the case. With respect to Section

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<sup>45</sup>17 C.F.R. § 240.10b-5.

16(b), there appears to be far more litigation than one would expect from such a precise statute,<sup>46</sup> even taking into account the special incentives to litigation produced by an enforcement scheme that relies heavily on a variant of the privately-initiated stockholder derivative suit. And, more importantly, both the Securities and Exchange Commission and the courts appear actively to be pressing against the rigidity of the statute, the effect being that the rule is operating more as a standard than might have been predicted in, say, 1934. For example, the SEC has administratively added a number of exceptions to the operation of the statute, almost all of which appear designed to prevent penalizing innocent shareholders whose stock transactions are part of employee benefit plans, large block transactions in connection with a distribution of securities, various stock conversions, many transactions that are part of mergers and acquisitions, and numerous other transactions that would have been covered by the “crude rule of thumb” had it not been for the proclivity of the SEC to make continuous exceptions when they become aware that the rigidity of the rule is reaching a transaction not likely to involve trading on inside information.

This same tendency to ameliorate the ruleness of Section 16(b) appears to exist in the courts as well. “Notwithstanding the clear congressional intent to provide a catch-all, prophylactic remedy, not requiring proof of actual misconduct, the statute is not always strictly applied.”<sup>47</sup> For example, whenever the transaction is the least bit unorthodox,<sup>48</sup> or whenever there is even the slightest question about the application of the relevant time periods,<sup>49</sup> the courts have abandoned the rule-based approach and have instead looked at the individual transaction in order to determine whether there has actually been some risk or realization of speculation on inside information. In defining “officer” and “director,”

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<sup>46</sup>See Hazen, op. cit.

<sup>47</sup>Ibid.

<sup>48</sup>E.g., *Kern County Land Co. v. Occidental Petroleum Corp.*, 411 U.S. 582, 594 n.24 (1973); *Pier 1 Imports of Georgia, Inc. v. Wilson*, 529 F. Supp. 239 (N.D. Tex. 1981).

<sup>49</sup>See *Gold v. Sloan*, 486 F.2d 340 (4<sup>th</sup> Cir. 1973).

the courts have tended not to look at who holds the formal title within the organization, but have looked in a more functional way at what various individuals actually do,<sup>50</sup> an approach that brings the benefits of fairness in individual cases, but at the cost of the very ruleness that Section 16(b) was originally designed to achieve. Indeed, the entire history of Section 16(b) litigation has been one of pressing against, and at times abandoning, the rule-based approach, substituting an approach that numerous commentators have labeled “pragmatic.”<sup>51</sup> In practice, therefore, Section 16(b), designed as a rule, has been increasingly taking on all of the earmarks of a standard.

When we look at Rule 10b-5, we see a very different phenomenon. The courts have filled in the rule’s uncertainty about standards of liability with relatively concrete references to common law standards of intentional wrongdoing.<sup>52</sup> So too with the importation of common law ideas, much more historically well-developed than Rule 10b-5 standards, about causation, reliance, and materiality.<sup>53</sup> Indeed, the much-discussed “fraud on the market” theory<sup>54</sup> can be understood, in part, as a rule-based approach that avoids the necessity of the kind of individualized proof that one would expect under a more standards-based approach. In assessing damages, the courts have looked to create

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<sup>50</sup>See *Colby v. Klune*, 178 F.2d 872 (2d Cir. 1949); *Selas Corp. of America v. Voogd*, 365 F. Supp. 1268 (E.D. Pa. 1973).

<sup>51</sup>See Hal Bateman, “The Pragmatic Interpretation of Section 16(b) and the Need for Clarification,” *St. John’s Law Review*, vol. 45 (1971), pp. 772-809; Thomas Lee Hazen, “The New Pragmatism Under Section 16(b) of the Securities Exchange Act,” *North Carolina Law Review*, vol. 54 (1975), pp. 1-57; Weinstock, “Section 16(b) and the Doctrine of Speculative Abuse: How to Succeed in Being Subjective Without Really Trying,” *Business Lawyer*, vol. 29 (1974), pp. 705-26; Wentz, “Refining a Crude Rule: The Pragmatic Approach to Section 16(b) of the Securities exchange Act of 1934,” *Northwestern University Law Review*, vol. 70 (1975), pp. 221-54.

<sup>52</sup>The technical term is scienter. See *Ernst & Ernst v. Hochfelder*, 425 U.S. 185 (1976); *Aaron v. SEC*, 446 U.S. 680 (1980). See also Douglas Branson, “Statutory Securities Fraud in the Post-Hochfelder Era: The Continued Viability of Modes of Flexible Analysis,” *Tulane Law Review*, vol. 52 (1977), pp. 50-84.

<sup>53</sup>See *List v. Fashion Park, Inc.*, 340 F.2d 457 (2d Cir. 1965).

<sup>54</sup>See *Zweig v. Hearst Corp.*, 594 F.2d 1261 (9<sup>th</sup> Cir. 1979).

moderately consistent rules,<sup>55</sup> and so too with many of the “procedural” dimensions of application of Rule 10b-5. Even more importantly, the application of Rule 10b-5 to insider trading issues has been marked by attempts to define in or out of the scope of the rule various classes of people (as with “tippees”) and various classes of information (as with “market information”<sup>56</sup>), the effect of which is to move Rule 10b-5 rapidly in the direction of a rule, with all of the caveats, qualifications, exceptions, definitions, and similar apparatus that we normally associate with rules but do not associate with standards.

Section 16(b) and Rule 10b-5 have obviously not become identical. They operate in different ways, and there is at least some path-dependence in the development of the doctrines that surround them. Still, it is hard to deny that the general trend of interpretation of Section 16(b) has been to make it more standard-like, and the general trend of interpretation of Rule 10b-5 has been to make it more rule-like, even though the two started in different places, and even though the two deal with the same large problem of insider trading.

These developments are surprising. Although there will inevitably be occasions for interpretation and litigation under any directive, one might have expected courts and other interpreters to take seriously Section 16(b)’s rule-like character and thus be unwilling to detract from that character by the addition of exceptions, qualifications, and opportunities to look at the real character of the entire transaction. And one might have expected courts and others to recognize Rule 10b-5’s inherent flexibility and thus be reluctant to engraft onto it various rules, categories, and well-understood common law doctrines. Yet in both cases these expectations have not been satisfied, and instead we have seen what appears on preliminary analysis to be a good example of the convergence phenomenon. What we have seen is a persistent tendency of courts and regulators to make the rule more standard-like and the standard more rule-like, plausibly guided in

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<sup>55</sup>E.g., *Osofsky v. Zipf*, 645 F.2d 107 (2d Cir. 1981).

<sup>56</sup>See *Chiarella v. United States*, 445 U.S. 222 (1980).

both cases by background beliefs about the desirable or optimal degree of ruleness in any regulatory regime.

## VI Testing the Convergence Hypothesis

The above analysis of Section 16(b) and Rule 10b-5 is preliminary and impressionistic, and awaits more careful empirical research. And even if it turns out that we have seen convergence in this area, it would be necessary to examine many others in order to make more substantial claims about the truth of the convergence hypothesis generally, as opposed to its truth in this or that substantive area. Still, there may be other fruitful areas to examine. Some college and university honor codes, especially the oldest ones, are highly open-ended, doing little more than prohibiting lying, cheating, and stealing. Others, especially more recent ones, are highly detailed, resembling the Internal Revenue Code more than they resemble the honor codes of the early 19<sup>th</sup> century. It is possible, therefore, that examination of the interpretation of such codes could illuminate us about the convergence hypothesis that would suggest a proliferation of ameliorating devices for the precise codes, and a proliferation of sub-rules for the more general ones. Similarly, many new constitutions, as with the South African example noted above, are far more highly detailed and more rule-like than the Constitution of the United States. Subject to all of the special problems of comparative analysis, where the volume of variables makes firm conclusions elusive, it will be instructive to examine trends, and to see if the interpretation of constitutions in general, or of specific provisions of constitutions, also exhibit the phenomenon of convergence.

It may turn out that there is no basis for the convergence hypothesis. But if it turns out that it is true, this could have important implications for institutional design and the design and management of regulatory instruments and institutions. If background understandings about the appropriate degree of flexibility of rules can push with some force against the rule-makers design of those rules, then the design of rules, and the choice between rules and standards, may make much less difference than often supposed.

And if this is the case, then efforts now spent on rule design might better be spent on the creation of incentives and education to ruleness itself, for if rule-appliers, rule-interpreters, and rule-enforcers have little reason to follow rules when they perceive their application to be sub-optimal in the individual case, then the use of rules as regulatory strategy will be illusory. Conversely, if discretion is seen as something to be rejected rather than embraced, then the use of discretion as a regulatory strategy may also be illusory. So if the virtues of both rules and discretion are to be part of the regulatory arsenal, it will be necessary to consider the background conditions under which they both might be possible, background conditions which, if the convergence hypothesis is true, might not now exist.