

# *Conflict and Supplement between Formal and Informal Institutions of Prepackaged Food Labeling*

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**Abstract:** Scholars have been paying contiguous attention to the topic of discussion of the relationship between the formal institution and the informal institution in the academic community. Through the case study and practical investigation, this paper discusses the integrated present of the boundary and relationship between food label system and informal system. The boundary between a dominant formal system and a hidden informal system is not static and the informal system may be transformed into a formal one, provided that the informal system must be based fully on indigenous cultural characteristics. The relationship between the formal and informal institutions is not simply one kind of relationship existing, but the integrated presence of complex relationships. On the one hand, the formal system excludes the informal system, squeezing the space for informal institutional practice and impacting local knowledge. On the other hand, the informal system practices protect small-scale producers, maintain local knowledge and build other trust systems that are different from the mainstream system. Informal food labeling practice is supplement to formal system.

## 1. Introduction

Academic community keeps an eye on the relationship between informal institution and formal institutions. Douglass North illustrates that “even the most casual introspection suggests the pervasiveness of informal constraints. Arising to coordinate repeated human interaction, they are (1) extensions, elaborations, and modifications of formal rules, (2) socially sanctioned norms of behavior, and (3) internally enforced standards of conduct. I elaborate on each of these aspects of informal constraints<sup>[1]-40</sup>. “Informal constraints come from socially transmitted information and are a part of the heritage that we call culture<sup>[1]-37</sup>. Formal order, to be more explicit, is always and to some considerable degree parasitic on informal processes, which the formal scheme does not recognize, without which it could not exist, and which it alone cannot create or maintain<sup>[2]</sup>. North and Scott discuss the relationship between informal constraints and formal constraints, emphasizing the importance of informal institution, which is rooted from Chinese local culture and practice. This kind of informal institution has positive effects. Scholars in our country also explore this academic topic. Some think it is dialectical between informal institution and formal institution, which is based on informal institutional practices. It is necessary to recognize some informal institutional forms

from social customs, traditional culture and so on<sup>[3]</sup>. On the other hand, some scholars consider informal institutional practice functions negative influence for China to build legal society<sup>[4]</sup>. During the transit period of modern society in China, informal rules exists not only as “origin”, “supplement”, and “decompressed information” for formal rules, but also as “competitor”, “second order effect”, and “error trial” for formal rules<sup>[5]</sup>.

Under the influence of globalization and foreign trade, China has constructed food labeling institution framework based on Codex Alimentarius and the experience of some developed countries. The food which labels attached to are not only for people to eat, but also associated with social elements, such as feelings, culture and so on. Beyond formal institution as the government tool functions, food labels embody other localities. Therefore, there are tension existing between local food culture and international food label institution framework. This paper, taking food labeling as example to explore the relationship between formal institution and informal institution, is meaningful. SU Li<sup>[6]</sup> thinks “habits, moral, convention, mores and social norms at all times are part of social order and system. Hence, it is the component to form legal system, and is essential. “ Informal rules are entrenched in the sociality. The purchase choices of food reflect customers’ habits and preference, which are deeply imbedded in the social background, closely bound up with mores and customs. China owns a long history, so Chinese social background is very different from other countries. Different system environments provide the field for the interaction between formal system and informal system. In America, many scholars research on how to maximally develop food labeling system functioning as formal institution. Food labels play third-party roles in the food marketing system through their impact on product design, advertising, consumer-confidence in food quality, and consumer education on diet and health. However, current analysis focuses overwhelmingly on the label’s direct use as a point-of-purchase shopping aid, even though such use is limited by consumers’ information processing abilities and time. In rewriting label regulations, policy makers should consider the benefits and costs of the broad array of roles labels serve, with evaluation of alternative regimes based on their impacts on consumer behavior and seller strategy<sup>[7]</sup>. In the United States, the federal government is increasingly using informational labeling as a means of shaping (a)consumers’ knowledge, purchasing patterns, and use practices, and (b)manufacturers’ product offerings and marketing practices<sup>[8]</sup>. Food labeling, as institution tool, begin to take into effect. Federal intervention in food labeling is often proposed with the aim of achieving a social goal such as improving human health and safety, mitigating environmental hazards, averting international trade disputes, or supporting domestic agricultural and food manufacturing industries. Economic theory suggests, however, that mandatory food-labeling requirements are best suited to alleviating problems of asymmetric information and are rarely effective in redressing environmental or other spillovers associated with food production and consumption. Theory also suggests that the appropriate role for government in labeling depends on the type of information involved and the level and distribution of the costs and benefits of providing that information<sup>[9]</sup>. This paper aims to answer the questions. This paper elaborates the boundary and relationship between formal institution and informal institution from the overflow effect produced by food label formal institution.

## **2. The Boundary between Formal Institution and Informal Institutional Practice.**

The formal system of food labeling refers to a system bundle related to labels, which is the sum of a series of laws, regulations, standards and methods formulated by the government. The informal system of food labels referred to in this paper means that the food label does not conform to the current formal legal system, but the quality of the attached food is guaranteed and there are fixed consumer groups.

The food labeling system is clearly stipulated in the relevant laws, regulations, management methods and national standards such as the “Food Safety Law”, “the Food Labeling Management Regulations” and “the General Rules for the Labelling of Prepackaged Foods”. The state constructs its macroscopic order through standardized, formatted labelling system symbols to facilitate a clear and traceable food management chain. In order to achieve institutional aims, formal institution is characteristics with integration and maneuverability, which is convenient for governors to carry out. It is formulated in the form of law and other regulation and document, so it is visible. Food label institution, as a kind of semiotic system, is the precondition of keeping market order normal. Standardization and regularization is manifestation of national governance system. On the opposite, informal institution is not regulated in the visible words, but existing in the minds and habits of people. The boundary between formal institution and informal institutional practice is clear in the legal text of law. However, it is blurred in practice. Referring to some local special type of food, especially drug and food homology, government attempts to take use of formal institution to solve the question. For example, tea made of *scutellaria baicalensis* and biscuits made of monkey head mushroom (which is “*hericium erinaceus*”). *Scutellaria baicalensis* and monkey head mushroom both could be Chinese medicine. Meanwhile, they could be ingredients for food. Formal institution regulated the food in the market should be sold in two divided categories: common food and health food. Generally speaking, it is forbidden to publicity the curative effects of common food. The nutrition claim of health food is strictly regulated in “Health Food Inspect and Evaluation Technique Norm[10]” “in order to avoid the behavior of cheating the customers. When food enterprises make use of drug and food homology as food ingredients, they can only choose either common food or health food to sell. In the case of “Jiangzhong *Heridium erinaceus* biscuits”, the biscuits are sold as the type of ordinary foods. *Heridium erinaceus* as Chinese medicine is famous for nourish the stomach. “Nourishing the stomach” is Chinese local saying, not regulated in the “Norm”. In order to maximize the benefits, companies take advantages of “Nourishing the stomach” as advertisement to attract consumers. This method of using informal rules publicity arise consumers’ doubts and was eventually brought to court with “false propaganda”. Although the final food company won the suit, the words “nourishing the stomach” no longer appeared in the package of the products and also vanished in its advertisement and slogan. The case has come to an end, but the results of the case are not unexpected, which has brought more confusion to other food companies. One manager, who is responsible for labeling in JJ Food Company in Hebei Province, conveys his opinions: “I have been paying attention to this case for a long time. It is like our products: drink made from ginger, which is sold as ordinary food. If I take such advertisement on the label: clearing damp and dispelling cold, warm uterus and stomach, there is no problem according to this case. But we didn’t do this. I still think it is not proper for common food.” Other related person in food companies said: “The key of this case is that “nourishing the stomach” is not curative effect expressions. If ordinary food could be declared as “nourishing the stomach”, then nourishing the heart, liver and so on such sayings could be permitted.” The discussion caused by this case fully illustrates that the present formal rules are not completely conform to Chinese tradition of food and medicine homology. The existing formal rules don’t clarify the boundary of formal institution and informal institution, but blur the boundary. The declaration is the implicit cultural constraint in informal rules; entrepreneurs display this kind of cultural constraint, which arouse the doubt of the public. Consumers make use of informal rules which are not accord with the formal label system to strike companies to earn profit.

The formal institution as a national governance tool must be characterized by operability to carry out. This feature determines that it is impossible for a formal institution to exhaust all the scenarios in practice. Informal institutional practices are usually in a vague area, across the institutional boundaries. If such informal institutional practices could always be a tacit rule, companies face little

risk. Once consumers use the formal system to judge the practice of informal institutions, both the enterprise and the government must pay corresponding governance costs because the formal system is mandatory. Therefore, the practice of informal institutions has the danger of being judged by formal institutions when they are contradictory. The occurrence of certain events blurs the boundary between formal institutions and informal institutions. The blurred boundaries become gray areas, and problems are often happening in this field. In short, the demarcation of the boundary between the formal system and the informal system is not fixed and clear, and the force that promotes the change of the boundary is constantly struggling, playing, and finally reaching a certain equilibrium state. In a particular case, the boundary is offset or the boundary is obscure.

### **3. Informal Institutional Practice Squeezed by Formal Institution**

The implementation of the formal system needs cost input. The production of the pre-packaged food labeling by the production entity not only requires capital costs, but also labor costs and time costs. These costs are a drop in the bucket for large-scale production entities, but may be a huge investment for small-scale production entities beyond their capabilities. The standardization of the labeling institution has further raised the market entry threshold, distinct some production entities entering the market.

The establishment of formal institution squeezes informal institutional practice space. For example, nutritional labels becoming mandatory contents of label expel those products without nutritional labels which would enter market. The implementation cost has been taken by food producers. As long as the formal system has implemented, operators have to bear the increased cost. Labeling nutrition information is relatively high-cost identification content compared to other label content, because the number marked in the nutrition label needs to be tested in lab by professional technicians. In addition to the capital cost, it is indispensable to invest in intellectual capital and time costs. The mandatory labeling of the nutrient composition table increases the cost of food labeling entities. The increase in the cost of food labeling raises the threshold for food producers to enter the market. Small-scale producers do not have sufficient financial strength to bear the cost of the labeling system, which further eliminates some small-scale food production entities. For example: BXY Farmer cooperative[11] produce chilli sauce from pepper. There is no nutrition information on the package of chilli sauce, which doesn't conform to the national standards. The reason is that cooperative doesn't want to pay for labeling the nutrition information, which takes a lot of money. The chairman of cooperative thought: "it is not cost-efficient. Second, restrict to small-scale and lack of money investment, small-scale producer couldn't afford the cost of labeling nutrition information". Therefore, food labels that do not conform to the formal institution can only be sold through non-mainstream channels. Non-mainstream channels are unblocked because of a stable customer group, which often does not care whether there are labels on the product or not. Influenced by price factors or trust mechanisms, customers purchase products not from mainstream circulation channels, without labels. So they will not bear the cost of labeling and enjoy relatively low prices. Even if we do not consider whether small-scale production entities have the ability to attach nutrition labels, it is thought that small-scale production entities will also be labeled with nutrition labels, the price advantage will be impaired. The original customer groups may be reduced or dissolved, and small-scale production entities will also face bankruptcy or loss.

Foods that are not labeled with nutrient ingredient are often produced by small-scale producers, which are often traditional and unique in their manufacturing processes, recipe. Mandatory labeling of nutritional labels excludes a number of small-scale production entities whose capital costs are insufficient, which reduces the variety and uniqueness of products in the market and narrows the range of food choices for consumers. For example, in the above-mentioned BXY cooperative, the

chili sauce is made by the non-industrial process. No other preservatives and other food additives are added to the chili sauce. The shelf life is short. Because the selected ingredients are peppers grown by the cooperative, the taste and quality obtain recognition of customers. A cooperative's product: scutellaria baicalensis tea, which has the effect of clearing away heat and purging fire, cannot be reflected in the standardized nutrient composition table. Unlike large-scale producers, food produced by small-scale production entities might be both the carrier of heritage culture and the guarantee of quality. If small-scale production entities are not able to survive the sales cycle of the market due to the problem of capital turnover, or if they are not aiming at absolute high returns, they will bankrupt. Then the products with uniqueness and traditional type are also excluded. In the market, the survival space of the carrier of local knowledge is squeezed, and the traditional production process that guarantees high quality cannot be continued.

The spatial and temporal boundaries of formal institution and informal institutional practices may overlap or may be separate. The rational division of institutional and non-institutional governance objects and functional boundaries can improve the effectiveness of institutional implementation. The informal institutional practice in rural acquaintances reduces production costs and meets the preferences of some consumer groups. The informal institutional rules of rural areas conform to the social network environment of acquaintances. If a universal national-level labeling system is adopted to regulate pre-package food labels, it must be labeled as required, which not only increases the production costs of small-scale producers, but also extends the industrial chain, leading to the disappearance of specific consumer groups. As the market economy and business continue to develop, processed foods flood into rural areas, destroying local rules and local knowledge. For example, some children in rural areas only eat spicy strips without eating anything else. Fake food, which imitates famous food name and package to mislead customers to buy by mistakes, has been very popular in rural areas, causing the destruction of the original food system of the local people, but the new foreign knowledge hasn't implanted into the thoughts of rural residents, and the original local knowledge has no longer existed. As a result, a series of problems have emerged, destroying local knowledge, leading to the inability of rural residents to have a nutritious diet, which is contrary to institutional goals set by government.

#### **4. Informal Institutional Rules Making Up Formal Institution**

##### **4.1 Informal Institution Transferring into Formal Institution**

The goal of food labeling institution built is to cope with market failures and simply to avoid fraud. With the government's role continuous transition from management to governance: serving the public. Food labels are gradually becoming information governance tool. Because it only provides the consumers with information, giving chances to consumers to choose. It is soft policy tool for target groups. The food label institutionalization carry the responsibility with diversified institution goals: (1) food security and safety; (2) standardizing corporate behavior; (3) reducing information asymmetry; (4) in line with social development goals. The multiple goals given to food label institutions have gradually improved the expected functions of information governance tools. From singularity to diversification, the change of system goals for food labeling tends to be diversified. The tendency of system goals is consistent with social development goals. Food label realize the institution goals by transferring the information. The real problem brought about by the diversification of system goals is the conflict brought by different goals. The multiple goals also bring the changes for compulsory label content and voluntary label content.

The compulsory content of food label is stipulated by the government through laws and regulations, which belong to the formal institution with publicness. The voluntary label content is that production entity can choose to label or not, which is the informal part of institution. Therefore,

the transfer of formal institution and informal institution can be investigated from the change between mandatory labeling content and voluntary labeling. The boundary between them is not fixed. Informal part can become formal institution. The reason of changes happening between mandatory and voluntary content is the shift in attention from institutional goals. With the economy and social environment changing, institutional goals keep adapting to the new changes. At the beginning, the food labeling institution goal is to keep the market order and keep information true. Then not only at the pursuit of keep information true, but also the institution goal is to keep people healthy, even environment friendly. The influence of the changing diversified institution objectives on food labeling is directly reflected in the content of the food label. In order to reflect the diversified institution goals, the mandatory content of food labels has increased, and the requirements for labeling have been more and more strict and detailed. Compared to the three versions of “General Standard for Food Labeling” issued in the year of 1994, 2004 and 2011, the compulsory content ranges differently as regulated. The Article 5 in 1994 version of “General Standard for Food Labeling”(GB7718-1994) stipulates that the mandatory labeling content includes: food name, ingredient list and other nine items. Compared with the 1994 version, “General Rules for Prepackaged Foods Labeling”(GB7718-2004), the mandatory labeling content has added “quantitative labeling of ingredients” and specific standardization requirements for the format has also enforced labeling. In 2011 version (GB 7718-2011), recommended labeling requirements of allergenic substances was entering the formal system. In 2013, nutritional label were added to the mandatory labeling content of prepackaged foods. The compulsory content of food labeling is continuously adjusted. The way of labeling food is gradually standardized and unified, reflecting the diversified institution goals. The format standardization regulates enterprises’ labeling behavior. The nutritional label is to reflect the institutional goal of guiding the public to nutrition diet. From the perspective of the function of food labeling and the compulsory content change, the diversification of the functions of the food labeling system is a process of transferring between formal institution and informal institution. The tendency and institutionalization process is the gradual increase in mandatory content.

#### **4.2 Informal Institution Embodying Social Connected Mechanism**

A prerequisite for the smooth implementation of the food labeling system is the consumer's trust in the institutional system. If this premise is not established, the exogenous system will not function. The food labeling system is built on the trust from the public. Consumers purchase according to the information obtained on the information label provides. The informal system practice depends on other trust systems different from the institution trust. The institution trust is replaced by other non-institutional factors. The trust mechanism established by non-institutional factors is irrelevant to the formal system of food labeling.

A famer cooperative in Hebei[12], the cooperative planted oil sunflower and used the oil sunflower to extract oil. Although no food labels are attached to the edible oil drums, the cooperative's edible oil is sold very well. Consumer groups who buy edible oil as follows: one is the cooperative members; the other is the folks in the village town. The oil bought by the folks is based on the social network of acquaintances. This intimate social relationship restricts the anomie of behavior, and the establishment of reciprocity-based trading guarantees the quality of the products. There is not simple buying and selling relationship between people, and mutual reciprocity is formed through other related network media.

In addition to the above phenomenon, the new food circulation market that is gradually emerging in the city, for example, the Organic Farmer's Fair regularly demonstrates in urban shopping malls, plazas, etc. Farmers directly sell their agricultural products. Consumers are invited to visit their

farms. The food they sell includes unlabeled prepackaged foods such as rice wine, cheese, tofu, milk, and yogurt. Organic Food is not certified by the third-party, but the price is much higher than that of an organically certified product. The high premium did not reduce the willingness of consumers to buy, and the consumer groups continued to increase. Urban residents judge food from direct communication with producers, from personal experience, and the credibility of the Fair. The Organic Farmers Fair reflects the social nature of the food, shortens the food supply chain within the urban space and return to the old market form, in which farmers and consumers can meet directly. At the same time, the Organic Farmers Fair has qualified the seller in the early stage to guarantee the quality of the food. The consumer group is based on the trust relationship with the Organic Farmers Fair and the seller.

The foods in the above sale network are not marked with standard food labels. Consumers choose not to rely on labels, but to consume by building a different trust system. At this point, consumers do no longer trust the labeling institution. Whether in the environment of unlabeled foods or in the labelled food sales environment, consumers have self-constructed different trust systems. The informal system leaves room for small-scale production entities, builds other trust systems different from institutional trust, and provides consumers with a variety of consumption ways, mitigating dissatisfaction from consumer groups with different needs for one purchase way, which embodies social connection mechanism.

## **5. Discussion the Relationship between Institution and Informal Institution Practice**

There is not existing one relationship form between institutions and informal institutions. Complex relationships are embedded in the context of the interaction among the state, the market and the society. The existence of informal institutional practices is based on the characteristics of social localization and social needs. The system is formulated by the government, which regulates the consumption behavior of consumers. There is a conflict between the informal system and the formal institutional practice.

The special food, whose label couldn't follow the formal institution, are produced by small-scale production entities. Labeling such food is in the informal rule space outside the labeling formal institution. The establishment of our country's labeling formal system is learnt from foreign countries. So it is not based on local informal institutional practice, squeezing the practice of informal institutions. On the other hand, the practice of informal institutions links the historical situation and the great changes of the current society. It is a supplement to the formal system. It is the best choice under the consideration of governance cost and governance performance. It is transitory stage of sale way from acquaintance society to stranger society and provide a special choice for non-mainstream groups. From the perspective of cost-benefit principle, the informal institutional practice is to minimize the cost of governance. From the perspective of social connection, the informal system is to establish a social connection mechanism between consumers and producers beyond the formal institution.

The formal institution, which lack to localization practices, can lead to a series of problems. The practice of the formal labeling system has objective requirements for the institutional environment, which must be based on the situation that institution is nearly matched with the institutional environment. The lack of connection with localized practices results in a failure between the formal system and the institutional environment. Once this objective requirement is not met, the practice of the informal system will exist. The existence of the informal system does not determine to replace the formal system, but to play a role in the field where the formal system cannot be effective.

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