Unbundling the State

Legal Development in an Era of Global, Private Governance

Michael O. Allen

October 28, 2022
Recent rise of transnational governance institutions (TGI)

Figure: Growth of TGIs

Source: Westerwinter 2019
Transnational Governance Institutions
Boon or Bane?

- Recent rise of transnational governance institutions (TGI)
- Scholarship focuses on first-order outcomes

*Figure:* Growth of TGIs
*Source:* Westerwinter 2019
Recent rise of transnational governance institutions (TGI)

Scholarship focuses on first-order outcomes

Second-order outcomes:

→ Risk substituting for domestic institutions

Figure: Growth of TGIs

Source: Westerwinter 2019
What is International Commercial Arbitration?
Private Substitute for National Courts

• Private, transnational system of cross-border contract dispute resolution
What is International Commercial Arbitration?

Private Substitute for National Courts

- Private, transnational system of cross-border contract dispute resolution
- Parties agree to send dispute to arbitration, not public court
What is International Commercial Arbitration?

Private Substitute for National Courts

- Private, transnational system of cross-border contract dispute resolution
- Parties agree to send dispute to arbitration, not public court
- Attractive to traders, investors, and commercial lawyers
  - Parties choose arbitrators and laws
  - Enforceable, no appeal
ICA in Global Economic Governance

Gaining Momentum

Sources: International Chamber of Commerce; United Nations Conference on Trade and Development
Overview of Argument

• ICA provides an exit option from local legal institutions
  → Reduces dependence on national courts for contract enforcement
• ICA provides an exit option from local legal institutions  
  \[\rightarrow\text{ Reduces dependence on national courts for contract enforcement}\]

• ICA erodes demand for public investment in efficient and neutral judiciary
Overview of Argument

• ICA provides an exit option from local legal institutions
  → Reduces dependence on national courts for contract enforcement
• ICA erodes demand for public investment in efficient and neutral judiciary
• Stagnation of local legal infrastructure
Exit → Stagnation
Two Institutional Channels

1. Generates dependence on transnational institutions in weakly institutionalized settings
   (Knack, 2001; Djankov, Montalvo & Reynal-Querol, 2008)
   → Global institutional exit-options reduce domestic demand for law
      (Nougayrède 2013; Sharafutdinova & Dawisha 2017)
   → Well-resourced actors have incentive to prevent institutional improvement (Sonin 2003)
Exit → Stagnation

Two Institutional Channels

1. Generates dependence on transnational institutions in weakly institutionalized settings
   (Knack, 2001; Djankov, Montalvo & Reynal-Querol, 2008)
   → Global institutional exit-options reduce domestic demand for law
     (Nougayrède 2013; Sharafutdinova & Dawisha 2017)
   → Well-resourced actors have incentive to prevent institutional improvement (Sonin 2003)

2. Reduces the cost of politicizing the judiciary
   → Sudan relied on ICA to attract investors to develop oil fields
     (Massoud 2013, 2014)
Primary Hypothesis

Expansion of International Commercial Arbitration

↓

Stagnation of Domestic Legal Institutions
“The standard by which a country’s laws pertaining to international arbitration is measured today…”
— South African Law Commission, 1998

Figure: Adoption of UNCITRAL Model Law
Measuring Cross-national ICA Protections

Adoption of the UNCITRAL Model Law

“The standard by which a country’s laws pertaining to international arbitration is measured today…”
— South African Law Commission, 1998

- What it does:
  → Regulates arbitration
  → Bars judicial intervention
  → Eases enforcement

Figure: Adoption of UNCITRAL Model Law
Estimating the Effect of ICA on Legal Development

- Estimate Model Law $\rightarrow$ $\Delta$Rule of Law using a diff-in-diff estimator with weighted, matched sets

(Persson & Tabellini 2007; Imai, Kim & Wang 2021)
Estimating the Effect of ICA on Legal Development

- Estimate **Model Law → ΔRule of Law** using a diff-in-diff estimator with weighted, matched sets
  
  (Persson & Tabellini 2007; Imai, Kim & Wang 2021)

- **Dependent Variable:** V-Dem’s Rule of Law Index
  - Low Rule of Law: < .8
  - High Rule of Law: ≥ .8
Estimated Effect of Model Law Enactment
Low Rule of Law Sample

![Graph showing estimated change in rule of law from t-1 over years from model law enactment.]

Full Results  Covariate Balance  First Differences  Alternative Cutoffs  Sensitivity Analysis
Estimated Effect of Model Law Enactment

High Rule of Law Sample

![Graph showing estimated change in Rule of Law from t-1 over years from Model Law Enactment.](image-url)
Firm Behavior Matters Too
Assessing Behavioral Effects of Model Law Enactment

- Effect primarily driven by ICA and the Model Law as an institution
Firm Behavior Matters Too
Assessing Behavioral Effects of Model Law Enactment

• Effect primarily driven by ICA and the Model Law as an institution
• Firms’ behavior matters too:
Firm Behavior Matters Too
Assessing Behavioral Effects of Model Law Enactment

- Effect primarily driven by ICA and the Model Law as an institution
- Firms’ behavior matters too:
  1. The Model Law increases the use of arbitration
Effect primarily driven by ICA and the Model Law as an institution

Firms’ behavior matters too:

1. The Model Law increases the use of arbitration
2. Arbitrations tend to take place abroad
Effect primarily driven by ICA and the Model Law as an institution.

Firms’ behavior matters too:

1. The Model Law increases the use of arbitration.
2. Arbitrations tend to take place abroad.

The location of arbitration matters:

1. Local courts manage the arbitration process: can impose interim measures, appoints arbitrators, etc.
2. Can annul an award.
Does the Model Law Affect Arbitration Behavior?

Country-level arbitration data collected from *ICC Bulletins*, 1992–2020
Does the Model Law Affect Arbitration Behavior?

Country-level arbitration data collected from *ICC Bulletins*, 1992–2020

- **Usage:** # of nationals party to a dispute
Does the Model Law Affect Arbitration Behavior?

Country-level arbitration data collected from ICC Bulletins, 1992–2020

- **Usage:** # of nationals party to a dispute
- **Oversight:** # of disputes seated in jurisdiction
Arbitration at the ICC by Local Parties

The Model Law increases usage by national parties

<table>
<thead>
<tr>
<th>DV: Party Nationality (count)</th>
<th>Total</th>
<th>Complain.</th>
<th>Defendant</th>
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**Note:** *p < .05, **p < .01
**Arbitration at the ICC by Local Parties**

*The Model Law increases usage by national parties*

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Location of ICC Arbitrations

The Model Law does not increase local oversight

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Conclusion

- Evidence of **unintended consequences** of the growth of international arbitration (e.g., Lake 2014; Sattorova 2018)
- ICA is an **exit option** from local legal institutions
  - ICA **erodes** local legal development
  - Increases ICA usage, with no effect on oversight
- Effect driven by countries with already **weak legal institutions**
Appendix

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1. Full Results Table
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3. First Differences
4. Alternative Cutoffs
5. Sensitivity Analysis
6. ICC Results w/ linear estimator
   → Party Nationality
   → Seat of Arbitration
# Full Table

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<tr>
<th>Years in Force</th>
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<th>Full</th>
<th>Low</th>
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Pre- and Post-Refinement Covariate Balance
Low Rule of Law Sample

Appendix TOC  Main Slide
First Differences
Low Rule of Law Sample

Change in Rule of Law Index

No Model Law
Model Law

Years Since Model Law Enactment

Appendix TOC  Main Slide
Alternative Rule of Law Cutoffs

Low Rule of Law Sample

![Graph showing ATT against Low Rule of Law Cutoff at t=0, t=2, and t=5.](image)
Sensitivity Analysis
Two-way Fixed Effects Model

Partial $R^2$ of confounder(s) with the treatment
Partial $R^2$ of confounder(s) with the outcome

- Unadjusted
  - 5x Trade
    - (−0.034)
  - 10x Trade
    - (−0.023)
  - 15x Trade
    - (−0.011)
  - 20x Trade
    - (0.001)

Appendix TOC
### ICC Party Nationality

Borusyak, et al. Estimator

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<thead>
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<th></th>
<th>Total (1)</th>
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## ICC Seat of Arbitration

### Borusyak, et al. Estimator

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<td>Model Law</td>
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<td>0.153 (0.095)</td>
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<td>0.152 (0.095)</td>
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<td>[.278] [.630] [.630]</td>
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