

Unbundling the State

Legal Development in an Era of Global, Private Governance

Michael O. Allen

October 28, 2022

Transnational Governance Institutions

Boon or Bane?

- Recent rise of transnational governance institutions (TGI)

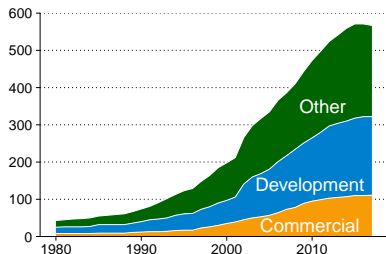


Figure: Growth of TGIs

Source: Westerwinter 2019

Transnational Governance Institutions

Boon or Bane?

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

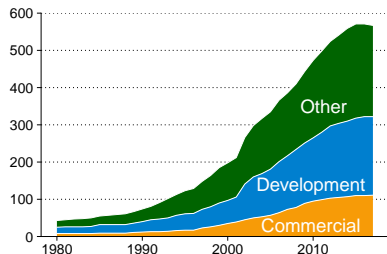


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Transnational Governance Institutions

Boon or Bane?

- Recent rise of transnational governance institutions (TGI)
- Scholarship focuses on **first-order** outcomes
- Second-order outcomes:
 - Risk **substituting** for domestic institutions

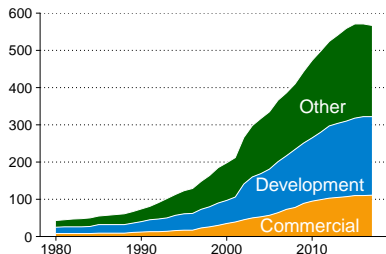


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What is International Commercial Arbitration?

Private Substitute for National Courts

- Private, transnational system of **cross-border contract dispute resolution**

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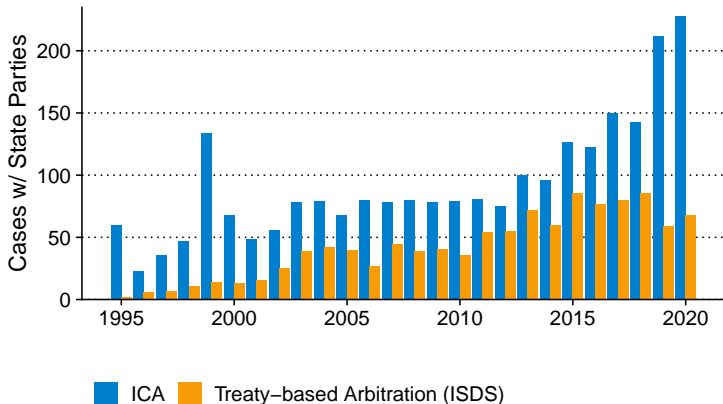
What is International Commercial Arbitration?

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

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 - **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

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

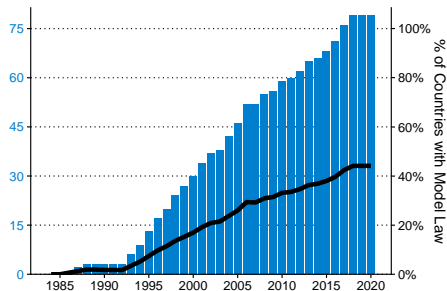


Figure: Adoption of UNCITRAL Model Law

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

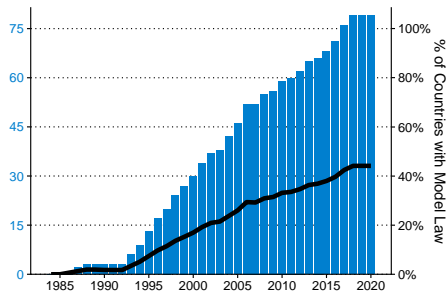


Figure: Adoption of UNCITRAL Model Law

Estimating the Effect of ICA on Legal Development

- Estimate **Model Law** \rightarrow Δ **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

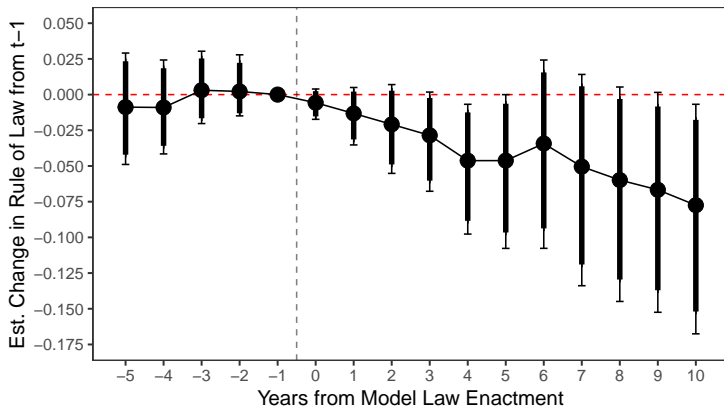
- Estimate **Model Law** \rightarrow Δ **Rule of Law** using a diff-in-diff estimator with weighted, matched sets

(Persson & Tabellini 2007; Imai, Kim & Wang 2021)

- **Dependent Variable:** V-Dem's Rule of Law Index
 - \rightarrow **Low** Rule of Law: $< .8$
 - \rightarrow **High** Rule of Law: $\geq .8$

Estimated Effect of Model Law Enactment

Low Rule of Law Sample



Full Results

Covariate Balance

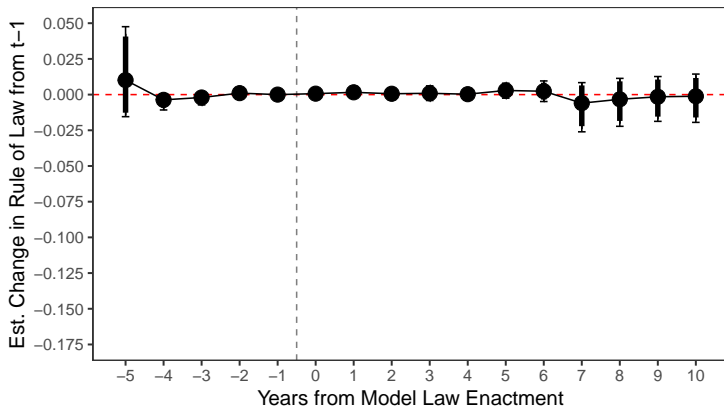
First Differences

Alternative Cutoffs

Sensitivity Analysis

Estimated Effect of Model Law Enactment

High Rule of Law Sample



Full Results

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Firm Behavior Matters Too

Assessing Behavioral Effects of Model Law Enactment

- Effect primarily driven by ICA and the Model Law as an **institution**

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 1. The Model Law increases the **use** of arbitration

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Assessing Behavioral Effects of Model Law Enactment

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

Firm Behavior Matters Too

Assessing Behavioral Effects of Model Law Enactment

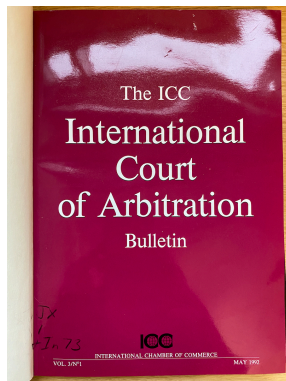
- Effect primarily driven by ICA and the Model Law as an **institution**
- Firms' **behavior** matters too:
 1. The Model Law increases the **use** of arbitration
 2. Arbitrations tend to take place **abroad**

The location of arbitration matters:

- Local courts **manage** the arbitration process: can impose interim measures, appoints arbitrators, etc.
- Can **annul** an award

Does the Model Law Affect Arbitration Behavior?

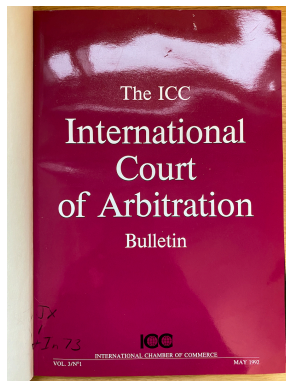
Country-level arbitration data collected
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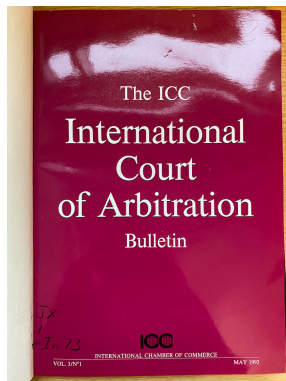
- **Usage:** # of nationals party to a dispute



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

	DV: Party Nationality (count)				
	Total			Complain.	Defendant
	(1)	(2)	(3)	(4)	(5)
Model Law	0.263*	0.202**	0.223**		
	(0.107)	(0.075)	(0.069)		
<i>Pretrend p-value</i>	[.619]	[.956]	[.975]		
Economic Controls		✓	✓		
Political Controls			✓		
Unit- and Year-FE	✓	✓	✓		

Note: * $p < .05$, ** $p < .01$

Arbitration at the ICC by Local Parties

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	Total			Complain.	Defendant
	(1)	(2)	(3)	(4)	(5)
Model Law	0.263*	0.202**	0.223**	0.295**	0.166*
	(0.107)	(0.075)	(0.069)	(0.082)	(0.072)
<i>Pretrend p-value</i>	[.619]	[.956]	[.975]	[.679]	[.721]
Economic Controls		✓	✓	✓	✓
Political Controls			✓	✓	✓
Unit- and Year-FE	✓	✓	✓	✓	✓

Note: * $p < .05$, ** $p < .01$

Location of ICC Arbitrations

The Model Law does not increase local oversight

	DV: Seat of Arbitration (count)		
	(1)	(2)	(3)
Model Law	0.437*	0.209	0.234
	(0.190)	(0.129)	(0.125)
<i>Pretrend p-value</i>	[.115]	[.539]	[.514]
Economic Controls		✓	✓
Political Controls			✓
Unit- and Year-FE	✓	✓	✓

Note: * $p < .05$, ** $p < .01$

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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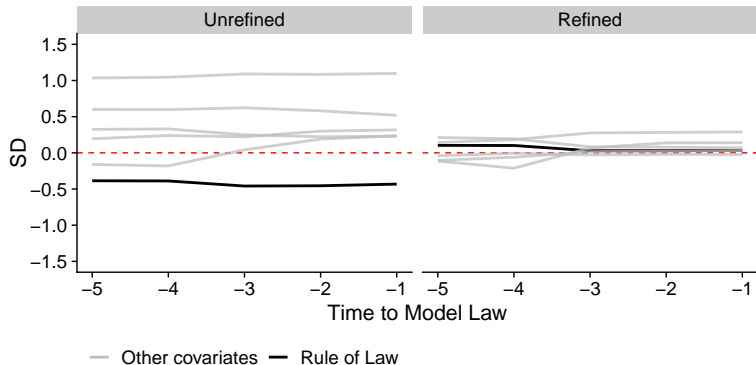
1. Full Results Table
2. Pre- and Post-Refinement Covariate Balance
3. First Differences
4. Alternative Cutoffs
5. Sensitivity Analysis
6. ICC Results w/ linear estimator
 - Party Nationality
 - Seat of Arbitration

Full Table

Years in Force	PanelMatch			BJS
	(1)	(2)	(3)	(4)
0	-0.01 (0.00)	-0.01 (0.01)	-0.00 (0.00)	-0.01 (0.01)
1	-0.01 (0.01)	-0.02 (0.01)	0.00 (0.00)	-0.02 (0.01)
2	-0.02 (0.01)	-0.03 (0.02)	0.00 (0.00)	-0.03 (0.02)
3	-0.02 (0.01)	-0.03 (0.02)	0.00 (0.00)	-0.03 (0.02)
4	-0.03 (0.01)	-0.05 (0.02)	-0.00 (0.00)	-0.05 (0.02)
5	-0.03 (0.01)	-0.05 (0.02)	0.00 (0.00)	-0.05 (0.02)
Sample	Full	Low	High	Low

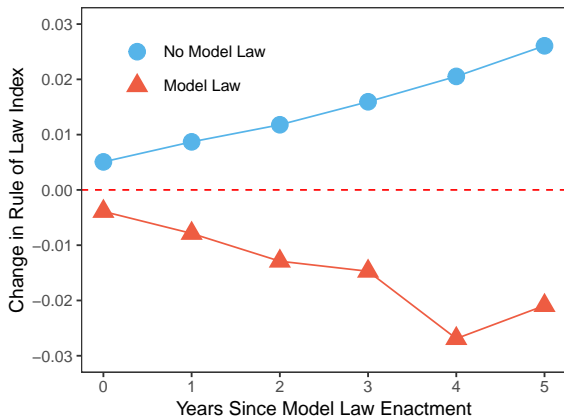
Pre- and Post-Refinement Covariate Balance

Low Rule of Law Sample



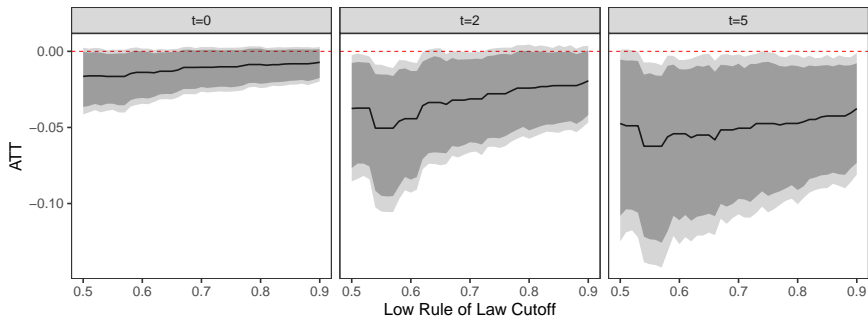
First Differences

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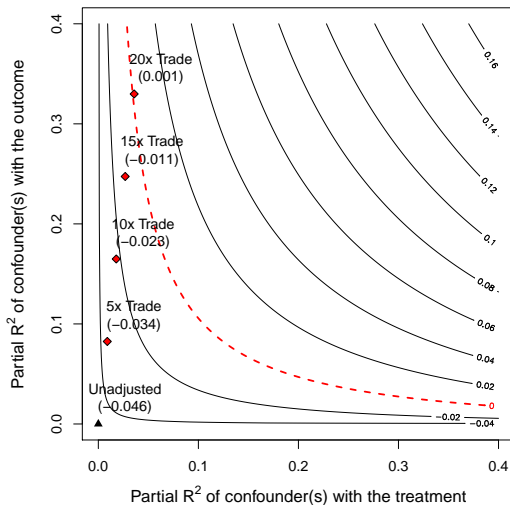
Alternative Rule of Law Cutoffs

Low Rule of Law Sample



Sensitivity Analysis

Two-way Fixed Effects Model



ICC Party Nationality

Borusyak, et al. Estimator

	DV: ihs Party Nationality				
	Total		Complain.	Defendant	
	(1)	(2)	(3)	(4)	(5)
Model Law	0.229** (0.084)	0.164 (0.086)	0.169* (0.086)	0.170** (0.064)	0.084 (0.067)
<i>Pretrend p-value</i>	[.335]	[.554]	[.542]	[.197]	[.863]
Economic Controls?		✓	✓	✓	✓
Political Controls?			✓	✓	✓

Note: * $p < .05$, ** $p < .01$

ICC Seat of Arbitration

Borusyak, et al. Estimator

	DV: ihs Seat Location				
	Total		Court	Parties	
	(1)	(2)	(3)	(4)	(5)
Model Law	0.233*	0.153	0.152	0.061*	0.114
	(0.091)	(0.095)	(0.095)	(0.027)	(0.068)
<i>Pretrend p-value</i>	[.278]	[.630]	[.630]	[.400]	[.528]
Economic Controls?		✓	✓	✓	✓
Political Controls?			✓	✓	✓

Note: * $p < .05$, ** $p < .01$