Unbundling the State: Legal Development in an Era of Global, Private Governance*

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Abstract

What happens to a public, domestic institution when its authority is delegated to a privately-run, transnational institution? This paper examines this question through a study of the global privatization of commercial dispute resolution. I present a theoretical framework for understanding how governmental tasks that have traditionally been "bundled" together in state institutions become "unbundled" and outsourced to private bodies. I apply this framework to international commercial arbitration (ICA), a private, transnational system of cross-border commercial dispute resolution. I argue that ICA provides key interest groups that would otherwise lobby for rule-of-law reforms an exit option from weak institutions which in turn reduces pressure on the state to invest in capacity-enhancing reforms. I demonstrate that the enactment of strong protections for ICA leads to the gradual erosion of the quality of local legal institutions, particularly in countries with already weak legal systems.

Keywords: Dispute settlement · Commercial arbitration · Global governance · Political development

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1 Introduction

Private, transnational governance regimes with the power to write, interpret and enforce commercial rules have proliferated in recent decades. As Braithwaite (2008, 3) wrote, many countries have "become rule-takers rather than rule-makers." Because much of the work on this form of private regulation focuses on the transnational regimes themselves, we know relatively little about the consequences of this changing institutional landscape for domestic political development. In this article, I argue that the growth of private, transnational authority carries with it an implicit model of political and legal development, what I called the "unbundled state," that cuts against traditional models of political development. "Unbundling" governance refers to the delegation of rulemaking authorities—that is, the power to write, interpret or enforce rules—that have traditionally been "bundled" in centralized public institutions. Under this model, rather than supporting holistic competence building within centralized institutions, states have the option of delegating piecemeal governance tasks to actors with little accountability to domestic publics. One unintended byproduct of the growth of transnational institutions is that countries with weak state capacity may suffer from institutional stagnation and divestment as powerful domestic and foreign actors, who would otherwise have a stake in the strength of domestic institutions, instead make use of transnational substitutes for the same services. This in turn erodes the domestic coalition for capacity-enhancing reform. In this article, I examine unbundling empirically through an analysis of the growth of international commercial arbitration, a substitute for local contract enforcement institutions.

On its face, there appears to be a net gain when states privatize governance tasks like contract enforcement. Perhaps private arbitration, for example, simply eases the process by which firms involved in international business enforce contracts and settle disputes while no one else is made worse off. The central theoretical claim put forward below is that emergence of transnational governance institutions has important implications beyond the boundaries of the specific issue-areas they are meant to regulate. I argue that this is due to the externalities of bundled and centralized institutions. Centralization establishes simple lines of accountability and creates externalities that,

when positive, benefit a wider constituency, and, when negative, ease the process of building broad political coalitions for reform. This means that the effect of unbundling on the underlying public institution depends on how the public and private bodies interact, specifically whether the private body acts as a complement or substitute to the public institution. Substitution provides actors an exit option from the public institution, thereby reducing the incentive for civil society groups to monitor and lobby for institutional improvements while also limiting the positive governance externalities of bundled, public institutions. Reducing incentives for the state to invest in rule-of-law reforms leads to an overall reduction in the competence of local legal institutions over time. The complementarity hypothesis, by contrast, expects unbundled institutions to enhance governing quality because civil society actors remain invested in the quality of the public institution while the state can direct the private body and take advantage of the private body's expertise.

The "de-localization" and privatization of services traditionally entrusted to public institutions is particularly prevalent in the area of commercial dispute resolution (Cutler, 2003; Sharafutdinova and Dawisha, 2017). Resource rich individuals and firms can access strong contract enforcement infrastructure by submitting disputes to foreign jurisdictions or arbitral tribunals, while those without such resources are left to deal with sub-par, local domestic legal infrastructure. Nougayrède (2013) refers to this phenomenon as the "outsourcing" of law. A key element of modern global economic governance facilitating legal outsourcing has been the development of international commercial arbitration (hereafter, ICA). ICA refers to a widely-used system of private arbitration for the adjudication of international commercial disputes. ICA allows disputants to design the dispute resolution forum to fit their needs by allowing them to choose the relevant procedural and substantive laws and pick the arbitrators who will hear the case, among other things. Parties typically enter into ICA through contractual provisions stipulating that future disputes will be sent to private arbitration rather than national courts.

ICA has accomplished the outsourcing of law in large part through the diffusion of two international legal instruments: the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (1958), commonly referred to as the New York Convention (NYC), and—the focus

of this paper—the UN Commission on International Trade Law's (UNCITRAL) Model Law on International Commercial Arbitration (hereafter, the Model Law). The New York Convention is a multilateral treaty that allows for the enforcement of arbitration awards in any signatory country so long as the award was subject to the jurisdiction of another signatory.[1] The Model Law is a ready-made legislative text incorporating key features of the "state-of-the-art" in ICA. It limits judicial intervention in the arbitral process by severely circumscribing the scope of judicial oversight while at the same time requiring courts to enforce arbitration agreements and awards without substantive review unless one of a very narrow set of exceptions are met. Over 75 countries have enacted legislation based on the Model Law. The NYC has helped eased global enforcement, while the Model Law has been integral to harmonizing and promoting the practice of ICA around the world.

Since the inception of modern commercial arbitration in the early 20th century, arbitration has sparked intense and persistent debate about the role of private authority in public affairs (Cutler, 2003; Hale, 2015). This debate has taken on added urgency—both domestically and abroad—in light of the increasing deference legislatures and judiciaries around the world have granted to arbitration (Szalai, 2013; Resnik, 2015; Stone Sweet and Grisel, 2017). This paper joins this debate by providing a framework for conceptualizing the interaction between transnational institutions such as international arbitration and local legal institutions. I then examine the second-order effects of the spread of ICA on domestic legal development in low-capacity states that promote arbitration typically as a means of attracting foreign capital and trade. I find that the growth of international arbitration has had a deleterious effect on the development of domestic legal institutions, particularly in countries with already weak legal institutions.

The paper proceeds as follows. In the next section, I briefly present the arguments of the two main competing hypotheses concerning the interaction between private and public systems of commercial dispute resolution. I then seek to synthesize the conflicting approaches particular to international arbitration by contextualizing this debate within the literatures on political development, globalization and the growth of transnational, private governing bodies. Following that, I

[1] An arbitration "award" refers to the legally binding decision of an arbitration panel.

apply this theoretical framework to the case of international commercial arbitration. I argue that ICA is best thought of as a substituting institution that risks hindering investment in local legal reform. And in the final section, I use a difference-in-differences estimator with weighted matched sets to examine the effect of enactment of strong protections for ICA on the development of a country's legal infrastructure. In short, I find that the enactment of the UNCITRAL Model Law on ICA results in the gradual degradation of public legal institutions in countries with weak legal institutions.

2 International Commercial Arbitration and the Rule of Law

In this section I provide a brief overview of the debate amongst scholars and practitioners concerning the interaction between international arbitration and local legal institutions. I draw from the literature on the interaction between national courts and international arbitration in the context of both investor-state dispute settlement (ISDS) or ICA. ISDS refers the global system of arbitration for resolving violations of international investment law between investors and host states, while ICA concerns the resolution of cross-border contract disputes (which may or may not be between investors and host states). Until recently, much of the debate around international arbitration and local legal development has focused primarily on ISDS (e.g., Ginsburg, 2005; Bodea and Ye, 2020). While ISDS and ICA can be thought of as distinct systems, there are many legal and substantive similarities between them and they enjoy similar levels of protection from oversight by domestic courts. For instance, many ICA disputes are between foreign investors and public entities, but these cases are considered to be "ICA" because the source of the arbitration panel's jurisdiction is a contract, rather than an international legal source like a bilateral investment treaty (BIT). In such cases, the distinction between the ICA and ISDS is little more than a technical jurisdictional matter. The basic structure of ISDS and ICA vis-à-vis national courts is essentially similar: each is designed to be a private, transnational alternative to national courts in their capacity to issue legally binding rulings over commercial disputes. This similarity allows me to draw on the theoretical and

empirical debates surrounding ISDS and apply them to ICA. Broadly, I divide the literature into two camps: those who think arbitration will enhance the rule of law and those who think arbitration will subvert the rule of law. I discuss each camp below.

International arbitration enhances the rule of law. One group of scholars argues that international arbitration enhances local rule of law. Franck (2007, 367-370) contends that a successful international investment regime requires the mutual support of both national courts and international arbitration, in other words that arbitration and courts are complementary. In addition to serving as a steward for international arbitration and as a potential venue for the resolution of national legal disputes, Franck writes that international arbitration also provides a "useful model" that helps "promote adherence to the rule of law" through both the power of example and the introduction of competitive pressures on judiciaries (p. 372). Arbitration, Franck argues, increases competitive pressure on judiciaries by taking away cases that would otherwise go to court, thereby spurring local reform by jealous judiciaries to win back their former caseloads.

Rogers (2015) shares Franck's central thesis but argues that we should expand our focus to include the role of ICA as well. Unlike ISDS, which is rooted in international law, ICA is directly tied to reform of domestic institutions through national legislation and domestically oriented initiatives meant to promote and legitimize arbitration. As Dezalay and Garth (1996, 142) note in their study of the Egyptian arbitration profession after Egypt enacted reforms based on the Model Law, "These activities [such as implementing the UNCITRAL Model Law] gain legitimacy for arbitration locally and legitimacy for local leaders in the centers of arbitration." This legitimacy depends, however, on the integration between national and transnational arbitral practice. This is fostered through activities like creating national arbitration centers and working with transnational pro-arbitration bodies like UNCITRAL to fund promotional activities such as training exercises, conferences and moot competitions. Rogers (2015, 74) expects that local legal elites, eager to integrate into transnational business and legal networks, will work to entrench rule-of-law norms locally through "legislative reforms, judicial training, reforms in legal education, and attorney training that improve rather than detract from national legal institutions." In this way, rule-of-law norms are expected

to spillover from the transnational to the national setting. In a subsequent extension and empirical analysis of this theory, Rogers and Drahozal (2022) argue that pro-ICA reforms will support the diffusion of rule-of-law norms for two reasons. First, ICA will create new business opportunities for local legal elites who will work to diffuse stronger rule of law norms in order to secure those opportunities (pp. 5-9). Second, legal and business elites will demand a similar level of treatment from local courts that they enjoy in international arbitration: "attorneys and arbitrators trained in international standards for conflicts of interest are less likely to accept much lower standards in domestic arbitration or in national court litigation" (p. 8). Using a two-way fixed effects model, they find that the enactment of the UNCITRAL Model Law exerts a positive effect on domestic rule-of-law institutions.

International arbitration subverts the rule of law. Others are skeptical of the "good governance" narrative behind the promotion of international arbitration. Indeed, Sattorova (2018) shows that the emergence of this narrative grew out of the realization within the practitioner community that BITs may not have the positive economic developmental effects for which their advocates had hoped. Some argue that rather than providing complementarities that facilitate the spillover of rule-of-law norms or institutional competition that leads to a "race to the top," the substitution of courts by ICA and ISDS may instead lead to the deterioration of local legal institutions (Puig and Shaffer, 2018). In contrast to the models offered by Franck (2007) and Rogers and Drahozal (2022), exit from local courts is expected to lead to an overall reduction in political pressure for progressive rule-of-law reforms because commercial actors exiting to arbitration no longer have a stake in the quality of local courts. Ginsburg (2005, 119) argues that the availability of international arbitration therefore "may reduce courts' incentives to improve performance by depriving key actors from a need to invest in institutional improvement." Local judiciaries are shielded from competitive pressures because they do not enjoy private benefits from producing law. Ginsburg finds limited support that signing BITs containing binding arbitration clauses are correlated with weaker legal institutions in the future. The harmful effect of substitution may be exacerbated in developing countries or already weak rule-of-law states. In a study of commercial arbitration in

Mechanism:	Competition	Norm Transfer	Reform Pressure
Direction of effect:	↑	↑	↓

Table 1: Causal Pathways and Expected Effect on Legal Development

Sudan, Massoud (2014) argues that the Sudanese regime promoted ICA in order to provide high-quality legal services demanded by foreign investors without risking spillover of such services into the broader judiciary. Arbitration thus grants key interest groups access to a highly competent and neutral contract enforcement institution, without undermining the regime's use of the judiciary as a tool for maintaining a repressive public order. This dramatically reduces the opportunity costs nondemocratic states face for failing to invest in reforms promoting transparency, accountability and efficiency within domestic legal institutions.

In sum, the literature has identified three causal pathways through which the growth of international arbitration is expected to influence the development of local legal infrastructure (see Table 1). While the existing models describing the interaction between international arbitration and local courts arrive at conflicting conclusions, they nevertheless seem to agree on the set of mechanisms that could be at work: competitive pressures, elite-driven norm transfer and political coalitions for reform. They disagree, however, over how those mechanisms are operating. Both sets of scholars largely agree that arbitration will to some extent deprive local courts of cases. But we do not know to what extent this diminishes state control over the adjudicative process or lessens political pressure from commercial interest groups for reform. Many would agree that promoting integration with transnational arbitral practice may lead to some knowledge and normative transfer, but, again, we do not know how much knowledge is transferred, to whom and whether that translates to broader reform and therefore improved outcomes overall. In the next section I situate the specific debate about international arbitration and the rule of law in the broader literature on globalization and the development of transnational, private governing institutions. Bringing these strands of research together provides useful tools for understanding the domestic effects of transnational

legal institutions by integrating the mechanisms of substitution and knowledge spillover within a common analytical framework.

3 Transnational Legal Institutions and the Unbundled the State

In this section, I draw on the concept of "unbundling" from work on globalization and apply it to political and legal development. One of the key consequences of technological change over the last two centuries has been the incremental "unbundling" of commerce (Baldwin, 2006). The first victim of the unbundling dynamic was the tight nexus between the locations of production and sale. Cheaper transport costs allowed for firms to fragment supply lines and production around the globe and ship to consumers anywhere. More recently, the firm itself has become unbundled as technology allows for the decoupling and sale of an increasingly large set of service-based tasks that were not thought of as tradable before the reduction of communication costs (Baldwin, 2006, 22-35). The common theme in each of these examples is that the efficient allocation of tasks between and within firms, occupations, etc. is largely a function of external and contingent technological and institutional constraints. As these constraints disappear or change, pressures build to alter the distribution of tasks which, in turn, disrupts traditional forms of political and economic organization. While this literature has focused primarily on the effect of technological change on the organization of production, firms, and occupations, I posit that we can fruitfully extend the concept of bundling and unbundling to state institutions in an age characterized by the proliferation of private and transnational sites of rulemaking authority unmediated by state actors.

A typical modern state is made up of "bundled institutions" that have authority over a wide set of diverse governance tasks. The judiciary is a prime example of a bundled, public institution. Broadly speaking, the same court will hear cases in any number of issue areas. This allows for a high degree of professional movement and knowledge sharing within bundled institutions. The same judge might sit on a national security case one week then an intellectual property case the next. Even in jurisdictions with distinct commercial courts, such as England and Wales, the judges appointed

to the court are part of broader, more general judicial organization and often sit on other courts hearing non-commercial cases. In addition to intra-institutional knowledge building, bundling also provides simple lines of accountability linking task to institution to outcome. Bundling thereby "internalizes externalities" which helps resolve collective action problems (Gerring and Thacker, 2004, 322-324). Because the policies of a bundled institution affect a wider range of actors, it is easier to identify negative externalities. This eases the process of building a coalition for reform as the policy affects a larger set of actors than it would have if the policy were implemented by an institution with a smaller task-set. This is especially true with respect to the law. Bundled legal institutions enhance public accountability by developing and applying broad principles to disparate cases, reducing the risk of contradictory rules forming in different issue areas.

Bundling comes with risks, as well. Generalist public officials and broad principles, while providing simplicity, might not offer the most optimal solution to any given problem. One benefit of unbundling is the creation of specialized, nimble governing authorities. In the regulatory space, private authorities often develop when consumer demand is unmet by unresponsive or overstretched public entities. One example of this occurred after food scares in the 1990s, when the British government imposed steep fines and strict liability on retailers for tainted food products they sold. That liability both incentivized the food retail industry to create strong private mechanisms for standard setting and monitoring of food safety practices, but also provided the state a mechanism for ratcheting up or down the level of regulation through its interpretation of that liability. This ultimately led to creation of what is now called GLOBALGAP, an effective transnational, private food regulatory body (Meidinger, 2011). GLOBALGAP is one of many such bodies making up the global field of private regulatory bodies for food. One key to its success has been the sustained role of governments in directing the goals of GLOBALGAP and its relation to other bodies in the space. Abbott and Snidal (2009) refer to this as the varying extent to which a state can "orchestrate" the regulatory activities of transnational private bodies. Such transnational regimes work "where government and private actors carry out many similar activities and overlap, cooperate, compete, feed off, and sometimes mimic each other" (Meidinger, 2011, 243).

While the orchestration model was developed to explain varying outcomes in transnational regulation, the concept carries implications for the underlying public institution as well. Given the state's continued involvement in the maintenance of the regulatory space, civil society remains invested in the quality of the public institutions orchestrating the private bodies. Adopting an orchestration model can thus lead to enhancements in the quality of the bundled state institution. The state institution must commit resources to monitor, learn and direct its regulatory intermediaries. By successfully deploying its ideational and material resources to orchestrate the unbundled, private rulemaking authority, the state remains a site of political accountability (Abbott et al., 2016, 4). Orchestration thus creates dependencies and complementarities between the private and public institutions. This allows for the resulting public-private governing complex to take advantage of both the flexibility and expertise of the specialized, unbundled task-set while retaining the simple lines of authority that enhances public accountability. For example, Franck argues that national courts are natural complements to investor-state arbitration because the success of ISDS depends on the "critical support" public courts provide to the process (Franck, 2007, 367-370). They do this by imposing stays on parallel judicial proceedings, enforcing interim measures, appointing arbitrators and so on. If courts provide the necessary infrastructure for arbitration to succeed, then local actors retain an interest in promoting reforms that benefit users of the legal system outside of commerce.[2] If, however, arbitration has minimal to no institutional linkages with local legal institutions, then we should expect a reduction in the incentive to invest in reform due to commercial actors' diminished reliance on local institutions.

The growth of transnational rulemaking institutions disconnected from public accountability not only risks reducing international reform pressure, but domestic pressures as well. Abbott and Snidal (2009, 558) write that such "orchestration deficits" serve as transnational governance's "most serious limitation." Because of the latitude given to contractual parties in defining what constitutes an "international" contract or dispute and the mobility of capital today, domestic actors can take advantage of the growth of transnational rulemaking institutions, as well. Sharafutdinova and

[2]Though, as I argue below, only a very limited set of courts, typically in countries like the US, UK, France and Switzerland, tend to serve this role for most international arbitrations.

Dawisha (2017) call this phenomenon "institutional arbitrage," whereby well-resourced domestic actors can exit out of national rulemaking institutions. The authors present evidence that Russian oligarchs and commercial interests have taken their capital abroad in order to avoid local institutions and take advantage of British courts and international arbitration bodies like the London Court of International Arbitration or the International Chamber of Commerce (ICC) to settle disputes and enforce contracts (pp. 369-71). The availability of these institutional exit options worsened the collective action problem facing Russian commercial interests (which had a history of advocating for liberal legal reform) when faced with an increasingly extortionate and illiberal state (pp. 364-5). It became easier to simply rely on transnational contract enforcement institutions than to lobby for domestic reforms. Sharafutdinova and Dawish thus go one step further beyond what I argue here. They argue that the availability of high-quality, transnational contract enforcement institutions not only reduces political pressure for domestic reform but instead *increases* the incentives for local business elites to maintain the illiberal domestic status quo. As they write, "business elites take advantage of weak institutions at home to make profits, while using strong institutions abroad to safeguard them" (p. 363).

Another proposed causal pathway, emphasized by Rogers (2015), is through the diffusion of norms and knowledge through elite actors that move between transnational and national settings. For this to occur, professionals and experts in the private and public institutions must move between each site of authority, carrying with them "best practices" or higher expectations of local institutions that lead local elites to lobby for reform. Prior research on norm transfer has found that progressive standards tend to diffuse where actors with incentives to promote reform move between sites with relatively "high" and "low" standards. For example, the work on the diffusion of womens' rights through trade and foreign direct investment (FDI) argues that the diffusion of such norms happens because of the greater integration of women into a workforce increasingly defined by multinational firms with relatively more progressive gender policies (Neumayer and de Soysa, 2011). Crucially, diffusion depends on women moving from the site of higher standards (the MNC) into sites with lower standards (local firms) and demanding change. Without movement and

		State Orchestration	
		High	Low
Professional Integration	High	Enhancement	Mixed
	Low	Mixed	Stagnation

Table 2: Theoretical Expectations

political demands, there is no mechanism of change. In the case of private governance, we need to identify bidirectional movement within and integration between the national and transnational professional classes granted governing authority.

To summarize, institutions can be thought of as bundles of tasks and authorities. Increasing economic interdependence has put pressure on state institutions to delegate authority to private transnational authorities. As private, transnational institutions develop to take over tasks that were previously bundled in more general public institutions, rulemaking authority risks becoming more diffuse, decentralized and complex. Increased complexity risks entrenching the power of well-resourced actors, while the export of governance authority risks subverting local political and legal development incentives. The framework presented here highlights two aspects of the design of transnational institutions that influences these outcomes. First, if the resulting public-private governing complex allows for state orchestration, then the quality of the unbundled local institutions is expected to be enhanced due to the added capabilities from integrating with a transnational authority paired with the sustained political pressure from interest groups to maintain governing quality. An alternative possibility is that the private body offers an independent functional equivalent to the public institution that allows for only minimal or even no state oversight. Because some subset of actors can then select out of the public institution into the private institution, the political and economic pressure to reform the public institutions decreases. The second factor is the degree of integration between transnational and national professionals. Professionals moving

between the transnational and national realms may support the transfer of norms and knowledge from one realm to the other. High orchestration and high professional integration between private and public bodies should have an *enhancing* effect on local rule of law institutions. Whereas I expect low orchestration and low professional integration to have a *stagnating* effect. In the next section I apply this framework to the case of international commercial arbitration.

4 ICA as an Unbundling Institution

This study builds on the rich and growing literature on the interaction between intergovernmental organizations and domestic institutions by exploring the unique dynamics of private, transnational governance. Why focus on international commercial arbitration? Prior work testing the relationship between investor-state dispute settlement (ISDS) and legal development has found mixed results (Ginsburg, 2005; Rogers and Drahozal, 2022). There are a few aspects of ISDS that limit its potential to substitute for local institutions. First, ISDS might be better described as a complement due to the frequent requirement to exhaust local remedies before an ISDS panel can grant itself jurisdiction over a dispute. Second, the influence of ISDS on domestic development incentives may be weak because it is not a very active international dispute resolution regime relative to ICA. In 2018, 56 cases were filed at the International Centre for Settlement of Investment Disputes (ICSID), a popular ISDS venue within the World Bank. Compare this to the 842 cases that were filed at just the International Chamber of Commerce the same year (141 of which involved a state-entity); 301 cases at the London Court of International Arbitration; 152 cases at the Stockholm Chamber of Commerce; and 343 cases at the Singapore International Arbitration Center. Given the relatively small ISDS caseload, perhaps foreign and domestic firms may still feel the need to push for more neutral, expert, efficient and predictable local dispute resolution mechanisms in countries that are party to treaty-based arbitration clauses. Third and relatedly, ICA's larger caseload is driven by the wider jurisdictional scope of ICA relative to ISDS. ISDS deals primarily with international law violations, many of which do involve contract disputes with host states. ICA by contrast is equipped

to resolve any cross-border contract dispute (very broadly defined). Any international contract can be written to shift related disputes from a local court to an ICA panel. ICA therefore provides a more complete substitute for a country's local contract enforcement institutions that applies to both fully private as well as public-private disputes. The comparatively limited ambit and activity of ISDS may help explain the mixed findings to date. In sum, while there are many institutional similarities between ISDS and ICA, the increased activity, the broader jurisdictional scope, and, as Rogers argues, its deeper integration with local legal institutions suggest that ICA is more likely to influence the development of local legal institutions for better or for worse (Rogers, 2015).

International arbitration as is just one part of a burgeoning movement to unbundle domestic judiciaries to the benefit of international commerce. We see this dynamic also at work with the rapid development of commercial courts and "legal hubs" that cater to the needs of international commercial actors (Bookman and Erie, 2021). Many of these activities are concentrated in authoritarian states seeking to enhancing their "legitimacy as a legal service provider" without extending these services to the broader, local population (Erie, 2019). For example, high-capacity autocratic states such as Qatar, Saudi Arabia, Singapore and China are actively developing and promoting their international commercial courts to foreign commercial actors (Bookman, 2020, 239-60). As Bookman (2020, 40) argues, these states are not motivated to make "better" courts. Instead these countries consider the development of specialized courts for commercial actors as a means of competing for foreign capital (or legal services export) without the need to invest in reforms promoting transparency, efficiency and independence throughout their domestic-facing judiciary. While the goal of the present article is to focus on one aspect of the broader strategy of unbundling (i.e. commercial arbitration), it should be noted that states around the world are experimenting with novel institutional methods for providing high-end legal services to international commercial actors in order to attract foreign capital without investing in similar reforms for domestic publics.

In the rest of this section I briefly situate the international commercial arbitration regime within the analytical framework discussed above, evaluating how ICA fares on each of the relevant dimensions. I begin with a short discussion of the competition hypothesis. Then I argue that ICA

admits minimal state orchestration and therefore creates few institutional dependencies that would retain simple lines of accountability and political pressure for reform. Finally, I examine the limited potential of ICA to promote exchange between transnational and national legal communities.

Institutional competition and the "race to the top." One proposed benefit of unbundling is the creation of competition between the specialized and bundled institutions. This is the logic behind Franck's "race to the top" hypothesis (Franck, 2007, 367-368). For competition to produce a "race to the top," however, there must be some mechanism by which competition creates costs that the public institution will seek to minimize or recoup. As the judiciary is not compensated on a per-case basis, it is unclear what those costs would be. Judges retain their salary and the judiciary as a whole retains its monopoly on the rest of its adjudicative task-set. To the extent that public institutions are insulated from competitive pressures we might see the opposite outcomes, that the state sees a *benefit* from a private alternative that provides an exit option for discontented actors (Gerring and Thacker, 2004, 317-318). This is especially true in autocratic states, where the growth of a private judicial alternative would relieve pressure from commercial interests on the state to implement reforms promoting judicial neutrality, predictability, expertise and independence. Privatization therefore enables autocratic states to provide neutral, efficient judicial-like adjudication while maintaining a tight control over the judiciary in matters of public order (Massoud, 2014, 19-21).

Outside of arbitration, the growth of public international commercial courts suggests that rather than a "race to the top" we see states participating in the public unbundling of commercial and non-commercial judicial functions (Bookman, 2020). There are thus few judicial competitive forces at work that might lead to a "race to the top" between public judiciaries and private arbitration institutions or their public offshoots. Where there is competitive pressure for other goods (such as foreign investment), we see states respond by further unbundling judicial work through the construction of commercial courts, further limiting the positive externalities of a bundled judiciary. As Ginsburg (2005, 119) puts it, local judges do not internalize the benefits of the law they provide. Therefore, there is little reason to expect courts to suffer when dispute resolution is outsourced to a third-party—judges do not lose from the growth of arbitration. We should therefore expect the

quality of local legal services to instead be the product of *political* coalitions pressing for reform.

Low levels of state orchestration. If the state is still involved in orchestrating a private authority, then the users of the private authority will remain invested in the quality of the state-orchestrating institution too. As Franck (2007, 369) argues, "national courts provide critical support to the investment arbitration process. There are various points in the process where the integrity of local courts can impact the efficacy of the dispute resolution process." If this is true, then a private "exit option" will likely not have the effect of relieving pressure on bundled institutions to invest in reform. Alternatively, low levels of orchestration can instead reduce pressure for reform. As I argue below, however, opportunities for state orchestration over ICA have been declining for decades. The two main opportunities for orchestration for ICA are in the design of domestic legislation governing ICA and in the judicial enforcement of arbitration agreements and awards. I deal with each of these factors in turn.

There are many ways a country can both promote ICA and orchestrate its practice. A country can grant the right to judicial review on the merits; require arbitrators to state the reasons for their decisions; require that awards be made public; etc. Few countries do so. Instead, most countries enacting ICA reforms today base those reforms on the UNCITRAL Model Law on International Commercial Arbitration, which expressly denies all of the potential orchestration mechanisms outlined above. The Model Law is considered the "gold standard" of the modern ICA regime. It is the standard against which all ICA reform is measured today. Pressure from UNCITRAL has thus been instrumental in harmonizing and increasing ICA protections around the world. While there is some variation in the enactment of these reforms, by and large the reforms are quite uniform across jurisdictions (Binder, 2010). Because the pressure for reform typically comes from a desire to attract capital, rather than reform of the judiciary, countries have opted into adopting the Model Law with minimal revision. A second homogenizing force is the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (1958), commonly referred to as the New York Convention (NYC). This convention allows for the enforcement of arbitration agreements and awards in any other signatory jurisdiction while at the same time (like the Model Law) prohibiting

essentially any form of judicial oversight. Competition for trade and investment drive states towards focal standards such as the Model Law and New York Convention and incentivized states to limit the scope of orchestration over the practice. Outside of the major arbitration jurisdictions like the United States, France, United Kingdom and Switzerland, there is little room for less prominent countries to orchestrate arbitral practice.

Another avenue of orchestration is for courts to carve out certain areas of law over which they have exclusive jurisdiction. Arbitrators today have wide latitude to base decisions on their own interpretations of almost any relevant rules of law. Judiciaries in the major arbitration states have been gradually increasing the authority of arbitration to interpret and apply public law. For example, through a series of interpretations of the Federal Arbitration Act, the United States Supreme Court has increased arbitrator's powers to rule on mandatory rules. This has given actors an avenue to circumvent mandatory rules in areas like securities law and antitrust (Guzman, 2000). European courts have similarly granted increased authority to arbitration panels to root decisions in their own interpretations of mandatory EU law (Stone Sweet and Grisel, 2017, 178-185). Stone Sweet (2006) argues that this deference has led to the transnationalization of commercial law and its decoupling from domestic law. Using both legal analysis and interviews with practitioners, Karton (2013) finds that the culture of ICA has led arbitrators to arrive at unique, though internally consistent, interpretations of domestic law (which, despite the divergence, public courts are required to enforce). If the legal reasoning of an arbitration award were reviewable by a court for errors in law, this would not pose any problem. But the Model Law bars courts from reviewing arbitral awards for mistakes of law, further limiting the opportunity for state orchestration through judicial oversight.[3]

A final potential avenue for state orchestration written into both the New York Convention and the Model Law is an exception that allows courts to deny enforcement of awards that cut against "public policy." The scope of this exception is very narrow and appears to be shrinking (Redfern and

[3]Indeed, despite its arbitration laws being inspired by the Model Law, Romania was not recognized as a Model Law country because of a provision that allowed Romanian courts to annul an arbitration award if the award were based on a legal provision that was deemed unconstitutional, see Leaua (2013).

Hunter, 1999, 471-474). Recently, courts in major enforcement states have increasingly interpreted this to mean not domestic public policy but *transnational* public policy. Courts in Italy, France and Switzerland have ruled that public policy challenges to international arbitration awards should be considered in light of international—not national—policy grounds, further limiting domestic authorities ability to orchestrate arbitration practice (Stone Sweet and Grisel, 2017, 147-150).

Minimal professional integration. Finally, in the absence of competitive pressures or institutional complementarities through state orchestration, rule-of-law norms may flow from ICA practice into local practice through a process of normative spillover. As discussed above, normative spillover requires social and professional interpenetration between the sites of normative export and import. But in the highly lucrative world international of commercial arbitration, it is typically a one-way street from public judge to private arbitrator. It is thus not uncommon for ICA to instead encourage the *export* of actors with strong credentials for independence and competence from the public to the private sector, not the other way around.

Nor is it clear that integration into the ICA regime will bring increased interpenetration between national and transnational sites of authority. Instead, it seems that ICA leads to a professional reorientation away from the local and towards more lucrative transnational practice. Dezalay and Garth (1996, 243) find that the burgeoning arbitration profession in Egypt typically shunned local professionals and institutions: "A state company lawyer underscored this point by referring to a list of fifteen top arbitrators who would be acceptable as the chair of an important arbitration—none were Egyptians." Second, the structure of the arbitral regime works against the diffusion of norms through lawyers working in local and transnational contexts. Instead, local professionals may seek to take advantage of ICA as a means of escaping local practice. Dezalay and Garth find that the introduction of Model Law-based legislation in Egypt helped spur "many conferences, workshops, and training sessions...[for which] many leading figures in the world of arbitration are brought to Cairo, adding stature to the Cairo center, gaining attention to Cairo, and not incidentally letting Cairo have a look at the stars of the [ICC] core [in Paris]." But they found little evidence of an increase in the number of arbitrations seated within the country (Dezalay and Garth, 1996, 242-

244). This is likely because contractual parties tend to select seats in jurisdictions that have robust legal institutions out of fear that a court in a weak rule-of-law jurisdiction will annul an award adverse to a local firm or state entity. Because of this, even when states actively promote arbitration as a mechanism for dispute resolution, it is unclear what effect increasing arbitral practice by local firms would have on local courts outside of a decline in caseload and authority.

In sum, there is little reason to believe competitive pressures will nudge local courts to invest in costly reform. The modern ICA regime is designed to prevent orchestration thereby removing the state from the regulation of commercial disputes. And rather than providing a mechanism for importing rule-of-law norms, ICA may instead encourage the export of local legal talent to more lucrative opportunities abroad. These three factors together push the state into the background and minimize whatever incentives would otherwise exist to invest in costly legal reforms. We should therefore expect to find stagnation or a *negative* association between the promotion of ICA and legal development. In the next section I test this hypothesis on a cross-national panel of countries that have implemented UNCITRAL's Model Law on ICA.

5 Data and Methods

Dependent Variable: Legal Development. The "rule of law" is a notoriously slippery and multifaceted concept. I make no pretension to contributing to the vast literature on the rule of law as a concept. Instead, I draw my operating definition from the growing field of rule-of-law development practitioners. This definition is particularly useful here because it represents the approach adopted by the very experts from whom public officials often seek advice and know-how when implementing rule-of-law reforms (Carothers, 2006, 10-11). If there is reduced pressure for legal reform, then we should expect to see a reduction in legal development along the lines defined by the international development community actually involved in legal development efforts around the world. These practitioners deploy what Rachel Kleinfeld refers to as an "institutional approach" for promoting the rule of law (Kleinfeld, 2006, 47-54). They focus on a set of concrete institutional

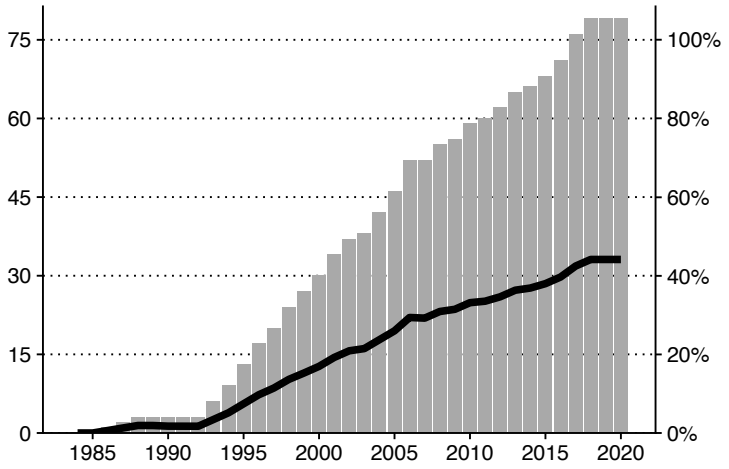
reforms. Kleinfeld identifies three main features of such a definition:

- "**Laws**...which are publicly known and relatively settled;
- "A **judiciary** schooled in legal reasoning...efficient...[and] independent of political manipulation or corruption; and
- "A **force able to enforce laws**, execute judgements, and maintain public peace and safety" (p. 47)

Kleinfeld's synthesis accords with common strategies adopted by rule-of-law development practitioners. The American Bar Association's Rule of Law Initiative, for example, focuses on these very institutions through its legal development efforts supporting broad-based reform initiatives such as "drafting and implementing codes of judicial ethics; promot[ing] judicial education and training; and help[ing] to enhance court administration and efficiency."[4] Moreover, each aspect of this definition is tied to the interests of commercial actors seeking fair treatment and efficient, predictable contract enforcement. In the absence of an exit option, commercial actors would have an interest in pressuring the state to pursue goals that align with the "best practices" of the development community. This definition thus serves to capture both what is lost when commercial interest groups exit to international arbitration and the practices adopted by the kinds of actors to which states that do feel the pressure to invest in reform would turn.

I use the Rule of Law Index from the Varieties of Democracy Project (V-Dem) to measure the quality of rule of law institutions cross-nationally and over time (Pemstein et al., 2018). The V-Dem Rule of Law Index an aggregation of expert-coded measures pertaining to both the independence and competence of multiple levels of each country's judiciary along with other aspects of modern legal development including the openness and transparency of laws, judicial independence, access to justice, quality of public administration, and the predictability of enforcement (Coppedge et al., 2020, 281-2). Aside from the substantive similarity this index has to the definition of the rule of law adopted here, the index is ideal because it has very wide coverage. It allows for the inclusion of over 150 countries in the sample across the full length of the relevant time span (1985, the year

[4]See https://www.americanbar.org/advocacy/rule_of_law/what-we-do/governance-justice-system-strengthening/



Note: Grey bars represent the total number of countries with Model Law-based legislation in force per year. The black line plots the global percentage of such countries per year (count of total countries per year is derived from Varieties of Democracy Dataset, v10).

Figure 1: Rate of National Legislation based on UNCITRAL Model Law on International Commercial Arbitration, 1985-2020

the UN General Assembly adopted the Model Law). This is ideal compared to other measures that either have an overly narrow theoretical focus or cover a relatively short a time span.

Independent Variable: Protections for International Commercial Arbitration. To proxy for integration into the transnational ICA regime, I collected data on the enactment of domestic legislation based on the UNICTRAL Model Law on ICA. The Model Law is considered to be the "state-of-the-art" in permissive arbitration laws. By 2020 over 75 countries had enacted national legislation based on the Model Law (see Figure 1). The data were collected from the UNCITRAL's yearly "Status of Conventions" reports. These reports update UNCITRAL members when a country is recognized by UNCITRAL for entering into force legislation based on the Model Law as well as all of UNCITRAL's other legal instruments.[5] Because of the flexibility built-in to all of UNCITRAL's legal instruments, it does not have an official and clear set of rules for inclusion in the reports. While UNCITRAL allows countries to shape local implementation as they see fit, transnational legal harmony is a primary goal (see Block-Lieb and Halliday, 2007). This discretion

[5]Due to some inconsistencies in the yearly reports, I verified all dates of entry into force by examining the implementing legislation in all Model Law countries.

does not mean that any country can win the approval of UNCITRAL as a "Model Law country," however. UNCITRAL has an interest in maintaining the value of its legal instruments as not only guides for commercial law reform, but also as heuristics for the international legal and commercial communities. This has led to significant legal harmony across Model Law jurisdictions. As one Senior Legal Officer at UNCITRAL writes, there is a "high degree of substantive uniformity in the implementation of the [Model Law]" (Faria, 2005, 22). An independent analysis of all Model Law countries in 2010 found a similar degree of harmony between jurisdictions (Binder, 2010).

By using the Model Law as a proxy for a permissive ICA regime my analysis leaves out some jurisdictions that are arbitration-friendly but have not based their law on the Model Law. Many of the major enforcement jurisdictions are in this category such as the United States, United Kingdom, France, Switzerland, Sweden, and others.[6] The primary difference between these two groups is the publicity afforded Model Law countries when they win UNCITRAL recognition and the utility of that marker as a heuristic for outside actors considering doing business in the country. Given the amount of money at stake in international trade and investment, the arbitration community is expert, well-informed and sensitive to changes in domestic laws governing ICA around the world, so it is unlikely that UNCITRAL recognition would create material differences between Model Law and non-Model Law arbitration-friendly countries. Either way, this measurement error is mitigated when I restrict the sample to weak rule-of-law countries, as pro-arbitration, non-Model Law countries tend to be high-income countries with robust legal systems.

Estimation Strategy. I estimate the effect of enacting strong protections for ICA on the quality of local legal institutions using a difference-in-differences (DiD) estimator with weighted matched sets (Imai, Kim and Wang, forthcoming).[7] I adopt this approach because of recent work on the standard two-way fixed effects estimator (TWFE) that has identified the potential for bias when treatment assignment is staggered (e.g., Borusyak and Jaravel, 2017; Imai and Kim, 2021; Goodman-Bacon, 2021; Strezhnev, 2018). The estimator used below helps resolve these issues with TWFE

[6] It should be noted that some subnational units have enacted Model Law-based legislation including Scotland in the UK and Texas, California, Illinois and others in the USA.

[7] I use the authors' `PanelMatch` R package for the estimation below.

as it accommodates treatment effects that are heterogeneous across units and time and prevents mismatched comparisons between already-treated and newly-treated units. A further benefit of this method is that it allows for the simple evaluation of covariate balance.[8]

The goal of the procedure is to estimate change in the trajectory of the quality of a country's legal institutions caused by enacting the Model Law. The problem is that we cannot observe what a country that did enact the Model Law would have looked like if it had not enacted the Model Law. To estimate that counterfactual, I construct a unique "control group" for each Model Law country made up of non-enacting countries (called a matched set, $\mathcal{M}_i$). To improve the comparability between each Model Law country and its matched set, I weight the observations within every matched set based on how similar each country is to its matched Model Law country. Countries that did not enact the Model Law but are just as likely to have enacted the Model Law (compared to the country the *did* enact it) are given a greater weight than countries that are more or less likely to have done so. I then calculate the change in the weighted control group's rule-of-law score from the year prior to the Model Law entering into force and subtract this from the change in the Model Law country's rule-of-law score over the same duration. I average the difference-in-differences across all of the Model Law countries for each time period to yield an average effect of the Model Law on legal development for the year it enters into force and each of the following five years. The six year window (including the year of enactment) was chosen in order to allow enough time for any effect of the Model Law to appear while also including a sizable set of countries in the analysis.[9] Importantly, this estimator relies on the common trends assumption that the difference between the trajectories of the treated and control units would have remained stable in the absence of treatment, conditional on a set of time varying covariates (Imai, Kim and Wang, forthcoming, 10-11). I first outline the estimation procedure in greater detail before presenting the results.

First, I set a time-window for the analysis, F. The results reported below estimate the effect of the Model Law over a five-year period, $F = [0, 5]$. I then construct a matched set for each treated

[8] See Figure C1 in the Appendix

[9] Any country that does not have at least five years of post-enactment data is dropped, so the data only include countries that enacted the Model Law on or prior to 2014. Expanding the window would therefore reduce the size of the Model Law sample. The results are robust to longer time windows. See Appendix B.

unit i, denoted $\mathcal{M}_i$, which includes all countries that have not yet enacted legislation based on the Model Law. Any unit that enacts the Model Law between the time country i enacts the Model Law and five years thereafter is dropped from i's matched set.

The next step is to refine each matched set to improve the comparability between the Model Law countries and their matched sets. This is done by using logit regression to estimate the propensity of each matched unit to have enacted the Model Law. Typically, these propensity scores are used to identify a subset of the full matched set that is most similar to the treated unit. "Nearest neighbor" matching, for example, simply selects the matched unit that has an estimated propensity to receiving the treatment closest to that of the treated unit. King and Nielson (2019) caution against using propensity scores for this style of matching because the resulting control group can be highly dependent on the model used to estimate the propensity scores. I mitigate the potential for model-dependence by weighting every country in the matched set rather than matching a treated unit to a limited (and equally weighted) subset of its matched set. The weights used in the results reported below are calculated from either propensity scores (PS) and the covariate balancing propensity score (CBPS) developed by Imai and Ratkovic (2014).

The propensity scores are estimated by regressing the treatment variable, enactment of the Model Law, on a set of covariates. I include four institutional covariates. First, I include V-Dem's Polyarchy index, which, like the Rule of Law index, is a composite measure running from 0 to 1 designed to measure the level of electoral democracy in a given country. Democracy is highly correlated with the Rule of Law and a relatively high percentage of democratic states have enacted legislation based on the Model Law. Second, I include a count of currently in force BITs. BITs provide access for foreign investors to international arbitration through ISDS. ISDS and ICA are highly interdependent systems with similar relationships to local courts, so it is possible that the effect of the Model Law might be amplified when a country is also integrated into the ISDS regime (Rogers and Drahozal, 2022). Third, I include an indicator variable for enactment of the New York Convention. Finally, I include the dependent variable of the second stage of the analysis, the V-Dem Rule of Law Index.

I also include a set of economic covariates. Countries that are more integrated into the global economy face greater pressure to provide neutral dispute resolution services and therefore may be more likely to invest in both capacity-enhancing legal reforms and transnational contract enforcement regimes like ICA. I therefore include a battery of economic variables that could influence both pressure for reform and access to legal development assistance. I include measures of logged GDP, GDP per capital, GDP growth to help adjust for any confounding effects of market size and economic development trajectory. These data were obtained from the World Bank's World Development Indicators. To measure a country's dependence on foreign direct investment (FDI), I obtained data on the total inward FDI stock as a percentage of GDP from UNCTADstat. Finally, I include a measure of total trade as a percentage of GDP, which I obtained from the Penn World Tables. I lag all explanatory variables by one year.

The final step of the procedure is to estimate the average effect of treatment on the treated (ATT) in the year of enactment of the Model Law (t_i) and for each of the five years thereafter (F). I apply the following DiD estimator for each time period F:

$$\widehat{ATT_F} = 1/N \times \sum_{i=1}^{N} \left((Y_{i,t_i+F} - Y_{i,t_i-1}) - \sum_{i' \in \mathcal{M}_i} \omega_i^{i'} (Y_{i',t_i+F} - Y_{i',t_i-1}) \right)$$

N is the number of countries within the sample that have enacted the Model Law. t_i is the year in which the Model Law enters into force for each country i. $Y_{i,t}$ and $Y_{i',t}$ are the rule of law scores for Model Law and matched non-Model Law countries, respectively. The term $\omega_i^{i'}$ denotes the normalized weight applied to the rule of law score for each unit i' in the matched set of Model Law-enacting state i. This equation yields an estimate of the change in the rule of law score from one year before the Model Law enters into force to years $t_i + F$ for Model Law countries minus the weighted average of the change within each Model Law country's matched set over the same duration. I calculate this for each Model Law country then average the results for each time period. The $\widehat{ATT_F}$ is therefore the estimated average effect of the Model Law entering into force for each year beginning from the year of enactment through each of the following five years.

Years in Force (F)	ATT			
	(1)	(2)	(3)	(4)
0	−0.006	−0.009	−0.009	−0.001
	(0.004)	(0.007)	(0.007)	(0.002)
1	−0.010	−0.017	−0.017	0.001
	(0.006)	(0.010)	(0.010)	(0.002)
2	−0.015	−0.025	−0.025	0.000
	(0.009)	(0.015)	(0.015)	(0.002)
3	−0.018	−0.031	−0.031	0.001
	(0.009)	(0.016)	(0.016)	(0.002)
4	−0.028	−0.048	−0.048	−0.001
	(0.012)	(0.021)	(0.021)	(0.002)
5	−0.026	−0.048	−0.048	0.002
	(0.013)	(0.024)	(0.024)	(0.003)
Refinement	CBPS	CBPS	PS	CBPS
Sample	Full	Low RoL	Low RoL	High RoL
Countries	64	39	39	25

Note: Table reports yearly estimates of the average treatment effect on the treated. Standard errors in parentheses are estimated via blocked bootstrap with 5,000 iterations.

Table 3: Results

6 Results

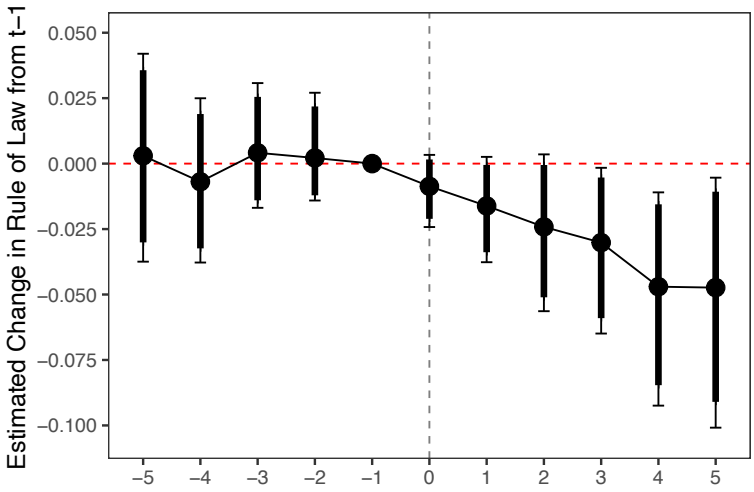
The results are reported in Table 3. The estimate in each cell represents the effect of the Model Law on the rule of law score for each year relative to the year just before the Model Law entered into force. For example, the year 5 cell in Column 1 indicates that five years after enacting the Model Law countries have, on average, a rule of law score .026 points below what they would have had if the country had not enacted the Model Law. Year 1 of Column 1 estimates that there is no significant difference between the observed rule of law score and the counter-factual estimate (i.e. if the country had not enacted the Model Law), one year after entering into force.

Column 1 reports the results when estimating the model using data from the full sample. While the Model Law and control groups are indistinguishable in the year of enactment, we see a gradual relative decrease in the Rule of Law score for Model Law countries. The gradually increasing

divergence between Model Law and non-Model Law countries is consistent with the framework presented above. We should not expect an immediate and "large" effect to manifest itself through a complex bundle of institutions like a legal system after the enactment of a single reform package. It takes some time for the legal and behavioral changes brought on by the Model Law to influence broader legal development in the country. Parties must opt-out of national judicial institutions by negotiating arbitration clauses into their contracts. Therefore, there should be some lag as firms shift their attention away from the judiciary and local rules and onto transnational arbitration centers. Exit by commercial parties from the local legal institutions lowers outside pressure on the state to invest in the progressive reforms like reforming archaic procedures, improving judicial training, increasing salaries, funding domestic law schools and legal training, and so on. This process leads to the gradual reduction in political pressure for investment in progressive rule-of-law reforms, which allows for problems in the legal system to persist and accumulate.

We are most interested, however, in the interaction between ICA and local institutions in counties that do not already enjoy a high quality, consolidated legal regime. Unpacking how ICA interacts with legal institutions in weak rule-of-law countries is important because the Model Law is embedded within broader development efforts to promote the rule of law in developing countries. As Rogers and Drahozal (2022, 1) put it, there is "an implicit promise of investment arbitration...that it will not only provide protection of foreign investors, but also foster good governance in developing and emerging economies." The sample in Column 1 includes enacting countries that have both high and low Rule of Law scores. The estimates in Column 1 may be biasing the results downward for a couple of reasons. First, countries that enjoy robust legal systems may not be actively engaged in legal reform, so a reduction in pressure for reform would have little effect on legal development. Second, weak rule of law countries tend to have fewer resources to devote to different reform projects. Minimizing pressure for legal reform may have a larger negative impact in those countries than in countries with more resources to devote to reform.

To examine the effect of the Model Law on countries with weaker legal infrastructure, I re-run the analysis after dropping all cases of strong rule of law countries that have enacted the Model



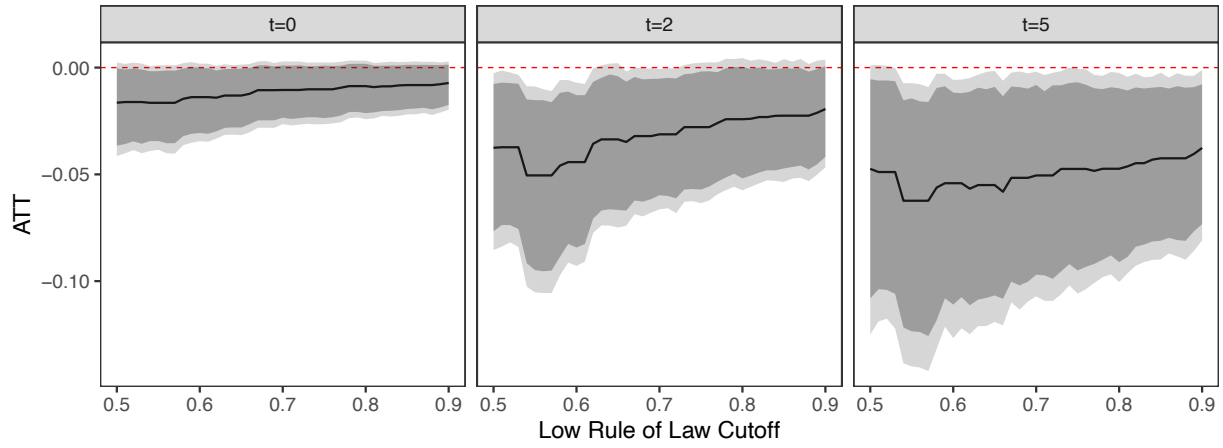
Note: Plots estimated change in rule of law from time $t-1$ for low rule of law sample (Table 3, Column 2). 90% and 95% confidence intervals are estimated via blocked bootstrap with 5,000 iterations.

Figure 2: Estimated change in Rule of Law Index 5 years before and after Model Law enactment

Law from the dataset. I classify as "low rule of law" any country with a Rule of Law Index less than .8 at the time of enactment of the Model Law. As a frame of reference, Bulgaria, a Model Law country, has hovered around .75 for the last decade. Another Model Law country, Mexico, has fluctuated between .5 and .65 over the last decade. Just above the cut point is Greece, which had a score of .82 in 2017. The results for this subsample are reported in Columns 2 and 3.[10] Comparing Columns 1 and 2 we see that the ATT for Low Rule of Law countries is roughly double that of the full sample. We also see the same pattern of gradual institutional degradation relative to the control group. The model estimates that, on average, five years after enacting the Model Law a country is around .048 points below where it would otherwise have been. This comes out to a cumulative effect over five years of a decrease of roughly 15% of a standard deviation of the Rule of Law score in the sample. I estimate a 25% SD decrease after a decade (see Figure B1 in the Appendix). The difference between weighting by propensity scores or covariate balancing propensity scores is negligible (compare Columns 2 and 3).

Figure 2 plots the ATT for weak rule-of-law countries (i.e. Table 3, Column 2). As was the case with the full sample, the non-Model Law and Model Law groups are statistically indistinguishable

[10] A full list and categorization of the Model Law countries included in the analysis can be found in Appendix A.



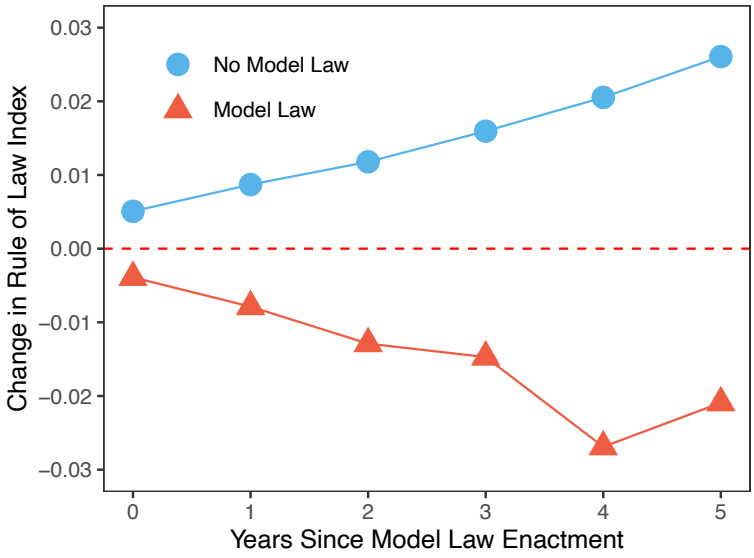
Note: Figures plot estimates for $F = [0, 2, 5]$ from analyses that implement various cut points to define "low rule of law" countries. As above, 90% (dark shaded region) and 95% (light shade) confidence intervals are estimated via blocked bootstrap with 5,000 iterations. For the complete results see Figure B2 in the Appendix.

Figure 3: Alternative cutoffs

for the first 2-3 years after enactment. Whereas by around the third year after implementation, the Model Law group becomes statistically distinguishable from the non-Model Law group (at the .05 level), with an estimated Rule of Law Index score of .03 less than that of the non-Model Law group. This figure also presents the results of a "placebo" test to help assess the common trends assumption: that Model Law countries and their matched sets would not differ in the absence of Model Law enactment. To do this, I estimate the "effect" of the Model Law on legal development *prior* to enactment of the Model Law (i.e. years −5 through −2 in the figure). The flat line prior to enactment suggests that any differences in the trajectories between the two groups in the years leading up to enactment are minuscule and highly statistically insignificant.

Does the Model Law exert a similar effect on countries with already consolidated legal regimes? It appears not. Column 4 reports the results for the high rule of law sample. Unlike with weak rule of law regimes, there appears to be no effect of the promotion of ICA on legal development in already consolidated legal regimes. The estimated effect is very small and jumps above and below 0. I estimate the effect of Model Law enactment to be a highly insignificant increase of about .002 points (~0.5% of a standard deviation) after five years.

To ensure these results are not overly sensitive to how I categorize "high" and "low" Rule of



Note: This graph plots the average changes in Rule of Law Index from year $t-1$ for Model Law and non-Model Law countries separately based on estimates from Table 3, Column 2.

Figure 4: First Differences

Law scores, I re-run the analysis using other cut points. The results are presented in Figure 3. These plots show that estimates presented in Table 3 are largely consistent across a range of other plausible cut points. As in the main results, we see a gradual reduction in Rule of Law scores after Model Law enactment across all analyses. Interestingly, the upward slope in each plot indicates that the effect size decreases as the mean rule of law score in the "low" rule of law group increases, suggesting further that countries with weaker legal systems are more susceptible to institutional erosion.

What is driving this divergence? One benefit of the DiD estimator is that we can disaggregate the second difference to see what is driving the growing divergence between Model Law and non-Model Law countries. Are legal institutions within recent Model Law countries weakening or are they simply not developing at the rate they otherwise would have? Figure 4 plots the estimated trajectories of the Model Law and non-Model Law groups individually (as opposed to Figure 2 which plots the yearly differences between these groups). The upper, blue line reveals that the non-Model Law group experiences steady improvement over time. By contrast, the red line,

representing the trajectory of the Model Law group, shows a slight decline in the quality of local legal institutions. This figure suggests that the effect is driven partly by institutional erosion within Model Law countries, but also partly by successful investment in local legal infrastructure in the non-Model Law comparison groups that the Model Law group does not enjoy. This is consistent with the theory presented above in which the exit of international and local commercial actors from the domestic legal system is expected to lower pressure on governments to invest in the costly reforms to improve the neutrality, competence and efficiency of local legal institutions, while at the same time reducing the opportunity costs (in terms of foreign investment and trade) faced by weaker legal systems.

7 Conclusion

The findings presented here suggest that the growth of transnational substitutes for domestic institutions may carry costs for the very countries they are often purported to assist. Particularly in light of the competing findings within the literature across ISDS and now ICA, extensions of the findings presented above should include greater empirical attention to the mechanisms of interaction between transnational and domestic institutions. I have attempted to set parameters around such an investigation by synthesizing the debate in a broader context of the growth of transnational private authority. The theoretical framework presented in this paper calls attention to two related phenomena: orchestration and professional integration. The former asks the extent to which local institutions retain rulemaking authority. The second mechanism, professional integration, demands a closer, cross-national examination of how ICA influences local professional incentives. The work of Dezalay and Garth (1996) and, more recently, by Grisel (2017) provide a foundation for such an investigation.

More broadly, the findings presented here lend support to the emerging body of scholarship in global economic governance that considers not just first-order effects but potential unexpected second-order effects as well. The findings reported here resonate, for example, with Bodea and

Ye (2020), who find that—beyond its effects on FDI—the international investment regime may be harming human rights practices abroad by limiting states' abilities to implement political, economic and social reforms that an arbitrator might deem harmful to the rights of foreign investors. Before declaring international arbitration a success for the rule of law because of the incredible ease by which international commercial actors can enforce contracts and protect their rights abroad, we need to evaluate potential downstream effects that are likely to hit emerging markets hardest.

The emergence of transnational, private authority in global economic governance comes with risks. Transnational authorities haven proven to be effective actors in the promotion of human rights as well as higher labor, environmental and product standards (e.g. Braithwaite, 2008; Abbott and Snidal, 2009). And much work remains to be done to better understand not just the effectiveness of transnational authorities themselves, but how the interaction between transnational and national authorities influences domestic governance outcomes outside of the narrow domain of any given transnational governance scheme. This requires increased focus on mechanisms for promoting complementarity between transnational institutions and their domestic counterparts (Puig and Shaffer, 2018). Progressive rule-of-law reform is most likely to succeed when foreign commercial actors and local civil rights groups have a joint interest in pressuring the state to invest in such reforms. The growth of substitutive international institutions risks undermining efforts in developing countries to invest in broad-based legal reforms by giving commercial actors an exit option unavailable to others. This emerging trend is especially important given the complexity of political accountability in global governance regimes. Simple lines of accountability channeled through visible, bundled domestic institutions facilitate coalitions for reform by clarifying the causal connections between governing institutions, tasks and outcomes. But the decentralized world of transnational authority diffuses accountability across an ever-growing array of overlapping institutions and shrouds political decision-making behind a veil of expertise. The theory and empirical findings presented here suggest that the design of transnational institutions is key and that we should focus on both the institutional and sociological dimensions of transnationalization. My results suggest that transnational institutions that are not designed to lock-in both interdependence between transnational and

national authorities and the interpenetration of professionals between transnational and national sites of authority may have the unintended consequence of causing local institutions to atrophy.

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Online Appendix for "Unbundling the State: Legal Development in an Era of Global, Private Governance"

A List of Included Model Law Countries

Country	t_i	Rule of Law	Country	t_i	Rule of Law
Armenia	2006	0.25	Mexico	1993	0.36
Azerbaijan	1999	0.04	Nicaragua	2005	0.39
Bahrain	1994	0.21	Oman	1997	0.57
Bangladesh	2001	0.29	Paraguay	2002	0.35
Belarus	1999	0.30	Peru	1996	0.14
Cambodia	2006	0.09	Philippines	2004	0.48
Croatia	2001	0.77	Russia	1993	0.31
Domin. Rep.	2008	0.31	Rwanda	2008	0.66
Egypt	1994	0.25	Saudi Arabia	2012	0.27
Guatemala	1995	0.29	Serbia	2006	0.58
Honduras	2000	0.31	Sri Lanka	1995	0.62
India	1996	0.70	Thailand	2002	0.51
Iran	1997	0.37	Tunisia	1993	0.22
Jordan	2001	0.61	Turkey	2001	0.73
Kenya	1995	0.21	Uganda	2000	0.41
Macedonia	2006	0.65	Ukraine	1994	0.27
Madagascar	1998	0.26	Venezuela	1998	0.54
Malaysia	2005	0.40	Zambia	2000	0.62
Maldives	2013	0.27	Zimbabwe	1996	0.62
Mauritius	2009	0.77			

Table A1: List of Low Rule of Law Countries

Country	t_i	Rule of Law	Country	t_i	Rule of Law
Australia	2010	0.99	Hungary	1994	0.90
Austria	2006	0.96	Ireland	1998	0.96
Belgium	2013	0.98	Japan	2004	0.97
Bhutan	2013	0.92	Lithuania	2012	0.95
Bulgaria	2002	0.82	Malta	1996	0.89
Chile	2004	0.97	New Zealand	1997	0.99
Costa Rica	2011	0.96	Norway	2004	0.99
Denmark	2005	1.00	Poland	2005	0.95
Estonia	2006	0.97	Singapore	1995	0.97
Georgia	2010	0.81	Slovakia	2014	0.83
Germany	1998	0.99	Slovenia	2008	0.90
Greece	1999	0.85	Spain	2003	0.99
Hong Kong	2010	0.94			

Table A2: List of High Rule of Law Countries

B Alternative Specifications

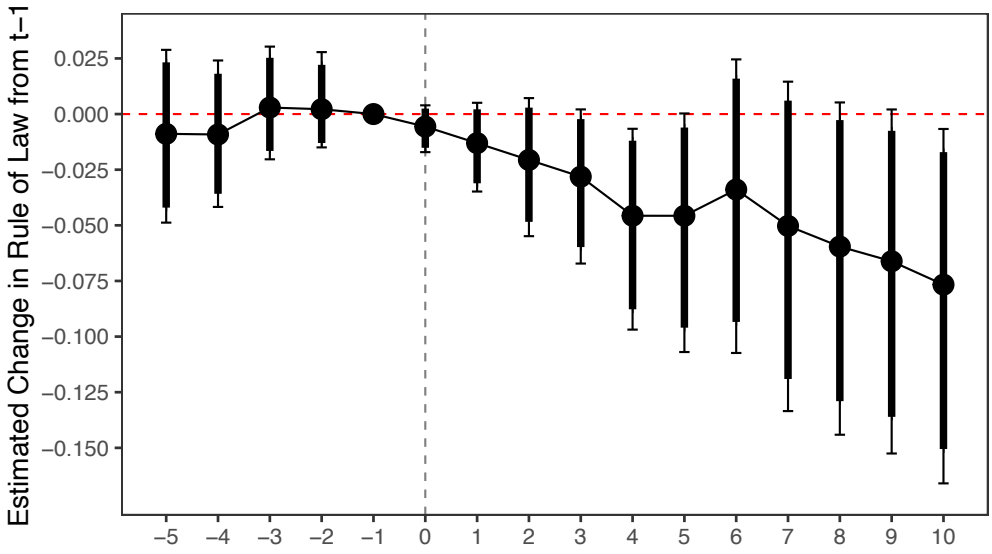

Figure B1: ATT, Low Rule of Law Sample, Ten Year Period

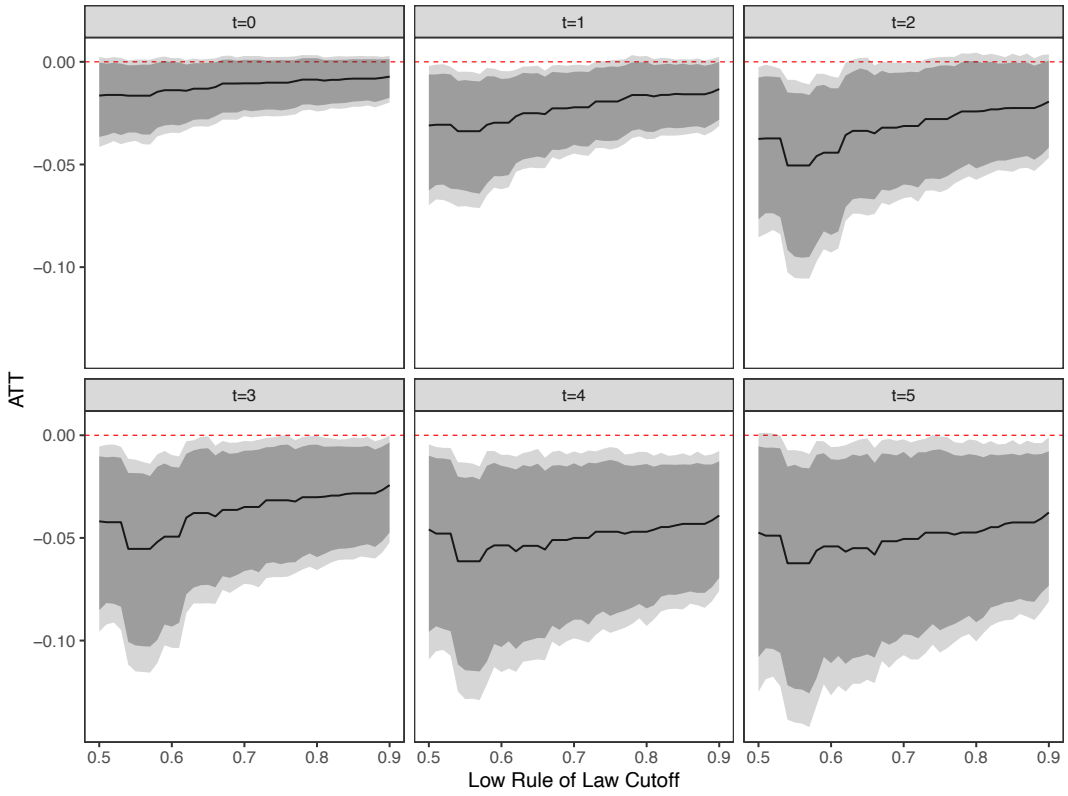

Figure B2: Alternative Low Rule of Law Cut Points

C Covariate Balance Pre- and Post-Refinement

This figure presents the standardized mean difference between treated and control countries for all covariates each year prior to enactment of the Model Law. This graph is based on the analysis summarized in Table 3, Column 2 (see Imai, Kim and Wang, forthcoming, 10-1).

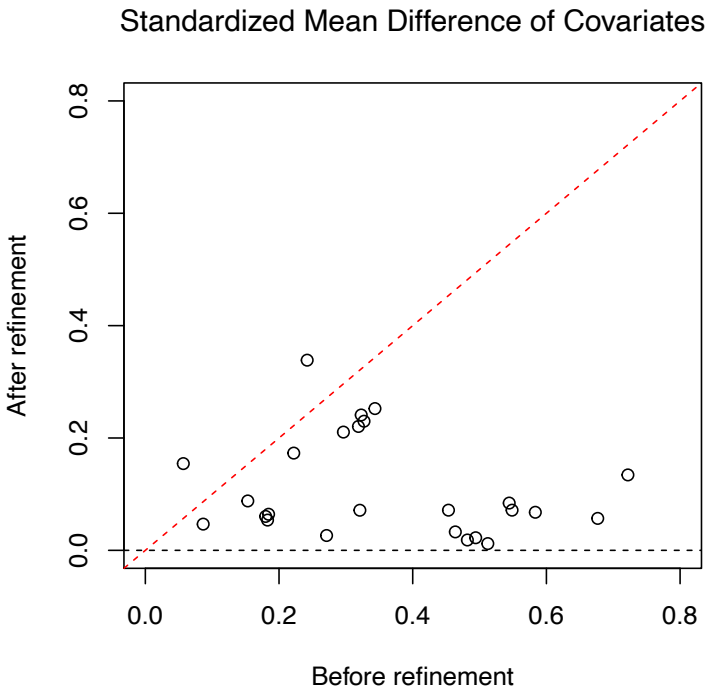

Figure C1: Covariate Balance