Seeking a Treasure: Behavioral Economics in the Sea Search-Armada v. Colombia Arbitration
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Mid-hearing, the Arbitral Tribunal in Sea Search-Armada, LLC v. The Republic of Colombia (PCA Case 2023-37) received an application for intervention from the Kingdom of Spain. The letter asserted Spain’s claim to certain rights over the San José Galeon, a “Spanish Navy warship sunk in naval combat against an English squadron in 1708” near the coast of the Colombian port city of Cartagena (Decision on the Application by Spain for Leave to Intervene, ¶ 6).

Amidst the complexity of a historical colonial and heritage war story, reminiscent of a narrative straight out of a Jules Verne novel, the Tribunal finds itself ensnared in the enigma of where the San José Galeon is located. This blog post tests the use of behavioral economics in arbitration to evaluate the consequences of a party’s failure to produce information. In particular, this post argues that by using the economic theories developed by Kahneman and Tversky in the 1970s (such as prospect theory, loss aversion, status quo bias, and information asymmetry), the Tribunal may infer consequences from the parties’ conduct, with or without the operation of the IBA Rules on the Taking of Evidence and the UNCITRAL Arbitration Rules.

Background of the Case

The investor, Sea-Search Armada (“SSA”), claims roughly USD 10 billion, equivalent to 50% of the treasure composed of emeralds and gold coins (RfA, ¶ 14). The SSA is the successor of certain companies that claim to have found a treasure by identifying the site where the San José Galeon lies. SSA, Colombia, and Spain are among the many interested parties that claim rights over the San José Galeon.

In what is now referred to as the “1982 Confidential Report,” SSA claims that its predecessors found the ship’s place of rest (RfA, ¶19). On the other hand, Colombia has repeatedly challenged the premise that SSA’s predecessors had identified the location of the San José Galeon or that Colombia’s Supreme Court had granted any rights exceeding the scope of the coordinates reported in the 1982 Confidential Report. Instead, Colombia argues that a so-called “1982 Columbus Report” concluded that the San José Galeon was not within the originally estimated coordinates.

Both SSA’s claim and Colombia’s main defense hinge on several communications, spanning several decades, exchanged between the parties regarding the whereabouts of the San José Galeon.
The question, notwithstanding Colombia’s position, remains a factual one. In this regard, arbitrator Jagusch made the following remark emphasizing the importance of Colombia’s conscious decision to not provide the location of the San José Galeon:

“So, the government of Colombia has taken the position publicly and in these proceedings that it has found the Galeón San José, so it knows the location.

Would I be right in assuming that if that location was not in the area of the coordinates stated in the 1982 Confidential Report, that would be an absolute defense to the Claimant’s claims?

Or is it the case that without your wanting to concede the exact location, the location is within the area of the coordinates stated in the 1982 Confidential Report, and your case is that they didn’t find it?”

Jagusch succinctly raised the question of whether it is reasonable to draw an inference from Colombia’s omission to provide the location of the San José Galeon. In response, Colombia sidesteps the issue by contending that SSA “could not have any claims over the Galeon San José for one simple reason: it did not discover the Galeon” (at 1:34:44), as allegedly shown in the 1982 Columbus Report.

**Evaluating the Parties’ Conduct**

Jagusch’s remark and Colombia’s conduct give much to think from the standpoint of behavioral economics.

First, Jagusch’s remark should be mindful of the representativeness heuristic bias, where the outcome (i.e., non-disclosure of a document) is associated with the most probable event familiar to the arbitrator. For example, if the arbitrator has observed instances where the parties withheld information that contradicted their position, then a future similar situation (such as Colombia’s failure to disclose the location of the San José Galeon) is associated with a familiar result for that conduct.

This bias might be produced, for instance, by the IBA Rules themselves, which state that a party’s failure to render a required document might conclude with the use of damaging inferences to its case (Art. 9 (6-7)).

Relevantly, while the IBA Rules stipulate that the inference be drawn specifically in relation to the unproduced document, the lesser-used Prague Rules on the Efficient Conduct of Proceedings in International Arbitration allow the arbitrator to make an “adverse inference with regard to such party’s respective case or issue” (Art. 10). This highlights a distinction between a fact inferred from the content of a document and from the overall issue that said document addresses.

It is not uncommon for people to fall prey to what Kahneman and Tversky called ‘illusions of validity’ (p. 1126), wherein they overestimate the accuracy of their predictions, believing them to be more closely aligned with reality than they truly are. For example, predisposition might be
generated by arbitrators when parties fail to provide information because it might be harmful to them, and not for reasons related to “grounds of special political or institutional sensitivity” (IBA Rules, Art. 9(2)(f)), such as ensuring local security of the San José Galeon.

This illusion can be both factual and legal. Legally, an inference of this nature would not hold scrutiny under the IBA Rules or the Prague Rules, which do not allow inferences for unproduced documents if there is a “satisfactory explanation” under the former, or a “justifiable ground” under the latter. Ensuring the protection of humanity’s largest treasure under the sea is a compelling reason against the application of adverse inferences. From a behavioral standpoint, it should also be questioned why SSA has not made a formal document production application or a proposal to appoint a confidentiality advisor to review the coordinates of the San José Galeon. The reasons behind this might range from the procedural stage to SSA’s expected outcome of a request of such nature.

Secondly, a decision-making result of this nature would likely fail to engage with loss aversion theories. In what has been called the ‘most influential theoretical framework in all of the social sciences’ since 1979, loss aversion has proven that “[l]osses loom larger than corresponding gains” (Tversky and Kahneman, p. 1039). Loss aversion induces “status quo bias” where a decision maker opts to stabilize a situation in the face of risk. Much alike, in the jurisdictional stage of an arbitration, in case of doubt, maintaining the claim would be far less damaging than depriving SSA of its last jurisdictional forum when its claims have not prospered before US courts and the Inter American Commission on Human Rights (Claimant’s brief 20.09.23 ¶¶ 102-109).

The myriad of behavioral economic theories that may be tested is well beyond the scope of this post. However, these examples are only a few that challenge the inclination toward making conscious or unconscious inferences in arbitration. While the use of inferences is documented in case law (see Metal-Tech v. Uzbekistan, on the use of inferences to presume the existence of corruption in an investment), caution is warranted.

Notably, cautious reliance on assumptions also follows the criteria laid out by the International Court of Justice (“ICJ”) in the Corfu Channel Case. In that case, the ICJ deliberated on the possibility of recurring to adverse inferences, stating: “The proof may be drawn from inferences of fact, provided that they leave no room for reasonable doubt” (p. 18). While aligning legal concepts with economic theories remains a challenge in international arbitration, recent cases such as the SSA Arbitration offer a promising avenue to explore and challenge these boundaries on a theoretical level.

The Pending Task for Practitioners

While we often scrutinize the parties’ actions in arbitration, there is little empirical review of the parties’ procedural inactions and how to assess them.

This post does not intend to draw a definitive conclusion from the parties’ behavior, but instead encourages the integration of behavioral economics, when appropriate, to the application of inferences in arbitration. In this regard, behavioral economics may assist arbitrators to conduct conscious off-the-record inferences being aware of the biases that they may have due to how the parties have pleaded.
The ongoing development in the SSA case, including whether the arbitrators apply any actual inferences in their partial award or request further information on the location of the San José Galeon, will shed further light on issues within the intersection of arbitration and behavioral economics.

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