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Ethical Aspect: Differences in Ethical Standards When Considering Arbitration Cases Involving Third-Party Funding

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Annotation: This report provides an exhaustive analysis of the ethical challenges introduced by Third-Party Funding (TPF) in international arbitration. It examines the fundamental conflicts of interest, threats to confidentiality, and issues of funder control that disrupt traditional ethical standards. Through a critical discussion of the fragmented regulatory landscape, institutional rules, and landmark case law, the report identifies the core problems and proposes a multi-layered solution aimed at harmonizing disclosure requirements and strengthening ethical duties to preserve the integrity of the arbitral process.

Keywords: Third-Party Funding (TPF), International Arbitration, Ethics, Conflicts of Interest, Disclosure, Arbitrator Impartiality, Confidentiality, Legal Privilege, Security for Costs, Essar v. Norscot.

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Introduction

International arbitration, long conceived as a private and consensual method of dispute resolution between two or more parties, has witnessed the rise of a transformative and disruptive force: the third-party funder. This new stakeholder, operating at the intersection of finance and law, has fundamentally altered the dynamics of arbitral proceedings, introducing novel opportunities while simultaneously creating profound ethical challenges that test the very foundations of the arbitral process.

At its core, Third-Party Funding (TPF), also known as litigation finance, is a commercial arrangement whereby an entity with no prior connection to a dispute agrees to finance all or part of the legal costs of one of the parties. This financing is provided on a non-recourse basis, meaning that if the funded party's claim is unsuccessful, the funder loses its investment and the party owes nothing in return. If the claim succeeds, the funder receives a share of the proceeds, which can be structured as a percentage of the award (often between 20% and 45%), a multiple of the amount invested, or a combination of both. This model distinguishes TPF from traditional financing mechanisms such as bank loans, which must be repaid regardless of the outcome, or insurance products that serve different risk-mitigation functions.

What began as a niche practice in jurisdictions like Australia has evolved into a formidable global industry, with a market value estimated at over $18.2 billion worldwide. The industry is now populated by a range of sophisticated players, from specialized funding firms like Burford Capital and Omni Bridgeway to investment banks and hedge funds seeking to diversify their portfolios. This market is highly selective; funders conduct rigorous due diligence and, according to anecdotal evidence, reject between 90% and 95% of the claims presented to them, choosing to invest only in cases with a high probability of success and a clear path to enforcement. This rapid expansion, with the number of funded arbitrations averaging nearly 200 per year since 2019, signals that TPF is no longer a peripheral phenomenon but a key feature of the modern dispute resolution landscape.

The initial and most powerful justification for TPF has always been its role in promoting access to justice. International arbitration can be a prohibitively expensive endeavor, and TPF provides a crucial lifeline for claimants who have meritorious claims but lack the financial resources to pursue them. By providing capital, TPF can level the playing field, ensuring that disputes are decided on their merits rather than on the relative financial strength of the parties. This is particularly salient in investor-state disputes, where claimants may face the vast resources of a sovereign state.

However, the contemporary use of TPF has expanded far beyond this foundational purpose. It has become a sophisticated financial and risk-management tool for large, well-resourced multinational corporations. These entities utilize TPF not out of necessity, but for strategic advantage. By outsourcing the costs of a dispute, a company can keep significant legal expenses off its balance sheet, manage cash flow more effectively, and redeploy its own capital into core business operations rather than tying it up in litigation. This strategic use effectively transforms a company's legal department from a traditional cost center into a potential revenue generator, insulated from the financial risks of the dispute. The evolution of the TPF user base from primarily impecunious claimants to include financially robust corporations fundamentally alters the ethical calculus. The arguments that validate TPF as a shield for the weak may not apply with the same force when it is used as a sword by the strong. This duality demands a more nuanced and robust regulatory posture, one that acknowledges both of TPF's roles and addresses the distinct ethical questions each one raises.

The introduction of the funder—a non-party who nonetheless possesses a direct and substantial economic interest in the outcome of the arbitration —creates a fundamental tension with the established ethical pillars of the arbitral process. The traditional architecture of arbitration, built on principles of arbitrator independence and impartiality, confidentiality, and party autonomy, was designed for a bipartite adversarial system. It is ill-equipped to manage the complex, tripartite relationship that emerges between the funded party, the opposing party, and the funder. This report will argue that this ethical dissonance requires a comprehensive recalibration of existing standards. The current patchwork of rules and guidelines is insufficient to address the systemic challenges posed by TPF. To preserve the integrity and legitimacy of international arbitration, a more coherent, principled, and holistic framework is necessary to govern the conduct of funders, arbitrators, and parties alike.

The Problem: The Tripartite Ethical Challenge of Third-Party Funding

The presence of a third-party funder introduces a new economic logic into the arbitral process, giving rise to a tripartite ethical challenge that is interconnected and systemic. The funder's financial stake is the root cause of a series of cascading issues that threaten the core values of arbitration: conflicts of interest that undermine impartiality, the erosion of confidentiality and privilege, and the distortion of party autonomy through funder control.

Conflicts of Interest: The Funder-Arbitrator-Counsel Nexus

The bedrock principle of international arbitration is the independence and impartiality of the arbitral tribunal. TPF jeopardizes this principle by introducing a complex and often opaque web of relationships between funders, arbitrators, and legal counsel. Because funders are repeat players in the arbitration market, they inevitably develop relationships with the relatively small and interconnected community of elite international arbitrators and specialized law firms, creating numerous avenues for potential conflicts.

Specific conflict scenarios that challenge the integrity of the process include:

Direct Financial Interest: An arbitrator may hold shares or other financial instruments in a publicly traded funding corporation that is financing one of the parties in the arbitration on which they sit.

Professional Relationships: An arbitrator's law firm may currently advise or represent a funder in unrelated matters, or an arbitrator may have previously acted as counsel in a case financed by the same funder. These professional ties can create an appearance of dependence or a lack of impartiality.

Repeat Appointments: A more subtle but equally pernicious risk arises from repeat appointments. An arbitrator who is regularly appointed by law firms or parties that are consistently backed by the same funder may, consciously or unconsciously, be influenced by the prospect of future appointments, creating a potential allegiance to the funder.

The International Bar Association (IBA) Guidelines on Conflicts of Interest have recognized this danger by defining a funder as an entity with a "direct economic interest" in the award, thereby making its relationships with arbitrators relevant to a conflict analysis. The critical issue is that even the *appearance* of bias is sufficient to undermine the legitimacy of the arbitral process and can provide grounds for challenging an arbitrator or resisting the enforcement of an award. Without transparency regarding the funder's identity, parties are deprived of the ability to conduct effective conflict checks, leaving the process vulnerable to hidden biases.

Erosion of Confidentiality and Legal Privilege

Confidentiality is often cited as a key advantage of arbitration over public court litigation. TPF places this principle under significant strain. To make an informed investment decision, a funder must conduct extensive due diligence, which typically requires access to confidential case materials, privileged legal advice, and counsel's candid assessment of the claim's strengths and weaknesses.

This necessary disclosure to a third party creates a significant legal risk: the waiver of attorney-client privilege (legal advice privilege) and litigation privilege (attorney work-product doctrine). Once privilege is waived, these sensitive documents could become discoverable by the opposing party, severely prejudicing the funded party's case. While parties may attempt to rely on the "common interest doctrine" to shield these communications, this doctrine is a fragile defense. Its application varies widely across jurisdictions, and it may be deemed to apply only *after* a funding agreement has been concluded, leaving pre-agreement due diligence communications exposed.

The problem is further compounded by the differences between legal traditions. The common law concepts of privilege are not universally recognized in civil law jurisdictions, which instead rely on a lawyer's professional duty of secrecy. This duty, however, typically does not extend to communications with third parties like funders, creating profound uncertainty in cross-border arbitrations. While parties can and should use robust non-disclosure agreements (NDAs) when approaching potential funders, these agreements are a contractual remedy and may not prevent a tribunal from ordering the disclosure of the underlying documents if it determines that privilege has been waived.

Distortion of Party Autonomy and Funder Control

The principle of party autonomy holds that the parties to a dispute control the conduct of their case. TPF can subvert this principle by shifting a degree of control from the funded party to the funder, whose primary objective is to maximize its financial return. The extent of this control is dictated by the terms of the Litigation Funding Agreement (LFA), which can grant the funder significant influence over critical aspects of the arbitration.

Common control provisions in LFAs may include:

Influence over Strategy: The funder may have the right to be consulted on or even approve key strategic decisions, including the selection of legal counsel, experts, or arbitrators.

Control over Settlement: Many LFAs give the funder the right to be informed of any settlement offers and, in some cases, the power to veto a settlement that the funded party wishes to accept. This creates a clear conflict of interest, as the funder's desire for a higher return may push for continued litigation, whereas the party may prefer the certainty and finality of a reasonable settlement.

Termination Rights: Funders typically reserve the right to terminate the funding agreement if their assessment of the case's prospects changes, for example, due to unfavorable developments. Such a termination can leave the funded party in a perilous position, unable to continue the arbitration and potentially liable for costs incurred to that point.

This potential for funder control gives rise to concerns about "funder-driven" litigation, where disputes are pursued or prolonged not to vindicate a party's legal rights but to serve the funder's investment strategy. This also fuels the argument that TPF may encourage the pursuit of marginal or speculative claims that might otherwise have been abandoned or settled early, thereby increasing the contentiousness and cost of arbitration.

Ultimately, these three ethical problems are not discrete but are causally linked, originating from the funder's core economic interest. To protect its investment, a rational funder seeks a degree of control over the claim. This need for control necessitates access to sensitive information, which in turn threatens confidentiality and privilege. Simultaneously, the funder's role as a powerful, repeat player in the market creates the network of relationships that gives rise to conflicts of interest. Any viable solution, therefore, cannot address these issues in isolation but must tackle them as interconnected components of a single, systemic challenge.

Discussion

The international arbitration community's response to the ethical challenges of TPF has been characterized by a combination of proactive institutional rule-making, landmark judicial decisions, and pioneering legislative reforms. However, this response remains fragmented, resulting in a patchwork of standards that varies significantly across jurisdictions and arbitral institutions. While an emerging consensus is visible on certain issues, particularly disclosure, a uniform global framework is still far from reality.

At the heart of the regulatory debate is the question of disclosure. Proponents argue that mandatory disclosure of the funder's existence and identity is the essential first step toward addressing the ethical dilemmas posed by TPF. Such transparency is seen as a panacea for several reasons. First and foremost, it enables parties, arbitrators, and institutions to conduct effective conflict-of-interest checks, which is crucial for safeguarding the independence and impartiality of the tribunal. By bringing the funder out of the shadows, disclosure protects the integrity of the arbitral process and mitigates the risk that an award could be challenged or refused enforcement on the grounds of an undisclosed conflict.

However, opponents and skeptics raise valid concerns that mandatory disclosure could open a Pandora's box of tactical maneuvering and satellite litigation. There is a fear that an opposing party, upon learning of a funder's involvement, might use that information not to ensure impartiality but to harass the funded party. This could take the form of frivolous challenges against arbitrators or burdensome applications for security for costs, designed to create delay and drive-up expenses for the funded party.

This debate has also focused on the appropriate *scope* of disclosure. A broad consensus is forming that disclosure should be limited to the mere existence of a funding agreement and the identity of the funder. This information is sufficient for conducting conflict checks. Demands for the disclosure of the full funding agreement, including its commercial terms, are generally resisted. Such terms are typically irrelevant to the merits of the dispute or potential conflicts and are considered highly confidential commercial information. Requiring their disclosure could prejudice the funded party without providing any tangible benefit to the arbitral process.

Leading arbitral institutions have been at the forefront of developing practical rules to govern TPF, responding to the demands of their users for greater clarity and transparency. While their approaches differ in detail, a clear trend toward mandatory disclosure of the funder's identity is evident.

International Chamber of Commerce (ICC): The 2021 ICC Rules marked a significant development by introducing Article 11(7). This provision requires parties to "promptly" disclose the existence and identity of "any non-party which has entered into an arrangement for the funding of claims or defences and under which it has an economic interest in the outcome of the arbitration". As the world's most preferred arbitral institution, the ICC's adoption of this rule signaled a crystallisation of the trend toward disclosure.

International Centre for Settlement of Investment Disputes (ICSID): Reflecting the unique public interest concerns in investor-state arbitration, the 2022 ICSID Arbitration Rules (Rule 14) mandate that parties file a written notice disclosing the name and address of any third-party funder. This disclosure must be made upon registration of the Request for Arbitration or immediately upon concluding a funding arrangement thereafter.

Singapore International Arbitration Centre (SIAC): SIAC has taken a multi-faceted approach. Its 2017 Practice Note on Arbitrator Conduct in Cases Involving External Funding clarified arbitrators' duties, and the tribunal's powers to order disclosure and consider funding in cost allocations. The new SIAC Rules 2024 (Rule 38) have codified this, now explicitly requiring parties to disclose the existence of any TPF agreement and the funder's identity and contact details.

Hong Kong International Arbitration Centre (HKIAC): The 2018 HKIAC Administered Arbitration Rules (Article 44) work in tandem with Hong Kong's legislative framework. The rule requires a funded party to communicate a written notice of the existence of a funding agreement and the identity of the funder to all other parties, the HKIAC, and the tribunal.

London Court of International Arbitration (LCIA): The LCIA has taken a different path. The 2020 LCIA Rules do not contain an express provision mandating the disclosure of TPF. Instead, the LCIA relies on the broad powers of the arbitral tribunal to manage the proceedings and order the disclosure of any relevant information if it deems it necessary. The rules do, however, contain general provisions on confidentiality that require parties to seek undertakings of confidentiality from any third parties they involve in the arbitration.

The financial implications of TPF manifest in two key procedural areas: applications for security for costs and the recoverability of funding costs themselves. Opposing parties increasingly cite the presence of a funder as a basis for seeking security for costs, arguing that a claimant's need for funding is evidence of its impecuniosity and potential inability to pay an adverse costs award should its claim fail.

This issue of costs was thrown into sharp relief by the English High Court's 2016 decision in ***Essar Oilfields Services Ltd v. Norscot Rig Management Pvt Ltd***. In this seminal case, the court upheld an arbitral award that ordered the losing party, Essar, to pay not only Norscot's legal fees but also the substantial success fee Norscot owed to its third-party funder. The arbitrator, and subsequently the court, found that the tribunal's power under the English Arbitration Act 1996 to award "legal or "**other costs**" was sufficiently broad to encompass the costs of obtaining litigation funding.

However, the decision was heavily influenced by the unique and extreme facts of the case. The arbitrator made a robust finding that Essar had engaged in "reprehensible" conduct designed to "cripple Norscot financially," leaving Norscot with "no option" but to seek TPF to pursue justice. In this context, it was deemed fair for Essar to bear the consequences of its actions. The funding terms themselves—a fee of 300% of the funds advanced or 35% of the recovery, whichever was greater—were accepted by the arbitrator as being on the "market standard," a point that has drawn considerable criticism for being potentially punitive and offensive.

The *Essar* decision, while celebrated by funders, creates a significant moral hazard and risks having perverse, systemic consequences. By establishing that the funder's premium—its profit—is potentially recoverable from the losing party, the ruling fundamentally shifts the funder's business risk. This could incentivize funders to charge higher success fees, secure in the knowledge that these costs might be passed on. It may also alter settlement dynamics, as a funded party might be less willing to accept a reasonable settlement offer if there is a prospect of recovering not just the damages but the full, grossed-up cost of the funding as well. A decision intended to achieve justice in a specific case of egregious misconduct could thus have the unintended effect of making arbitration more expensive and contentious for everyone, undermining the core goals of efficiency and cost-effectiveness. This danger underscores the limitations of relying on ad hoc judicial decisions to regulate a complex market and reinforces the need for a more principled, rules-based approach.

To address the tripartite ethical challenge and the fragmented regulatory landscape, a holistic and principled solution is required. Such a framework must move beyond a narrow focus on disclosure to regulate the conduct of all three key actors in a funded arbitration: the parties, the arbitrators, and the funders themselves. This multi-layered approach aims to integrate TPF responsibly into the arbitral process, preserving its benefits while mitigating its risks.

A global best practice for disclosure should be adopted to balance the need for transparency with the imperative of procedural efficiency. This can be achieved through a two-tiered model.

Building on the emerging consensus seen in the ICC, ICSID, SIAC, and HKIAC rules, there should be a mandatory and automatic duty on any funded party to disclose certain baseline information at the outset of the arbitration or as soon as a funding agreement is concluded. This disclosure should be limited to what is strictly necessary for conflict-of-interest checks: the existence of the funding agreement and the full legal name and address of the third-party funder. This provides the essential information needed to ensure the impartiality of the tribunal without opening the door to tactical abuse.

Arbitral tribunals should be explicitly vested with the power to order the disclosure of further information about the funding arrangement, but this power should be exercised with caution. Such an order should only be made following a reasoned application from the opposing party that demonstrates a specific and material relevance to a live issue in the proceedings. For example, a party might need to show credible evidence that the funder is exercising undue control over settlement decisions or that a specific term of the LFA is relevant to a challenge to the tribunal's jurisdiction. This approach provides a crucial safety valve to address genuine concerns while preventing speculative "fishing expeditions" into a party's confidential funding arrangements.

Transparency through disclosure is only effective if the key legal actors have clear duties to act upon the information revealed. Therefore, the ethical obligations of arbitrators and counsel must be clarified and strengthened.

The duty of independence and impartiality must be explicitly defined to encompass relationships with third-party funders. Soft law instruments like the IBA Guidelines on Conflicts of Interest, which treat funders as equivalent to parties for conflict purposes, should be more formally incorporated into the procedural rules of arbitral institutions. Furthermore, arbitrators should have an affirmative duty not only to disclose their own relationships but also to proactively investigate potential conflicts with known, major funders in the market, recognizing the interconnectedness of the arbitration community.

Professional conduct rules must unequivocally affirm that a lawyer's primary and non-delegable fiduciary duty is to their client (the funded party), not to the third-party funder. This is paramount in situations where the funder's commercial interests may diverge from the client's best interests, particularly regarding settlement. Counsel must be ethically bound to provide independent advice that serves the client's objectives, even if it conflicts with the funder's desire to maximize its return on investment.

The most effective way to address the root causes of the ethical challenges is to regulate the conduct of funders directly. Drawing inspiration from the pioneering legislative models of Hong Kong and

Singapore, an international "Code of Conduct for Third-Party Funders" should be developed and promoted by arbitral institutions and industry bodies. Adherence to such a code could become a prerequisite for funders wishing to finance cases under the rules of major institutions.

Key provisions of this code should include:

The code must prohibit terms in LFAs that grant the funder the ultimate power to control the litigation strategy or to unilaterally veto a reasonable settlement offer that the funded party wishes to accept. While funders have a legitimate interest in being consulted, the final decision-making authority must remain with the party.

The code should impose a strict and binding duty of confidentiality on the funder for all privileged and confidential information received during due diligence and throughout the course of the arbitration. This provides an additional layer of protection against waiver of privilege.

To protect funded parties from the risk of a funder becoming insolvent or withdrawing mid-case, the code should require funders to maintain and demonstrate sufficient capital to cover their aggregate funding liabilities under all of their agreements for a minimum period (e.g., 36 months, as in the Hong Kong code).

The circumstances under which a funder can unilaterally terminate a funding agreement must be clearly defined, reasonable, and limited, ensuring that a funded party is not improperly left without financial support at a critical stage of the proceedings.

This three-layered solution is designed to be holistic. Mandatory disclosure provides the necessary transparency. Strengthened ethical duties ensure that arbitrators and counsel act appropriately on the information that is disclosed. Finally, the funder code of conduct addresses the underlying behaviors and contractual terms that create the ethical problems in the first place. Together, these measures create a robust and proactive ethical ecosystem capable of integrating TPF into arbitration in a manner that is both responsible and sustainable.

Conclusion

Third-Party Funding has irrevocably altered the landscape of international arbitration. It has evolved from a tool for promoting access to justice into a mainstream financial product used for sophisticated risk management. While its benefits are undeniable, this report has demonstrated that TPF introduces a powerful commercial logic that creates profound ethical dissonance with the core principles of the arbitral process. The introduction of a non-party with a direct economic interest has strained the traditional duties of impartiality, confidentiality, and party autonomy that underpin the legitimacy of arbitration.

The current global response to these challenges is a fragmented patchwork of institutional rules, national laws, and judicial precedents. This lack of uniformity creates uncertainty and allows for inconsistencies in ethical standards. As this analysis has shown, addressing the problem requires more than just a debate over disclosure. The ethical quandaries of TPF are interconnected, stemming from the funder's economic interest and cascading through issues of control, confidentiality, and conflicts of interest.

Therefore, a piecemeal approach is insufficient. The path forward lies in a coherent, multi-layered solution that targets the conduct of all key actors. This involves, first, harmonizing disclosure standards to mandate the revelation of a funder's identity, thereby enabling effective conflict checks. Second, it requires strengthening the ethical duties of arbitrators and counsel to ensure they remain steadfastly impartial and loyal to their clients in the face of new financial pressures. Third, and most critically, it demands the direct regulation of funder conduct through a robust code that sets clear limits on control, imposes duties of confidentiality, and ensures financial stability.

Third-Party Funding is now a permanent and prominent feature of international dispute resolution. The challenge for the global arbitration community is not to resist or prohibit it, but to integrate it in a principled and responsible manner. By adopting a holistic ethical framework, the community can harness the benefits of TPF while ensuring that the pursuit of profit by an external stakeholder does not corrode the fundamental promise of arbitration: to deliver fair, impartial, and efficient justice.

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