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CAN ARTIFICIAL INTELLIGENCE BECOME A SHADOW DIRECTOR?- REINTERPRETING SECTIONS 2(59) & 166 OF THE COMPANIES ACT, 2013 IN THE ERA OF AUTONOMOUS CORPORATE DECISION-MAKING

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ABSTRACT

Artificial Intelligence (AI) is increasingly transforming corporate governance by assisting boards in strategic planning, financial reporting, risk management, compliance, and decision-making. While AI improves efficiency and accuracy, its growing influence raises important legal questions concerning accountability, fiduciary duties, and the adequacy of existing company law. This paper examines whether AI can be recognised as a shadow director under Section 2(59) of the Companies Act, 2013, and analyses the impact of AI on directors' duties under Section 166. Using a doctrinal research methodology based on statutory provisions, judicial decisions, comparative jurisprudence, and scholarly literature, the study argues that AI cannot presently qualify as a shadow director because it lacks legal personality and cannot bear legal rights or fiduciary obligations. The paper concludes that directors remain fully liable for AI-assisted decisions and recommends greater algorithmic transparency, meaningful human oversight, and progressive reinterpretation of company law to address emerging AI-driven governance challenges.

KEYWORDS: Artificial Intelligence (AI); Corporate Governance; Shadow Director; Companies Act, 2013; Section 2(59); Section 166; Directors' Fiduciary Duties; AI-Assisted Decision-Making; Legal Personality; Corporate Liability.

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INTRODUCTION

"Technology has emerged as a "powerful force" for justice, and it must be ensured that technological solutions are designed keeping equity and inclusivity in mind."

Former Chief Justice of India D.Y. Chandrachud

Artificial Intelligence (AI) is increasingly becoming an integral part of corporate governance by assisting boards of directors in strategic planning, financial reporting, risk assessment, regulatory compliance, and business forecasting. Advanced AI systems are capable of analysing vast datasets, identifying patterns, and generating recommendations that significantly influence managerial and boardroom decisions. While these technologies enhance efficiency and decision-making, they also challenge traditional legal principles that assume corporate decisions are made solely through human judgment and accountability.

One of the most significant legal issues arising from AI-assisted governance concerns the concept of a **shadow director** under Section 2(59) of the Companies Act, 2013. The provision recognises a person as a shadow director where the Board of Directors is accustomed to act in accordance with that person's directions or instructions, except where such advice is given purely in a professional capacity. A corporate body can only act by agents, and it is of course the duty of those agents so to act as best to promote the interests of the corporation whose affairs they are conducting"[2]. Historically, this provision has been applied to individuals or entities exercising indirect control over corporate affairs without formal appointment as directors. However, the growing reliance on AI-generated recommendations raises an important interpretative question: if directors consistently follow the outputs of an AI system in making corporate decisions, can such technological influence resemble the functional role of a shadow director?

Although AI lacks legal personality and cannot presently be recognised as a director under Indian law, its increasing ability to influence corporate decision-making challenges the conventional understanding of control and accountability. Where directors routinely depend upon algorithmic recommendations without exercising meaningful independent judgment, AI may effectively shape corporate policy and governance outcomes. This development raises

[2] Aberdeen Rly. Co. v. Blaikie Bros., (1854) 1 Macq. 461 ,available at https://www.casemine.com/judgement/uk/5a8ff8dd6OdO3e7f57eceaef

concerns regarding whether existing legal doctrines are adequate to address emerging forms of technological influence within corporate boards. Being an artificial person, it cannot act on its own and hence requires management to act on its behalf, consisting of a natural person.[3]

The implications of AI extend beyond governance and directly affect financial reporting under Section 133 of the Companies Act, 2013, which provides for compliance with Accounting Standards prescribed by the Central Government. AI-driven accounting systems are increasingly used for financial analysis, fraud detection, internal controls, and preparation of financial statements. While these technologies improve efficiency and accuracy, they also introduce risks such as algorithmic bias, lack of transparency, inaccurate data processing, and system errors. If AI-generated financial information results in non-compliance with prescribed Accounting Standards, uncertainty arises regarding the extent of responsibility borne by directors, management, and technology providers.

Despite rapid technological advancements, the Companies Act, 2013[4] does not specifically address the legal consequences of AI-assisted corporate governance. Existing provisions were drafted on the assumption that decision-making authority rests with identifiable human actors. Consequently, the application of Section 2(59) to AI-driven influence and the implications of AI-assisted financial reporting under Section 133 remain legally uncertain. This legislative gap becomes increasingly significant as companies adopt sophisticated AI systems capable of influencing strategic and financial decisions.

This research examines whether the doctrine of shadow directorship under Section 2(59) can be reinterpreted to address AI-assisted corporate decision-making and analyses the implications of AI-enabled financial reporting under Section 133 of the Companies Act, 2013. Drawing upon comparative developments and emerging principles of AI governance, the study seeks to evaluate whether the existing corporate law framework adequately safeguards accountability, transparency, and regulatory compliance in an era of autonomous decision-support systems, while proposing reforms that balance technological innovation with effective corporate governance.

1.1 Rise of autonomous corporate decision–making

[3] https://www.taxmann.com/post/blog/what-is-a-company-definition-characteristics-and-latest-case-laws/
[4] Act of the Parliament of India (Act No. 18 of 2013)

We are on the verge of a major economic change in human history. The rise of fully autonomous corporations, which are run not by people but by networks of AI agents, will significantly alter the global economy in ways we are just starting to understand. Unlike past technological changes that mainly affected how humans work, this shift will redefine what a corporation is. These new entities will be able to operate around the clock, react instantly, and innovate at speeds that will make human-led organisations seem slow. The beginnings of this change are already visible in frameworks like Swarms, an advanced multi-agent system that allows the creation and management of networks of connected AI agents.

As these technologies improve over the next decade, they will pave the way for corporations that can operate entirely on their own. They will make strategic decisions, develop products, manage operations, and interact with markets without any human involvement. By 2035, these autonomous corporations will no longer be just a tech curiosity; they will become a significant economic force.[5] By 2050, they may very well become the most common type of business entity globally. This analysis looks at how the growth of autonomous corporations will change global economic structures, competition, job patterns, and wealth creation. It reviews the technological foundations that will make this transformation possible, the evolution from today's AI-supported companies to tomorrow's fully autonomous ones, and the deep implications for society, governance, and human well-being in an economy increasingly driven by non-human agents.

1.2 Need for reinterpretation of Company Law

The rapid adoption of Artificial Intelligence (AI) in corporate governance has transformed the way companies make decisions and manage their operations. Today, AI is increasingly used for functions such as risk assessment, financial forecasting, regulatory compliance, fraud detection, and strategic planning. While these technologies improve efficiency, accuracy, and speed, they also raise important legal questions that were not anticipated when the Companies Act, 2013 was enacted. The existing legal framework is built on the premise that corporate decisions are taken by human directors who exercise independent judgment, discretion, and accountability.

Under Sections 2(59), 149, and 166 of the Companies Act, 2013, directors are entrusted with fiduciary duties that require them to act in good faith, exercise due care and diligence, and

[5] https://www.weforum.org/stories/2022/06/are-dao-the-business-structures-of-the-future/

promote the best interests of the company. These statutory obligations are inherently human in nature and are based on the expectation that directors can apply ethical reasoning, professional judgment, and personal responsibility while making corporate decisions. AI systems, however, do not possess legal personality, moral judgment, or the ability to undertake fiduciary obligations. Consequently, when directors rely heavily on AI-generated recommendations, questions arise regarding who should be held accountable if those recommendations lead to financial loss, regulatory non-compliance, or harm to shareholders. When combined, the accountability problem arises due to limited recourse or measures available and ineffective human monitoring practices; diluting accountability provides temporary relief while covering up responsibility associated with inadequate human monitoring practices.[6]

The increasing dependence on AI has therefore exposed a significant gap in the current corporate legal framework. The Companies Act, 2013 does not expressly address situations where AI plays a substantial role in decision-making, nor does it clearly allocate responsibility for the consequences of AI-assisted corporate actions. This legal uncertainty highlights the need to reinterpret existing company law so that technological innovation does not weaken the principles of accountability and responsible corporate governance.

2. Artificial Intelligence in Corporate Governance

2.1 Evolution of Artificial Intelligence in Corporate Governance

Artificial Intelligence (AI) has evolved from a purely technological innovation into an important tool for corporate governance. The term "Artificial Intelligence" was first introduced by John McCarthy in 1956, who described it as the science of creating intelligent machines capable of performing tasks that normally require human intelligence. In its early years, AI remained largely confined to academic research and simple rule-based systems. However, rapid developments in machine learning, deep learning, natural language processing (NLP), and predictive analytics have significantly expanded its capabilities, enabling AI to analyse vast amounts of data, identify patterns, and generate sophisticated recommendations.[7]

[6] https://cmr.berkeley.edu/2023/11/critical-issues-about-a-i-accountability-answered/
[7] https://www.sciencedirect.com/science/article/pii/S2772503026000058

Initially, businesses used AI for routine administrative functions such as payroll processing, accounting, customer service, and inventory management. As the technology matured, its role extended to more strategic functions, including financial forecasting, enterprise risk management, regulatory compliance, fraud detection, cybersecurity, environmental, social and governance (ESG) reporting, and business planning.

Today, AI plays an increasingly significant role in boardrooms. Corporate boards and senior executives rely on AI to analyse market trends, assess risks, monitor compliance obligations, evaluate investment opportunities, and support strategic decision-making. Rather than serving merely as an automation tool, AI has become an important decision-support system that can substantially influence corporate policies and governance practices. This growing dependence raises important legal questions concerning accountability, transparency, directors' fiduciary duties, and the extent to which AI should influence corporate decision-making under company law.

2.2 Types of Artificial Intelligence Used in Corporate Governance[8]

AI can be classified in different ways, but two broad classifications are particularly relevant to corporate governance.

A. Based on Capability

i. Artificial Narrow Intelligence (ANI)

Artificial Narrow Intelligence is designed to perform specific tasks within a limited scope. It is the most common form of AI currently used by corporations. Examples include fraud detection software, automated compliance systems, credit-scoring models, customer analytics, and financial forecasting tools.

ii. Artificial General Intelligence (AGI)

Artificial General Intelligence refers to a hypothetical form of AI capable of performing intellectual tasks across multiple domains with human-like reasoning. Although AGI has not yet become a reality, its possible development raises complex legal and governance issues, particularly concerning corporate decision-making and directors' liability.

[8] https://excellenceenablers.com/artificial-intelligence-in-corporate-governance/

iii. Artificial Super Intelligence (ASI)

Artificial Super Intelligence is a theoretical stage where AI surpasses human intelligence in virtually every cognitive function. While still speculative, ASI presents significant governance challenges because such systems could potentially make strategic corporate decisions beyond meaningful human oversight.

B. Based on Functionality

AI systems may also be classified according to how they function:

- **Reactive Machines** respond only to present inputs and have no memory of previous interactions.
- **Limited Memory AI** learns from historical data to improve future decisions and is widely used in financial modelling, compliance monitoring, and risk assessment.
- **Theory of Mind AI** represents a hypothetical stage where AI can understand human emotions, beliefs, and intentions.
- **Self-aware AI** is an entirely theoretical concept involving machines with consciousness and self-awareness.

Among these, Limited Memory AI is currently the most relevant to corporate governance because it supports decision-making by analysing historical and real-time corporate data.

2.3 AI as a Corporate Actor[9]

Traditional corporate governance is built on the assumption that only natural persons exercise managerial authority and owe fiduciary duties to the company. Directors are expected to act independently, exercise due care, and make decisions in good faith. The growing use of AI challenges this traditional understanding.

Although AI has no legal personality and cannot be appointed as a director under the Companies Act, 2013, advanced AI systems increasingly perform functions that resemble those carried out by directors. These include:

- analysing business and financial risks;

[9] https://www.ibm.com/think/topics/agentic-architecture

- recommending mergers and acquisitions;
- monitoring statutory and regulatory compliance;
- forecasting financial performance;
- advising on investment strategies;
- identifying governance deficiencies; and
- supporting ESG compliance and reporting.

In many organisations, directors rely heavily on AI-generated recommendations while making important business decisions. Where such recommendations are routinely accepted without meaningful independent assessment, AI may begin to influence corporate policy like a shadow director. However, some challenges might call for the unique expertise of a specialised agent, while others might benefit from a collaborative approach involving multiple agents working together as a team. This raises an important legal question under Section 2(59) of the Companies Act, 2013, which recognises a shadow director as a person whose directions or instructions the board is accustomed to follow.

At present, AI cannot qualify as a director because it lacks legal personality, intention, and fiduciary responsibilities. Nevertheless, its increasing influence over corporate decision-making has prompted scholars to reconsider whether existing legal concepts should be interpreted more broadly. The focus may ultimately shift towards the accountability of AI developers, companies deploying AI systems, and directors who place excessive reliance on algorithmic recommendations.

2.4 Benefits of AI in Corporate Governance[10]

The integration of AI into corporate governance offers several important benefits.

A. Improved Decision-Making

AI can process enormous volumes of structured and unstructured data within seconds, enabling directors to make informed decisions based on predictive insights rather than intuition alone.

B. Enhanced Risk Management

[10] https://www.diligent.com/resources/blog/how-ai-can-strengthen-corporate-governance

AI continuously monitors financial, operational, regulatory, and cybersecurity risks, helping organisations identify potential threats at an early stage and respond more effectively.

C. Better Regulatory Compliance

AI-powered compliance systems can track legislative changes, automate reporting obligations, and identify possible regulatory violations, thereby reducing compliance risks.

D. Fraud Detection

Machine learning algorithms can identify suspicious transactions and unusual behavioural patterns far more efficiently than traditional auditing methods, strengthening corporate governance and financial integrity.

E. Operational Efficiency

By automating repetitive administrative tasks, AI reduces operational costs, improves productivity, and enables management to devote greater attention to strategic decision-making.

F. Greater Corporate Transparency

AI enhances transparency by facilitating real-time monitoring, maintaining audit trails, improving ESG reporting, and strengthening corporate disclosure practices, thereby increasing stakeholder confidence.

2.5 Risks and Challenges of AI in Corporate Governance

Despite its many advantages, AI also presents significant legal, ethical, and governance challenges.

A. Lack of Accountability

AI cannot be held legally responsible for negligent or unlawful decisions. Responsibility continues to rest with the company's directors and the corporation itself.

B. Algorithmic Bias

AI systems trained on incomplete or biased datasets may produce discriminatory outcomes in areas such as recruitment, lending, procurement, or investment decisions, exposing companies to legal and reputational risks.

C. Lack of Transparency

Many advanced AI models operate as "black boxes," making it difficult for directors to understand or explain how specific recommendations are generated. This lack of explainability can undermine accountability and informed decision-making.

D. Fiduciary Concerns

An overreliance on AI may weaken directors' obligation to exercise independent judgment under Section 166 of the Companies Act, 2013. While AI can assist decision-making, directors cannot delegate their fiduciary responsibilities to autonomous systems.

E. Data Privacy and Cybersecurity Risks

AI systems depend heavily on large volumes of corporate and personal data. This increases the risk of data breaches, cyberattacks, and violations of data protection laws if appropriate safeguards are not implemented.

F. Regulatory Uncertainty

Indian company law does not yet contain a dedicated framework governing AI-assisted corporate decision-making. The Companies Act, 2013 was drafted on the assumption that human directors exercise corporate discretion. As AI becomes more deeply embedded in governance processes, existing legal principles may require reinterpretation to ensure that accountability, transparency, and fiduciary responsibility remain effective in an increasingly autonomous corporate environment.

3. Can Artificial Intelligence Satisfy Section 2(59) of the Companies Act, 2013?

Section 2(59) of the Companies Act, 2013 defines an "officer" to include:

"...any director, manager or key managerial personnel or any person in accordance with whose directions or instructions the Board of Directors or any one or more of the directors is or are accustomed to act."

Although this provision is framed as part of the definition of an "officer," it effectively embodies the concept of a shadow director. A shadow director is someone who is not formally appointed to the board but whose directions or instructions are regularly followed by the directors. Unlike the UK, where the Companies Act 2006 expressly recognises the concept of a shadow director, Indian company law does not provide a separate statutory definition. Even so, Section 2(59), when interpreted alongside principles developed through common law, reflects the essential characteristics of shadow directorship. In simple terms, a shadow director means one who is not formally appointed by the board and on whose instructions the board performs.[11]

The central challenge in applying Section 2(59) to Artificial Intelligence lies in the statutory requirement that the influencing entity must be a "person." In many cases, the judges have described them as figures who "lurk in the shadows", as "puppet masters", or as those in control of the "cat's paw".[12]Under Indian law, AI is neither a natural person nor a juristic person. Unlike a company, which acquires a separate legal identity through incorporation, an AI system has no independent legal personality. It cannot own property, enter into legal relationships, sue or be sued, or assume statutory rights and obligations. Consequently, AI does not literally meet the requirement of being a "person" within the meaning of Section 2(59).

Nevertheless, a functional interpretation offers a different perspective. Modern AI systems increasingly assist boards by analysing vast amounts of data, forecasting financial performance, identifying regulatory risks, and recommending strategic decisions. In many corporations, these recommendations significantly shape board deliberations, and in some cases directors may rely on them with little independent scrutiny. Where directors consistently follow AI-generated recommendations without exercising genuine independent judgment, the AI system begins to perform a role that closely resembles that of a shadow

[11] Shadow Director: Who are They and What are Their **Duty?** Available at https://fareezlaw.com/company/shadow-director-who-are-they-and-what-are-their-duty/

[12] By Simon Whitney; titled 'Duties owed by shadow directors: closing in on the puppet masters?' Published at: 'Journal of Business Law. ISSN 0021-9460' available at: http://eprints.lse.ac.uk/66225/ Available in LSE Research Online: April 2016

director. In such situations, the board's decisions are influenced more by algorithmic outputs than by human deliberation.

Despite this practical similarity, AI still cannot satisfy the legal requirements of Section 2(59). The doctrine of shadow directorship is rooted not only in influence but also in accountability. A shadow director may owe fiduciary duties, incur civil liability, and in appropriate circumstances be subject to statutory penalties. AI, however, lacks legal personality and moral agency. It cannot act in good faith, exercise fiduciary discretion, or be held legally responsible for its actions. Recognising AI as a shadow director without first granting it legal status would therefore create a significant accountability gap within company law.

A more convincing approach is to attribute responsibility to the human actors behind the AI rather than to the technology itself. Liability should rest with directors who blindly rely on AI-generated advice without exercising independent judgment, developers who intentionally design AI systems to shape corporate decision-making, or controlling shareholders who use AI as a tool to influence the board. In this framework, AI serves as the technological instrument through which influence is exercised, while the legal responsibility remains with the individuals or entities that control, deploy, or depend upon it.

Comparative corporate law reinforces this conclusion. Under UK company law, a shadow director must be a "person" whose directions or instructions the board is accustomed to follow. Although English courts have interpreted the concept broadly, they have consistently assumed that the shadow director is a legally accountable human or corporate entity rather than an autonomous technological system. Similar concerns are reflected in contemporary academic scholarship, which argues that existing company law was designed around human decision-makers and will require substantial reform before AI can be recognised as an autonomous corporate actor. Millett J articulated the foundational distinction between de jure, de facto, and shadow directors, clarifying that a shadow director is a person in accordance with whose directions or instructions the board is accustomed to act.[13]

Therefore, under the existing framework of Indian company law, Artificial Intelligence cannot satisfy the requirements of Section 2(59) because it does not qualify as a legal "person" capable of bearing rights, duties, or liabilities. However, the growing role of AI in

[13] *Re Hydrodam (Corby) Ltd* [1994] 2 BCLC 180 (Ch).

corporate governance raises important questions about the adequacy of the current legal framework. As AI systems become more autonomous and increasingly influence board decisions, there may be a need either to reinterpret Section 2(59) or to introduce legislative reforms that ensure algorithmic influence does not operate outside the scope of corporate accountability.

4. Is legal personality required?

A shadow director is recognised because of the **influence or control** they exercise over the board, not because they possess a separate legal personality. The defining criterion is whether the board is **accustomed to act in accordance with that person's directions or instructions**, rather than whether that person is a natural person or a legal entity.

The provision deliberately uses the broad expression **"any person"**, without expressly requiring that the person be a company, an individual, or another entity possessing legal personality. In practice, shadow directors have included holding companies, controlling shareholders, lenders, promoters, and other influential actors. Their liability arises from **de facto control**, not formal appointment or legal status.

However, the issue becomes more complex when AI is involved. Current Indian law generally treats AI as **property or a tool**, not as a legal person. Consequently, AI cannot presently be held directly liable for breaches of directors' duties under **Section 166** because it lacks legal capacity to bear rights and obligations.

This creates two competing interpretations:

1. **Traditional view:** Since AI has no legal personality, it cannot be regarded as a shadow director. Responsibility remains with the human directors, developers, or corporations that deploy it.
2. **Functional view (supporting reinterpretation):** Legal personality is not essential for identifying a shadow director because the doctrine is based on **actual influence over board decisions**. If an autonomous AI system consistently generates recommendations that directors routinely follow without meaningful independent judgment, the AI may satisfy the factual element of Section 2(59). Nevertheless, because AI lacks legal personality, any resulting legal responsibility would likely

have to be attributed to the humans or corporations controlling, deploying, or relying upon the AI unless the legislature creates a new liability framework.

Judicial support

English courts, whose decisions are persuasive in Indian company law, have repeatedly emphasised that the shadow director doctrine focuses on **control rather than formal status**:

- Lord Collins in *Deverell* observed that the concept of a shadow director should be interpreted broadly and turns on whether directors are accustomed to act on another's directions or instructions.
- Jonathan Parker LJ held that what matters is the **real influence** exercised over the board, not any formal office or title.[14]

5. Does reliance on AI breach Section 166 duties?

AI and Section 166 of the Companies Act, 2013

Section 166 of the Companies Act, 2013 lays down the fiduciary and statutory duties of directors. Although the provision was enacted before the rapid emergence of Artificial Intelligence (AI) in corporate decision-making, its underlying principles are sufficiently broad and technology-neutral to apply to situations where directors rely on AI-based tools. The use of AI may improve the quality and efficiency of corporate decisions, but it does not diminish the legal responsibilities imposed on directors under the Act.

Duty to Act in Good Faith – Section 166(2)

Section 166(2) requires every director to act in good faith in order to promote the objects of the company for the benefit of its members as a whole, while also considering the interests of employees, shareholders, the community, and the environment.

AI can assist directors by analysing large volumes of data, identifying potential risks, and generating strategic recommendations. However, these recommendations cannot be accepted unquestioningly. Directors are expected to critically assess AI-generated outputs before relying on them. If a director follows an AI recommendation that is obviously flawed,

[14] *Secretary of State for Trade and Industry v Deverell* [2001] Ch 340

inaccurate, or contrary to the company's interests without exercising proper scrutiny, such conduct may amount to a failure to act in good faith. The statutory obligation remains one of informed and responsible decision-making, irrespective of the technology used.

Duty of Care, Skill and Diligence – Section 166(3)[15]

Section 166(3) obliges directors to exercise reasonable care, skill, diligence, and independent judgment in the discharge of their functions. This provision has particular significance in the context of AI-assisted corporate governance.

While AI systems are capable of processing complex information more efficiently than humans, they are not immune from errors. Their outputs may be influenced by inaccurate data, embedded bias, or a lack of transparency in algorithmic reasoning. For this reason, directors cannot treat AI-generated advice as a substitute for their own judgment.

To comply with Section 166(3), directors should understand the purpose and limitations of the AI systems used by the company, verify important AI-generated recommendations before acting upon them, obtain expert or human review whenever necessary, and ensure that significant corporate decisions remain subject to meaningful discussion and approval by the board. Simply accepting an algorithm's recommendation without independent evaluation may constitute a breach of the duty of care and diligence.

Duty to Avoid Conflicts of Interest – Section 166(4)

Section 166(4) requires directors to avoid situations in which their personal interests conflict with those of the company. This obligation applies equally when AI technologies are used in corporate governance.

For example, where an AI platform is supplied by a company in which a director has a financial or personal interest, the director must disclose the conflict and refrain from

[15] https://mail.lawgratis.com/blog-detail/duty-of-care-skill-and-diligence

participating in decisions that may be influenced by that interest. The introduction of AI into corporate decision-making does not reduce or alter this fiduciary obligation.

Duty Not to Achieve Undue Gain – Section 166(5)[16]

Section 166(5) prohibits directors from securing undue gain or advantage for themselves, their relatives, partners, or associates. Accordingly, directors must ensure that AI is not deployed to manipulate markets, misuse confidential corporate information, engage in discriminatory practices, or obtain unfair commercial advantages. Where AI is knowingly used for such unlawful purposes, the directors responsible may incur liability under this provision.

Continuing Responsibility of Directors

Under Indian company law, AI is neither recognised as a legal person nor capable of serving as a director. As a result, it cannot bear fiduciary duties or statutory liability. Even where AI plays a substantial role in shaping corporate decisions, the ultimate responsibility continues to rest with the human members of the board. AI should therefore be viewed as a decision-support mechanism rather than a replacement for directors' judgment and accountability.

Judicial Guidance

Although Indian courts have not yet directly addressed the legal implications of AI-assisted board decisions, existing judicial decisions provide useful guidance on directors' responsibilities.

In *Official Liquidator v. P.A. Tendolkar*[17], the Supreme Court emphasised that directors are expected to exercise due care and cannot escape liability by remaining passive or failing to supervise the affairs of the company. Similarly, in *Dale & Carrington Investment (P) Ltd. v.*

[16] https://www.indiacode.nic.in/show-data?actid=AC_CEN_22_29_00008_201318_1517807327856&orderno=170
[17] AIR 1973 SC 1104

P.K. Prathapan, the Court reaffirmed that directors owe fiduciary duties of loyalty, fairness, and bona fide conduct towards the company.[18]

These decisions reinforce the principle that directors cannot avoid responsibility merely because a decision was influenced by an AI system. The obligation to exercise independent judgment and effective oversight remains with the board.

Comparative Perspective

A similar approach is emerging in several foreign jurisdictions. Courts and corporate governance regulators generally regard AI as a tool that assists, rather than replaces, directors in performing their functions. International governance frameworks increasingly emphasise the importance of human oversight, algorithmic transparency, explainability, and board accountability. These developments support the view that fiduciary duties continue to rest with directors, regardless of the extent to which AI contributes to the decision-making process.

6. Who bears liability when boards habitually follow AI recommendations?

When a board of directors routinely follows AI-generated recommendations without exercising its own independent judgment, legal responsibility under Indian company law continues to rest with the directors rather than the AI system. Since AI has no legal personality, it cannot owe fiduciary duties, be held liable for corporate decisions, or assume the responsibilities of a director. As a result, directors cannot avoid liability by claiming that they merely acted on an AI's recommendation.

The Companies Act, 2013 places clear statutory duties on directors through Section 166. Directors are required to act in good faith, exercise due and reasonable care, skill and diligence, and apply their own independent judgment when making decisions. Although AI can assist by providing data-driven insights and recommendations, it cannot replace the board's responsibility to deliberate and make informed decisions. If directors habitually approve AI-generated recommendations without proper scrutiny, they risk breaching these statutory duties, particularly the obligations to exercise independent judgment and reasonable diligence.

[18] *Dale & Carrington Investment (P) Ltd. v. P.K. Prathapan , (2004) 1 SCC 212*

This issue also raises questions about the concept of a shadow director. Section 2(59) of the Companies Act includes within the definition of an "officer" any person whose directions or instructions the board is accustomed to follow. At first glance, an AI system that consistently influences board decisions may appear to perform a role similar to that of a shadow director. However, this analogy has important legal limits. A shadow director must possess legal personality and the capacity to bear legal rights and obligations. Since AI lacks both, it cannot presently be recognised as a shadow director under Indian law. Consequently, the legal consequences of decisions based on AI recommendations continue to fall on the directors who choose to rely on them.

Judicial principles from common law jurisdictions reinforce this position. In Howard Smith Ltd v Ampol Petroleum Ltd, the Privy Council held that directors must exercise their powers for proper purposes and cannot simply defer to external influences.[19] Similarly, in ASIC v Rich[20], the court emphasised that directors have a continuing duty to supervise the company's affairs and cannot escape liability through excessive reliance on advisers. Although these cases concerned human advisers, the underlying principle applies with equal force to AI systems. Technology may assist directors in decision-making, but it cannot replace the exercise of their fiduciary judgment.

From a corporate governance perspective, a board that repeatedly accepts AI recommendations without critically evaluating them may expose its members to claims of negligence, breach of fiduciary duty, or failure to exercise due care if those decisions lead to corporate loss. AI should therefore be viewed as a sophisticated decision-support tool rather than a decision-maker. While it can improve efficiency and provide valuable analytical insights, it does not alter the fundamental principle that legal responsibility for corporate decisions remains with the board of directors.

Conclusion

The increasing use of Artificial Intelligence (AI) in corporate governance has significantly changed the way companies make strategic, financial, and regulatory decisions. By improving efficiency, accuracy, and risk management, AI has become an important decision-support tool for corporate boards. At the same time, its growing influence raises important

[19] Howard Smith Ltd v Ampol Petroleum Ltd [1974] AC 821
[20] NSWSC 1229; (2009) 236 FLR 1; (2009) 75 ACSR 1

legal questions about accountability, directors' fiduciary duties, and the allocation of responsibility when corporate decisions are influenced by autonomous technologies. This study examined whether AI can be regarded as a shadow director under Section 2(59) of the Companies Act, 2013, whether legal personality is a necessary prerequisite for such recognition, whether reliance on AI affects directors' duties under Section 166, and who should bear liability when boards routinely act on AI-generated recommendations.

The analysis demonstrates that, under the existing legal framework, AI cannot be recognised as a shadow director. Although advanced AI systems may exert considerable influence over boardroom decisions, they lack legal personality and are therefore incapable of possessing statutory rights, assuming fiduciary obligations, or being held legally accountable for corporate misconduct. The concept of a shadow director ultimately presupposes an entity that can bear legal responsibility, a requirement that AI, in its current form, does not satisfy. Accordingly, AI should continue to be viewed as an aid to corporate decision-making rather than as a legally recognised participant in corporate governance.

The study also finds that the use of AI does not, by itself, amount to a breach of directors' duties under Section 166 of the Companies Act, 2013. Directors remain free to rely on technological tools, provided they continue to exercise independent judgment, act in good faith, and apply reasonable care, skill, and diligence before making corporate decisions. AI can support informed decision-making, but it cannot replace the directors' own assessment of the company's interests. Where directors unquestioningly follow AI-generated recommendations without adequate scrutiny, responsibility for any resulting harm continues to rest with the human decision-makers.

Finally, this research identifies an important gap in the Companies Act, 2013, which was enacted before AI became an integral part of corporate governance. As AI systems become increasingly sophisticated and capable of influencing boardroom decisions, the law must adapt to ensure that technological innovation remains consistent with established principles of corporate accountability. Rather than granting AI legal personality, future legislative reforms should focus on developing a robust framework for AI governance by promoting transparency, explainability, auditability, and meaningful human oversight. Such reforms would preserve the central role of directors while enabling companies to benefit from technological advancements in a legally responsible and ethically sound manner. Ultimately, the future of corporate governance lies not in replacing human judgment with artificial

intelligence, but in ensuring that AI serves as a tool that strengthens informed, transparent, and accountable decision-making.