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Introduction

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Preface

The Indian Journal of Legal Affairs and Research is a testament to our unwavering commitment to excellence in legal scholarship. This volume presents a curated selection of articles that reflect the diverse and dynamic nature of legal studies today. Our contributors, ranging from esteemed legal scholars to emerging academics, bring forward a rich tapestry of insights that address critical legal issues and offer novel contributions to the field. We are grateful to our editorial board, reviewers, and authors for their dedication and hard work, which have made this publication possible. It is our hope that this journal will serve as a valuable resource for researchers, practitioners, and policymakers, and will inspire further inquiry and debate within the legal community.

Description

The Indian Journal of Legal Affairs and Research is an academic journal that publishes peer-reviewed articles on a wide range of legal topics. Each issue is designed to provide a platform for legal scholars, practitioners, and students to share their research findings, theoretical explorations, and practical insights. Our journal covers various branches of law, including but not limited to constitutional law, international law, criminal law, commercial law, human rights, and environmental law. We are dedicated to ensuring that the articles published in our journal adhere to the highest standards of academic rigor and contribute meaningfully to the understanding and development of legal theories and practices.

THE SLUMBER SURROUNDING SHADOW DIRECTOR'S REGULATORY FRAMEWORK IN INDIA

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ABSTRACT

The issue of shadow directorship in India has been overlooked and seldomly been deliberated on by both the Indian legislature and judiciary. Such an important concept that counteracts and strikes at the heart of good corporate governance ideology has found no development or progression in the realm of Indian jurisprudence which raises major complications. The sheer fact that there exists no legal framework to directly apply fiduciary duties and liabilities to such covert directors on parity with the *de jure* directors raises multiple questions regarding the accountability of such shadow directors. The judiciary's attempt at constructing a poor framework attaching liability through the path of the terminology of 'officer' proves to be inconsistent and difficult in the identification of any veiled puppeteer orchestrating the corporate affairs of a company unlawfully. This cloaked method of control without any safeguards has become a tool for influencing a company's activities and management to one's benefits and advantages and reformative measures are a matter of significant need. This paper envisions to shed light on the present lacunae in the Indian laws and take aid from varying jurisdictions to explore the concept deeply and the mode of implementation of the same in the Indian jurisdiction.

Keywords – shadow director, officer, India, fiduciary, accountability

INTRODUCTION

The term 'shadow directors' briefly refers to those cloaked individuals who directly control a company's management or have a real influence on the individuals controlling the company's management for the greed of their beneficial interest or some ulterior motive. Covert exercising of power helps them to absolve the duties, responsibilities and liabilities the recognised board of

directors are subjected to. Remaining unrecognised in the eyes of the law additionally assists them in prioritising their interests over the law and the company's interests. This derogatory practice has led the courts to nomenclate such individuals by phrases such as "puppet master" and "cat's paw".¹

The idea was first laid down in section 3 of the United Kingdom's Companies (Particulars as to Directors) Act, 1917 which included persons on whose instructions the *de jure* directors were accustomed to act and the first formal recognition was in 1985 through the legislation of United Kingdom Companies Act of which section 741(2) explicitly defined the expression shadow director. However, the concept of shadow directors is still an abstract idea viewed from the perspective of the Indian law standpoint. The definition of the term has not been laid down in any of the Indian statutes or regulations. The collaborative judgments by the Foreign Courts act as the sole authoritative source for seeking a further explanation for this question. The lack of safeguarding regulations against this practice is a colossal gap in our laws that needs to be addressed soon as such a malafide practice of administration strikes at the heart of good corporate governance resulting in a nullification of shareholders' interest and stakeholders' beliefs and trust. This procedure exclaims unjustifiable practice as the 'board observers' exercise subtle influence without the fiduciary responsibilities and control without formal control.²

LACK OF A DEFINED DEFINITION

Section 2(13) of the Companies Act, 1956 provided an inclusive definition of a director and brought within its ambit, directors who are not officially appointed and wielded the same or more powers as the *de jure* directors. Whereas its counterpart, section 2(34) of the Companies Act, 2013 limits its definition of directors specifically to the appointed directors only.³ It shuns the idea of any directors existing outside of the composition of the board of directors transforming the nature of the definition from an inclusive to an exhaustive one. While it's true that the concept of shadow directors becomes irrelevant and abstract in the new Act, there are several various provisions such

¹ *Witney Duties owed by shadow.Pdf*, https://eprints.lse.ac.uk/66225/1/Witney_Duties_owed_by_shadow.pdf (last visited Mar. 18, 2025).

² Nizan Geslevich Packin & Anat Alon-Beck, *Board Observers: Shadow Governance in the Era of Big Tech*, SSRN JOURNAL (2024), <https://www.ssrn.com/abstract=4745278>.

³ A Ramaiya, *Guide to the Companies Act* (18th edn, LexisNexis 2015) 2764.

as sections 2(59), 2(60), and 185 of the new Act that constructs a liability for those who control the reins of power while lurking in the shadows. The substantial complication then lies therein that an implied construction under terms like ‘officer’ and ‘officer in default’ needs to be done to hold the veiled directors accountable for the wrongful acts committed under their control and illicit supervision which minimizes their liabilities and accountability to that of a *de jure* director.⁴

The J.J. Irani Committee Report dated 31st May, 2005 in Chapter IV, paragraph 36.1, stressed the issue and reported that a legal framework should be established to attribute liability by recognizing such shadow directors pulling strings and exercising actual control over the Board.⁵ In the same report under Chapter XII, paragraph 10, the Committee recommended that a legal mechanism should be developed to discourage this practice by utilizing a framework of ‘attributability’ of any such illegitimate directions on which the Board is accustomed to act to such respective persons issuing those directions.⁶ Further, the Uday Kotak Committee Report in 2017 recommended that a green channel should be established - an explicit framework of communications should be established between the Board and the promoters/controlling shareholders to legitimise and avoid the cloaked conversations.⁷

Unfortunately, even after such significant reports demonstrating the visible lacuna, the absence of statutes preventing such deceitful practices continues, proving the inadequacy and crevices of the present equipped laws along with the overwhelming need to reformat them.

THE PREDICAMENT SURROUNDING THE DEFINITION

As shadow directors are not explicitly defined in a proper manner anywhere in the Indian statutes, a state of confusion, uncertainty, and scepticism exists in identifying and affixing responsibility to such directors. Further deliberation on this topic requires taking the assistance of foreign judgments and statutes which are in line with the Indian jurisprudence developed.

⁴ *ibid* 204.

⁵ Dr Jamshed J Irani, *REPORT ON COMPANY LAW*. Page 36

⁶ *Id.*

⁷ *Id.* Page 50

A multitude of foreign statutes such as the Companies Act, 2006 of the United Kingdom, Corporations Act 2001 (Cth) – Section 9 of Australia, Companies Act (Cap. 50) – Section 4(1) of Singapore, and Companies Ordinance (Cap. 622) – Section 3 define the term shadow director in a favourable less ambiguous manner than the Indian statutes and at the same time lay down the foundation to fix attributability for any unlawful acts committed. Through these provisions, the foreign courts are able to recognise the directors hiding behind a veil and charge them for their wrongful acts directly. The essential ingredients are the same for each definition clause, which is that a person not officially appointed on the Board when exercising control over the workings of a company covertly, is termed to be as a shadow director⁸. The elucidation of the terminology of ‘shadow directors’ provided in the different foreign statutes aligns with our given definition as well. Even though the above-mentioned provisions provide an excellent reference point in the further exploration of the topic, this is the juncture when precedents set by foreign courts progress to become a greater authoritative source of law in determining the character and nature of shadow directors. A concatenation of English cases signifies the considerable developments of this concept historically through time and several benchmarks and guidelines laid down for the identification and imposition of liability. The English cases are vital and it is crucial to traverse through them first before progressing ahead as the Indian cases cannot afford to offer a needful degree of clarity and articulation due to the cases being relatively few in quantity.

JUDICIAL PRECEDENTS ESTABLISHED OVERSEAS

The issue of recognition of shadow directorships in foreign jurisdictions has greatly been stressed throughout many years and decades and courts have directly delved into the problem statement revolving around illusionary control rather than specifying the issue as ancillary thus lowering its importance in comparison to other relevant issues in question. Thus, we must refer to certain cases of foreign jurisdictions that have contributed to greatly developing and shedding light on this extremely abstract concept.

⁸ Rehana Cassim, *A Comparative Analysis of the Identification of De Facto and Shadow Directors in South Africa, The United Kingdom and Australia* (2021), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3848703.

*Re Canadian Land Reclaiming & Colonizing Co.*⁹ is one of the earliest cases in which directors who were not formally appointed to the Board were held liable for their lapse of judgment. Two individuals, in this case, did not fulfil the prerequisites (i.e., to have at least 100 shares of the company) to be elected as directors, nevertheless, they were still nominated to be on the Board. The court ignored the contention that liability cannot be attached due to the *de facto* nature of the impugned directors and imposed the liability to pay the required amount. This case proved to be a pioneer for further subsequent judgments advancing the jurisprudence surrounding the idea of silent directors. Thereafter in *Re Hydrodan (Corby) Ltd*,¹⁰ Millett J. established the guidelines to identify a shadow director for the first time and also the minute differences between *de facto* and shadow directors. The criteria in brief to check whether one was a shadow director or not was – that the *de jure* directors are directed by an individual on how to act the directors act according to those instructions and they are accustomed to acting in that manner¹¹. This criterion has been predominantly utilized by several courts of law in imposing liability due to its simple and unequivocal understanding. But in the case *Secretary of State for Trade and Industry v Deverell*,¹² Morritt LJ broadened the parameters by holding that it may not be necessary for the *de jure* directors to be ‘accustomed to act’ to the given directions and also that for an individual to be termed as a shadow director, he needs to have real influence on all or at least the majority of the board members, expanding the criteria set in the *Hydrodan case*.¹³ After the leading case of *Ultraframe (UK) Ltd v Fielding & Ors* [2005] EWHC 1638 (Ch),¹⁴ the English law witnessed no such divergence between *de facto* directors and shadow directors and treated them as almost interchangeable. Additionally, the historical development within the British context showed the Supreme Court emphasising more on the issue of who has ‘real influence’ on the working affairs of the company rather than the identification of *de facto* directors and shadow directors.¹⁵

⁹ *Re Canadian Land Reclaiming & Colonizing Co* [1880] 14 Ch D 660.

¹⁰ *Re Hydrodan (Corby) Ltd* [1994] BCC 161.

¹¹ Neil Jamieson, *The Identification of Shadow Directors under English Law: What Guidance Might Buzzle Provide?*, BUTTERWORTHS JOURNAL OF INTERNATIONAL BANKING AND FINANCIAL LAW 364 (2012).

¹² *Secretary of State for Trade and Industry v Deverell* [2001] Ch 340.

¹³ *Hydrodan*, *supra* note 10.

¹⁴ *Ultraframe (UK) Ltd v Fielding & Ors* [2005] EWHC 1638 (Ch).

¹⁵ Jamieson, *supra* note 11.

A case law decided by the New South Wales (NSW) Court of Appeals, Australia needs to be enumerated and discussed before proceeding further to the Indian cases is *Buzzle Operations Pty Ltd (in liq) v Apple Computer Australia Pty Ltd*.¹⁶ In which Apple was accused of shadow directorship of Buzzle. The Court held in its decision that there must be a meaningful direct linkage between the directions issued and the actions taken by the Board to justify a person as a shadow director. Essentially this means that the Board should prioritise the instructions first in its dealings by treating those directions or wishes “*as themselves being a sufficient reason so to act, rather than making their own decisions in which those instructions or wishes are merely taken into account as one factor... bearing on what is in the best interests of the company*”.¹⁷ Thus this landmark case provides a breathing room and culminates into a shield of protection for lenders and creditors against the allegation of shadow directorship.

JUDICIAL PRECEDENTS ESTABLISHED IN THE INDIAN JURISDICTION

Concerning the Indian context, even though the judges have refrained expressly from citing any foreign cases, the method and the outcome adopted by the Indian courts are similar or even occasionally identical to that of the foreign courts. In *Ionic Metalliks & Ors. vs. Union of India*¹⁸, Pardiwala J. properly explained the definition of shadow directors while deciding on the validity of a Master Circular by RBI. Justice Pardiwala stated, “*A person, who is not appointed to the Board, but on whose directions the Board is accustomed to act, is liable as a director of the company unless he or she is giving advice in his or her professional capacity.*”.¹⁹ This definition wholly summarises the perspective of the Indian judiciary on this subject matter which is then been cited in several other subsequent judgments such as *Nikhil P. Gandhi v. State of Gujarat*²⁰. *Raj Chawla v. SEBI*²¹ is one of the cases in which the Delhi High Court held that Raj Chawla, the petitioner in the instant case was not found to be a person under whose advice or instructions the company was accustomed to act, thus failing to qualify the criteria to be a shadow director. In the

¹⁶ *Buzzle Operations Pty Ltd (in liq) v Apple Computer Australia Pty Ltd* [2010] NSWSC 233.

¹⁷ *ibid.*

¹⁸ *Ionic Metalliks & Ors. vs. Union of India* (2015) 2 GLH 156.

¹⁹ *ibid.*

²⁰ *Nikhil P. Gandhi v. State of Gujarat* [2016] SCC OnLine Guj 1856

²¹ *Raj Chawla v. SEBI* [2010] SCC OnLine Del 90

landmark case of *In Re: Issuance of Optionally Fully Convertible Debentures by Sahara India Real Estate Corporation Limited and Ors.*,²² Mr Subrata Roy Sahara was held by the Securities Regulation Board of India (SEBI) to be a person under whose directions and advice the company functions and is accustomed to acting as he was the founder and a major shareholder of the Sahara India Real Estate Corporation Ltd. In another recent landmark case of *Cyrus Investments v. Tata Sons & Ors.*,²³ Mr. Ratan Tata's position as a shadow director was in dispute and the court interpreted the expression 'shadow directors' in an interesting manner. The court held that when the term 'shadow director' is being utilised, it should suggest something illegitimate which means that one can only be labelled as a shadow director if the execution of such directions issued or advice given by him sprouts into some unlawful and illicit conduct undertaken by the Board.

A question then remains why is it so that courts identify shadow directors under the ambit of terms like 'officer' or 'officer in default' in the Companies Act? The courts generally favour interpreting in such a manner and refuse to attribute fiduciary duties to such individuals because the legislature simply did not intend it so. Even though the legislature recognises such backseat directors indirectly as can be seen in the report of the Standing Committee on Finance (2011-12). Provisions attaching primary liability to such directors are absent which compels the courts to attach a secondary form of liability through interpretation under the term 'officer', creating a cloud of complications in the process of recognition and affixion. If the legislature had wanted such individuals to be responsible directly, then it would have followed the English or Australian approach by clearly defining 'shadow director' among its provisions.²⁴

TESTS FOR DETERMINATION OF FIDUCIARY DUTIES

Various parameters have been employed by the courts of law throughout time immemorial to discover the existence of fiduciary relationships between a *de jure* director and a controlling personality who is in the dark. A test determining the existence of a veiled link between shadow directors and officiated directors gathers significant importance for identification, attributability

²² *In Re: Issuance of Optionally Fully Convertible Debentures by Sahara India Real Estate Corporation Limited and Ors.* [2011] 5 CompLJ 470 (SAT).

²³ *Cyrus Investments v. Tata Sons & Ors* (2020) 2 CompLJ 94.

²⁴ Michael D Hobson, *The Law of Shadow Directorships*, 10 BOND LAW REVIEW (1998), <https://blr.scholasticahq.com/article/5315-the-law-of-shadow-directorships>.

and accountability. This paper would strictly restrict itself and adhere itself to deliberate on two paramount tests laid down in company law jurisprudence – English’s undertaking test and Canada’s power and discretion test which have also been incorporated into landmark judgments delivering a cohesive and coherent methodology to recognise such concealed associations.

UNDERTAKING/ASSUMPTION OF RESPONSIBILITY TEST

The ‘undertaking’ test found its inception by an American professor Austin W. Scott and he formulated his opinion in a much more lucid and simpleton manner stating that “*A fiduciary is a person who undertakes to act in the interest of another person*”²⁵ The question concerning the mode of establishment of the relationship whether contractual or gratuitous had no implications on this test. In other words, if such camouflaged ties exist wherein a person is acting in the interest of another, notwithstanding the nature between them is contractual or not, the individuals are alleged to be in a fiduciary bond.²⁶ The undertaking test was applied in the case of *Ultraframe (UK) Ltd. vs. Gary Fielding & Ors.*²⁷ by Justice Lewinson drawing the ratio held in *Bristol and West BS v Mothew* where a fiduciary assumes responsibilities and poses loyalty and fidelity to another person acting in accordance to him. An interesting *obiter* made by Lewison J worth mentioning is the restricted and narrow interpretation he opined regarding the imposition of fiduciary duties to shadow directors. Quoting his severely criticised phrase of the *Ultraframe* judgment, “*indirect influence exerted by a paradigm shadow director who does not directly deal with or claim the right to deal directly with the company’s assets will not be usually enough to impose fiduciary duties upon him.*”²⁸ Essentially this fact that an indirect exercise of control over the company’s assets or management by a shadow director is not adequate for a shadow director to be held liable. Such directors do not *per se* have direct control of the actual directors, rather they can merely influence them making shadow directors held at a different level. This position laid down by Lewison J was negatively perceived and reproached by multiple authors specifically in the case of *Vivendi v. Richards*²⁹ by Newey J where further development of the undertaking test was observed. Justice Newey broadened the undertaking test into a parameter which was more

²⁵ Austin W. Scott, *The Fiduciary Principle*, 37 CALIFORNIA LAW REVIEW 539 (1949).

²⁶ *ibid.*

²⁷ *Ultraframe* (n 14).

²⁸ *ibid.*

²⁹ *Vivendi v. Richards* [2013] EWHC 3006 (Ch).

stringent and rigorous to escape from. He held, that a person having significant control over the assets or the management of a company would owe certain prescribed fiduciary duties notwithstanding whether he has been elected or is indirectly controlling the affairs of the company.³⁰ Furthermore, Newey J reiterated the Prentice and Payne observation wherein it stated that Lewinson J's approach was wholly defective as his ideology focused on 'imposing' fiduciary duties whereas the duties were "*assumed rather than being imposed.*"³¹ Justice Newey's groundwork culminated the undertaking test firmly ensuring that certain criteria to establish a fiduciary relationship by following a two-fold condition – the identification of such an undertaking/assumption must be based on objectivity and no heed should be given to the intent of such accused individual and how the acts are carried out are to strictly imply such a position of undertaking/assumption of control.³²

The undertaking test is normally what is the norm followed in the sphere of Indian laws, the reason being it is ingrained into the Companies Act, 2013. The language codified under section 2(59) of the Act has the same keywords needed for construing the applicability of this test to various facts in the issue of various cases. Keywords such as '*accustomed to act*' and '*by whose directions or instructions*' resemble that of the undertaking test encompassing elements such as duty of good faith and loyalty. Thus, the Indian cases discussed above have all almost followed this set of criteria solely to determine the existence of fiduciary relationships. For illustration, the benchmark set by Justice Pardiwala in the *Ionic Metalliks* case where the assumption of responsibility is prioritized is an implied signatory to the application of the undertaking test to disputes in India by the judiciary. Subsequently in the *Sahara* case as well, this test was implemented extensively to detect the presence and attributability of fiduciary duties to Mr. Subrata Roy.

POWER AND DISCRETION TEST

Justice Wilson gave birth to this principle by his observations in the case of *Guerin v. Queen*.³³ Held in the Supreme Court of Canada where he elucidated the concept in a brief single paragraph

³⁰ *ibid.*

³¹ David Kershaw, *Company Law in Context: Text and Materials* (2. ed, Oxford University Press 2012) 330

³² *Vivendi*, *supra* note 30.

³³ *Guerin v. Queen* [1984] 2 SCR 335

without elaborating much and delving into the topic properly. Subsequently though, Justice Wilson in the case of *Frame v. Smith*³⁴ Developed and expanded on this concept by trifurcating the observation of the *Guerin case* into comprehensive concocted concise guidelines for identifying the presence of fiduciary relationships. The three guidelines that were laid down, in brief, were – the fiduciary has the ability and capacity to exercise his power or discretion without any riders, the fiduciary can be able to exercise this power or discretion unilaterally affecting the beneficiary's interest, and that the beneficiary is at the mercy and exposed to the whims of such controlling fiduciary.³⁵ The first requirement is quite lucid and simple which mandates for an individual to have broadened powers of control and supervision to be able to dictate the affairs of the company without which no further deliberation is necessary. The second requirement bestows the condition that absolute unfettered unilateral execution of power should reside in the hands of the shadow director (fiduciary) which can affect the stakeholders' (beneficiary) interests. This is an essential element of the test showcasing the helplessness of the beneficiaries of a company in which a fiduciary may misuse the power obtained by him for personal gains and against which no action can be taken by the beneficiaries.³⁶ The third point is an extension of the second point which states that the power obtained by the fiduciary should be such paramount and plenary that the beneficiaries should be at the mercy of the whims of the fiduciary and to which the beneficiaries have no remedy to enforce against any of the wrongful actions committed by the fiduciary.³⁷

The 'power and discretion' test has seldom been implemented to adjudicate matters wherein the determination of fiduciary duties is concerned with by the Indian courts. The courts adopt the undertaking test instead of the power and discretion test as the undertaking test is consonant and is in harmony with the idea of shadow directors engraved in our statutes as substantiated earlier. However, in the case of *Cyrus Investments v. Tata Sons & Ors*, the Supreme Court utilised this criterion to disprove the allegations made on Mr Ratan Tata of shadow directorship explaining that Mr Tata although being a noble emeritus of the company, did not have such widened and unlimited

³⁴ *Frame v. Smith* [1987] 2 SCR 99

³⁵ *ibid.*

³⁶ Colin R. Moore, 'Obligations in the Shade: The Application of Fiduciary Directors' Duties to Shadow Directors' (2016) 36 *Legal Stud* 326

³⁷ *ibid.*

powers to influence the company's affairs of management, thus failing the first guideline of the power and discretion test.

However, it should be noted and mentioned once again that the Indian judiciary has not adopted the stipulated tests explicitly in adjudicating litigations of a similar nature but they do have taken the assistance of the above two authorised tests in determining the existence of fiduciary relationships in a company's management. By equating the verdicts held by different Justices in different cases with the criterion of the tests, we can observe the traces of the guidelines set by these tests being utilised in cases of the Indian jurisdiction as well.

POSITION OF NOMINEE DIRECTORS AS STRAWMEN

The one designation of a director which is highly susceptible and compromised to a degree of foreign control is the post of nominee director in a company. Generally, financial institutions, banks, and majority investors appoint a nominee director to the Board to be kept in the loop with the company's operations and management. Now, as a director nevertheless, a nominee director while acting in his/her capacity shall keep in mind the best interests of the company and its shareholders but a catastrophic commercial diversion may occur due to a conflict-of-interest culminating into a force acting over a nominee director to act as per the whims and interests of his/her appointer rather than the interests of the company.³⁸

The Financial Action Task Force (FATF) which was established in 1989 by the G7 has alerted the accompanying risk of appointing a nominee director to the Board factoring the vulnerability of nominee directors to outside unregulated control.³⁹ The critical nuance lies therein that beneficial owners may abuse this discrepancy to dictate the mannerisms and actions of a nominee director appointed by him to benefit the maximum while simultaneously escaping any responsibility that arises due to the undisclosed status of the shadow directors.⁴⁰ The FATF in another report has directly and substantially signified the unethical and unlawful practice of appointing nominee directors to override jurisdictional controls and conceal the identity of the beneficial owner, albeit

³⁸ Caroline M. Hague, 'Directors: De Jure, De Facto, or Shadow' (1998) 28 Hong Kong LJ 304.

³⁹ Risk based approach guidance, FATF, 201 and 202

⁴⁰ *ibid.*

the designation is lawful. The FATF further has recommended countries adopt mechanisms such as mandatory disclosure of the identity of the nominators to any relevant registry and for nominee shareholders and directors to be licensed to keep updated information and make it available to competent authorities whenever needed. Thus, the FATF through various document releases has made an effort to raise awareness against the use of a lawful position of nominee directors for an unlawful exercise of power by the shadow directors. However, the silence of the law surrounding this subject matter continues to remain predominant.

The Organisation of Economic Co-operation and Development (OECD) as well has indicated that the utilisation of nominee directorships has become an instrument to add layers of opacity and complexity complicating the identification of the actual beneficial owners, providing them with a veil to carry out tax or other financial crimes.⁴¹

The notion of external control on a narrow thin ice was explained by an English court in the case of *Boulting vs Association of Cinematograph, Television and Allied Technicians*⁴², where it was observed that a nominee director acting on behalf of a large shareholder and representing his interest is independent of any external influence only if he is also free to exercise his judgment to determine the best interests of the company.⁴³ Pardiwala J. in the case of *Ionic Metalliks & Ors vs. Union of India & Ors.*⁴⁴, through interpretation has provided us with an *obiter* on similar lines, “However, nominee Directors must be particularly careful not to act only in the interests of their nominators, but must act in the best interests of the company and its shareholders as a whole”.⁴⁵ Thus recommendations with regards to curbing the possible dictatorship over nominee directors by shadow directors can be acknowledged in many significant references but the improvement is yet to take place in the Indian circumference.

⁴¹ OECD, ENDING THE SHELL GAME: CRACKING DOWN ON THE PROFESSIONALS WHO ENABLE TAX AND WHITE COLLAR CRIMES (2021), https://www.oecd.org/en/publications/ending-the-shell-game_79e22c41-en.html.

⁴² *Boulting vs Association of Cinematograph, Television and Allied Technicians* [1963] 2 QB 606.

⁴³ Caroline, *supra* note 38.

⁴⁴ Metalliks, *supra* note 18.

⁴⁵ *ibid*.

AN IMPERATIVE REQUIREMENT FOR REFORMS

The longer the legislature stalls in formulating improvements to the existing provisions, the window widens providing a larger scope for the abuse of law, on account of the existing loopholes that it has. The major concern arises from the element that a shadow director is interpreted as ‘officer in default’ under 2(60) or 2(59) as ‘officer’ for attaching any liabilities upon them. The failure of the current law in force to give equal recognition to the *de facto* and *de jure* directors alike demonstrates a lacklustre character due to the reason that the *de facto* directors neither owe any fiduciary duties to any of the stakeholders of the company nor are bound by the Memorandum or Articles of Association of the company which greatly reduces their liability abundantly.⁴⁶ It should be noted and emphasized that even though they are not formally appointed, they nevertheless exercise immense control and have ‘real influence’ over the corporate affairs of the company placing them on a pedestal same as the *de jure* directors. Though the foreign courts of the United Kingdom and Australia have significantly developed the jurisprudence revolving around the instant substance in question, their judgments are strongly persuasive at the very best, thus requiring India to flourish in its own jurisdiction but the legislature unfortunately showcases little to no motivation in this scenario.

This exact lackadaisical character of the legislature to forge laws against such maladministration has provided a backdoor to venture capital and private equity investors to misuse this to their beneficial advantage. Venture capital and private equity investors usually have a representative of them on the Board to monitor the operations and working of the company in order to protect and safeguard their investments. Although this was the common and usual practice of such companies, an increase in the tendency to refrain from nominating such a representative can also be noticed. The reason for this is that the venture capital and private equity investors choose to rather adopt the role of ‘observer to the Board’ than being officially appointed to it.⁴⁷ The ramifications that this produce is that they get absolved of all the fiduciary duties or responsibilities owed as well as

⁴⁶ brillopedia, *EXPLORING THE LEGAL FRAMEWORK GOVERNING SHADOW DIRECTORS IN INDIA*, BRILLOPEDIA (May 14, 2021), <https://www.brillopedia.net/post/exploring-the-legal-framework-governing-shadow-directors-in-india>.

⁴⁷ *Nishith Desai Associates*, https://www.nishithdesai.com/fileadmin/user_upload/Html/Hotline/Yes_Governance_Matters_Jan0524_M.htm (last visited Mar. 20, 2025).

of any accountability in the future. This enables the investors to assume charge and take control unlawfully of the decision-making power (if majority shareholder) without the fear of any dire consequences or repercussions tarnishing the whole system of the governance structure. The concept of separate legal personality and the doctrine of alter ego in their entirety are being exploited for the benefit of individual gain by assuming power and majority control with the simultaneous abdication of duties and responsibilities massacring the general corporate governance structure and making a company vulnerable to unethical and deceitful acts and procedures.

A requirement of greater enforcement of the law has been realised since the year 1963 when the inquiry on the administration of the Dalmia-Jain companies was conducted and the outcome was quite surprising. Unexperienced and young relatives comprised the Board of Directors who did not look after the company's management and corporate affairs, instead an individual who was not on the Board had exclusive control and autonomy over the company's assets and activities.⁴⁸ When the time came to affix accountability onto the directors, they refuted any liability by pointing out the actual person in control and pleaded that they were just serving as *dummy directors*.⁴⁹ The report showcases that some mandatory directions are required to be dispensed with by each company's management to exterminate any shadow control. Obligations such as disclosure by the directors to the Registrar of Companies mentioning whose shares are they holding on their behalf, if any and providing the identity of the person for whom they are obligated to act in a certain manner.⁵⁰

Under the gamut of corporate governance, transparency and disclosure are preserved and have attained paramount importance and significance. The notion of shadow directorship strikes at the heart of corporate governance through the usage of illegitimate techniques that undermine the stakeholders' trust. Graver than this, the notion vehemently betrays the shareholders of a company who elect their representatives on the board to control the affairs of the company and a person supervising the workings of the company not being on the board and opaque to the shareholders'

⁴⁸ Irani, *supra* note 5.

⁴⁹ Ramaiya, *supra* note 4.

⁵⁰ *ibid*.

eyes straight forwardly opposes the idea of transparency and accountability as for a simple reason that the

CONCLUSION

A bizarre remark that warrants attention is that provision 2(56) of the Companies Act, 2013 used by the Indian judiciary to attach liability to the shadow directors is in *pari materia* to section 3 of the Companies (Particulars as to Directors) Act, 1917 of United Kingdom. The anomaly which resides herein is the strange fact that our law even though enacted after a century after United Kingdom's statute exactly resembles the UK's statute meaning that there has been no evolution in the side of our law revolving around the issue of shadow directors. In 1985, the UK had developed this lacuna by unambiguously defining shadow directors but India omitted to deliberate on this issue and adopted a regressive and outdated provision lacking conceptual clarity and explanation surrounding shadow directors.

Thus, rectification is of the utmost need of the hour or this quiet plague will continue to spread corruption engulfing the corporate governance practices of a significant number of companies. Especially in a country like India where family-owned businesses are prevalent, such safeguards and measures to be laid down by the legislature and judiciary become desperately needed.

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