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AI AND CORPORATE GOVERNANCE IN INDIA: EXAMINING DIRECTORS' DUTIES, FIDUCIARY RESPONSIBILITIES AND LIABILITY FOR AI-ASSISTED DECISIONS

~ Priyanshi Pandey

Abstract

Artificial intelligence (AI) is increasingly used to support corporate decisions involving finance, compliance, recruitment, risk assessment, cybersecurity and business strategy. These tools can improve speed and help directors process large amounts of information, but they can also produce inaccurate, biased or difficult-to-explain recommendations. This creates a central corporate-law question: when a director relies on an AI-generated recommendation, does that reliance satisfy the director's existing legal duties, and who should be accountable if the decision causes harm?

This paper examines the question through a doctrinal and comparative legal method. It analyses the Companies Act, 2013, particularly section 166, relevant principles emerging from Indian decisions on directors' fiduciary obligations and oversight, and selected regulatory approaches to AI governance. It argues that Indian company law already provides a meaningful foundation for accountability through duties of good faith, care, diligence, independent judgment and avoidance of conflicts of interest. Those duties do not disappear when a company uses technology. However, the application of traditional standards to opaque or probabilistic AI systems raises practical questions about reasonable reliance, explainability, documentation and board-level supervision. The paper recommends a proportionate, risk-based approach: directors should not be strictly liable merely because an AI-assisted decision fails, but they should be expected to understand material risks, test important outputs, preserve meaningful human judgment and ensure appropriate

oversight. The aim should be responsible innovation rather than either unrestricted automation or a blanket prohibition on AI-assisted governance.

Keywords: Artificial Intelligence; Corporate Governance; Directors' Duties; Fiduciary Responsibility; Companies Act, 2013; AI Accountability.

1. Introduction

Artificial intelligence has moved from being a specialised technological tool to becoming part of ordinary business operations. Companies may use AI to analyse market conditions, forecast cash flows, identify suspicious transactions, screen job applications, assess credit risk, monitor regulatory compliance and summarise information for board meetings. Used carefully, these tools can help directors identify patterns that might otherwise be missed and make better-informed decisions.

Yet an AI system is not a director. It does not hold office under the Companies Act, 2013, owe statutory duties to a company, or exercise judgment in the legal sense in which a director is expected to do so. Its output depends on its design, training data, instructions, limitations and the quality of information supplied to it. Some systems may provide reasons for their recommendations; others may produce results that are difficult for users to explain or independently verify. Generative AI systems can also produce confident but inaccurate answers.

This creates a governance problem rather than merely a technical one. If a board approves a major transaction after relying on an AI-generated risk assessment, responsibility cannot be answered simply by saying that "the system recommended it." Equally, it would be unfair and impractical to treat every unsuccessful AI-assisted decision as proof of director misconduct. Business decisions are often made under uncertainty, and corporate law must preserve space for honest, informed risk-taking.

Indian law already recognises that directors must act in good faith, exercise due and reasonable care, skill and diligence, use independent judgment and avoid conflicts of interest. Section 166 of the Companies Act, 2013, is central to this framework. The Act does not, however, set out a detailed, AI-specific standard for directors who use algorithmic or generative systems. The issue is therefore how existing duties should be applied to a new decision-making environment.

This paper argues that AI should be treated as a tool that may assist, but cannot replace, directors' legal responsibility. The appropriate standard should be proportionate to the significance of the decision, the foreseeable risks of the system and the director's role and access to expertise. The paper first explains AI's corporate uses and risks, then examines the Indian legal framework, considers possible liability scenarios, briefly compares selected international approaches and proposes safeguards for Indian companies.

2. Research Problem, Questions and Objectives

2.1 Research problem

The growing use of AI in corporate decision-making creates uncertainty about the practical application of directors' duties, particularly the duties of care, diligence and independent judgment. The central problem is not that Indian law has no relevant principles; it is that those principles do not provide detailed operational guidance for AI-assisted decisions, including how directors should assess reliability, document reliance and respond to risks that they cannot fully understand.

2.2 Research questions

(i) To what extent may directors rely on AI-assisted recommendations while complying with their duties under Indian company law?

(ii) How should the duties of care, diligence and independent judgment apply where an AI system materially influences a board decision?

(iii) What factors should be considered when deciding whether a director's reliance on AI was reasonable?

(iv) How can companies allocate responsibilities among directors, management, technology vendors and compliance teams without allowing accountability to disappear?

(v) What governance safeguards would improve accountability while allowing beneficial uses of AI?

2.3 Objectives

The paper aims to examine the relevant duties under Indian company law; analyse the accountability issues created by AI-assisted decisions; identify gaps in practical guidance; consider selected comparative approaches; and propose proportionate governance safeguards.

3. Research Methodology and Scope

This paper adopts a doctrinal legal research methodology. It analyses statutory provisions, judicial decisions and regulatory materials, supported by secondary legal scholarship and selected international instruments. A limited comparative approach is used to draw lessons from the European Union and the United Kingdom. The study is primarily concerned with directors' responsibilities under Indian corporate law, rather than the technical design of AI systems or the full regulation of every AI application.

The paper is conceptual and legal in nature. It does not claim to measure how frequently Indian companies use AI, nor does it present empirical findings from interviews or surveys. Its conclusions should therefore be understood as legal analysis and policy recommendations, not as a report of original fieldwork. Before submission, the author should check the latest amendments, commencement notifications and regulatory directions applicable to the particular AI use being discussed.

4. AI in Corporate Governance: Benefits and Risks

AI can support governance in several ways. It can organize large volumes of documents before board meetings, identify unusual patterns in financial data, flag potentially suspicious transactions, model business risks and assist compliance teams in tracking obligations. In regulated sectors, including banking and securities markets, AI-supported tools may help identify anomalies and improve monitoring. These applications can strengthen oversight when they are properly tested and supervised.

The same tools create risks. First, an AI system may be inaccurate because of poor-quality data, unsuitable assumptions or limitations in its design. Second, a system may reproduce bias present in its training data, potentially affecting recruitment, lending, customer treatment or other decisions. Third, complex models may be difficult to explain, making it harder for directors to understand why a recommendation was produced. Fourth, a company may disclose confidential, commercially sensitive or personal information to a third-party AI provider without adequate safeguards. Fifth, cyberattacks or manipulation of input data may compromise the output. Finally, directors may become over-reliant on an apparently sophisticated tool and fail to apply their own judgment.

These risks are not identical. A tool used to summarize a public report presents a different level of risk from one used to approve a large acquisition, determine access to credit or make a decision affecting thousands of employees. Governance should therefore be risk-based. The more significant the decision and the greater the potential harm, the stronger the expected controls should be.

The central distinction is between using AI to inform a decision and delegating judgment to it. A board may reasonably use analytical tools, expert advice and software. However, a director who accepts a consequential recommendation without asking whether it is reliable, relevant and consistent with the company's interests risks turning assistance into abdication. Corporate governance should focus not on whether AI was used, but on how it was used, what the directors understood, what checks were undertaken and whether the final decision was genuinely theirs.

5. The Indian Legal Framework

5.1 Section 166 of the Companies Act, 2013

Section 166 provides the clearest starting point. It requires directors to act in accordance with the company's articles; act in good faith to promote the company's objects and in the interests identified by the statute; exercise due and reasonable care, skill and diligence; exercise independent judgment; avoid situations involving actual or possible conflicts of interest; and not obtain or attempt to obtain undue gain. These obligations are technology-neutral. Nothing in their wording suggests that a director is relieved of them because a decision was supported by software or generated by an algorithm.

The duty of care and diligence is particularly relevant. A director need not personally recreate every calculation performed by a technical system. Reasonable governance often involves reliance on staff, professional advisers and specialist tools. But the director should have a basis for considering the information sufficiently reliable for the purpose for which it is used. Relevant factors may include the importance of the decision, the known limitations of the tool, the quality of the underlying data, the availability of independent verification, warnings or anomalies in the output, and the director's access to expert advice.

The duty to exercise independent judgment is equally important. It should not be interpreted as requiring directors to make decisions without assistance. Rather, the director must retain

responsibility for evaluating the recommendation and deciding whether to accept it. A board paper that merely reproduces an AI output, without meaningful scrutiny of its assumptions or risks, may raise questions about whether independent judgment was actually exercised.

5.2 Board oversight and reporting obligations

Other provisions of the Companies Act are relevant depending on the company and the circumstances. Section 134 addresses the Board's report and directors' responsibility statements, while section 149 and Schedule IV contain requirements relevant to independent directors and their role in governance. These provisions should not be treated as creating a universal, AI-specific duty. Their relevance is that they form part of the broader framework through which board oversight, internal controls, risk management and responsible decision-making are expected to operate.

For listed entities, the Securities and Exchange Board of India's Listing Obligations and Disclosure Requirements Regulations, 2015, provide an additional governance framework, including requirements concerning board composition, committees, risk management and disclosures. The precise obligation depends on the applicable regulation and the nature of the entity. A company using AI in a material business function should consider whether the use affects its existing risk-management, internal-control or disclosure processes.

5.3 Data protection and cybersecurity

AI systems may process personal data, confidential business information or sensitive commercial material. The Digital Personal Data Protection Act, 2023, is relevant where the processing falls within its scope, but the applicability of particular duties must be assessed alongside the Act's commencement notifications and rules in force at the relevant time. It would be inaccurate to assume that every provision is necessarily operational in the same way at every date. Companies must verify the current legal position before relying on a compliance conclusion.

The Information Technology Act, 2000, and applicable rules and directions may also be relevant to particular electronic records, unauthorised access, data handling or cyber incidents. CERT-In directions may be important for entities within their scope. These instruments do not by themselves answer every question about directors' liability for AI, but they demonstrate that AI governance often overlaps with existing privacy, security and compliance obligations.

5.4 No automatic transfer of responsibility to AI

Under the current corporate framework, AI is not a substitute for the legal role of the board or its directors. A company may contract with a vendor or use a third-party platform, but that arrangement does not automatically eliminate directors' own statutory responsibilities. At the same time, liability must be assessed according to the applicable law and facts. The use of AI, by itself, should not establish a breach. The question is whether the relevant director or company failed to meet an applicable legal duty.

6. Judicial Principles and Their Application to AI

Indian courts have developed important principles concerning directors' fiduciary position, care and responsibility. These decisions pre-date the current wave of generative AI and should not be presented as direct rulings on AI. Their value lies in the principles they establish and the questions those principles raise when technology assists corporate decisions.

In Dale & Carrington Investment (P) Ltd. v. P.K. Prathapan, the Supreme Court examined directors' fiduciary obligations in the context of a share allotment used to obtain control. The decision illustrates that directors must exercise powers for proper purposes and in the interests of the company, rather than for collateral personal objectives. Applied to AI-assisted governance, the principle suggests that a director cannot use an algorithmic recommendation as a cover for a decision driven by an undisclosed personal interest. A conflict may remain a conflict even if an AI tool appears to support the decision.

In Official Liquidator v. P.A. Tendolkar, the Supreme Court considered the circumstances in which directors may be held responsible for misconduct in a company's affairs. The decision is useful as a reminder that responsibility depends on the role played and the surrounding facts, rather than a simplistic assumption that every director is automatically liable for every wrong. In an AI context, relevant facts may include the director's involvement, what information was available, whether warning signs were ignored and whether reasonable oversight was exercised.

In N. Narayanan v. Adjudicating Officer, SEBI, the Supreme Court emphasised the importance of integrity and responsibility in corporate disclosures and securities-market conduct. The case is relevant where AI is used to prepare financial information, support disclosures or monitor market-

related compliance. A company cannot treat an automated process as a reason to disregard the legal need for accurate and responsible disclosures.

These cases do not establish a special AI liability test. Instead, they support a more careful approach: examine the statutory duty, the director's role, the decision-making process, the information reasonably available, any conflicts or red flags, and the connection between the alleged failure and the resulting harm. A director who reasonably tests and evaluates an AI recommendation should be distinguished from one who blindly accepts an unreliable output despite obvious warning signs.

7. When Should a Director Be Responsible for an AI-Assisted Decision?

A useful legal analysis distinguishes several situations.

First, suppose an AI system provides a recommendation that is reasonably supported by available information, the company has tested the system for the relevant purpose, the director asks appropriate questions and the board records its reasoning. If the decision later proves commercially unsuccessful, that outcome alone should not establish breach. Corporate decision-making involves risk, and the law should not discourage informed and honest decisions simply because they do not succeed.

Second, suppose a director relies on a tool that is known to be unreliable for the task, ignores a warning about missing or biased data, or fails to seek verification before approving a major transaction. In such circumstances, reliance on AI may support an inference that the director failed to exercise due care and diligence. The concern is not the use of AI itself, but the unreasonable manner in which it was used.

Third, suppose a system produces a discriminatory or otherwise unlawful recommendation. The company should not assume that a decision is legally acceptable merely because it was generated automatically. Depending on the context, applicable employment, equality, consumer, data-protection or other laws may be engaged. Directors' responsibility will depend on the relevant duty, their knowledge and role, and the steps reasonably available to them.

Fourth, suppose confidential or personal data is entered into an external AI platform without appropriate assessment of data handling, access controls or contractual terms. This may create risks under applicable data-protection, confidentiality, cybersecurity or contractual obligations.

Board-level oversight is especially important where the data or potential consequences are material.

Fifth, suppose a vendor designed the system defectively or misrepresented its capabilities. The vendor may bear contractual or other liability depending on the facts and law. That does not automatically absolve the company or its directors from their separate duties. Conversely, directors should not automatically be held liable for every hidden defect that could not reasonably have been identified. A fair approach must distinguish the vendor's technical responsibility from the board's responsibility to select, deploy and supervise the tool with reasonable care.

These examples support a standard of reasonable, informed and proportionate reliance. The assessment should consider the seriousness of the decision; foreseeable harm; the system's purpose and limitations; whether the company performed suitable testing; whether human review was meaningful; whether the director had access to expertise; and whether warnings or contrary evidence were ignored. Such factors can guide application of existing duties without inventing strict liability for every AI-related failure.

8. Comparative Perspective

The European Union's Artificial Intelligence Act, Regulation (EU) 2024/1689, adopts a risk-based approach to AI regulation, with different requirements depending on the system and its use. Its relevance to corporate governance is not that it replaces directors' duties, but that it illustrates how risk classification, transparency, human oversight and accountability can be addressed through a structured regulatory framework. Its requirements apply according to the Regulation's scope, roles and implementation timetable; they should not be assumed to apply identically to every company or every AI tool.

The United Kingdom's Companies Act 2006, section 174, requires a director to exercise reasonable care, skill and diligence, assessed by reference to both an objective standard and the director's actual knowledge and experience. Although it is not an AI-specific provision, it provides a useful comparison for thinking about directors who rely on technology. A director's responsibilities may be evaluated in light of the role and the circumstances, while still requiring a baseline level of care.

These comparative approaches suggest that India need not immediately create a separate liability regime for every AI-assisted corporate decision. Existing duties can remain the foundation, supplemented by practical guidance and proportionate obligations for higher-risk systems. Comparative law should be used cautiously: the EU's regulatory structure and the UK's company-law framework differ from India's institutional and statutory context. The goal is to identify useful governance practices, not to transplant foreign rules without considering local needs.

9. Recommendations for India

9.1 Adopt a risk-based internal AI governance policy

Companies should classify AI uses according to their potential impact. Low-risk administrative assistance may require limited controls, while AI affecting major investments, financial reporting, employment, customer eligibility or regulatory compliance should receive stronger scrutiny. The policy should identify permitted uses, prohibited uses, approval levels and escalation procedures.

9.2 Preserve meaningful human judgment

For material decisions, the responsible director or board committee should understand the purpose of the tool, the principal assumptions and the limits of its output. Human review must be substantive rather than a routine approval of an automated recommendation. Directors should be able to reject, question or seek verification of the output.

9.3 Record the decision-making process

For significant AI-assisted decisions, companies should document the tool's purpose, the material information considered, checks undertaken, identified risks, expert advice received and the reasons for accepting or rejecting the recommendation. Documentation can help the company learn from mistakes and allow later assessment of whether the process was reasonable. It should be proportionate and should not become a paperwork exercise detached from actual scrutiny.

9.4 Strengthen board competence and access to expertise

Boards do not need every director to become a computer scientist. They should, however, understand the material risks associated with the systems on which they rely. Companies should provide training and ensure access to suitable technical, legal, cybersecurity and compliance expertise where needed.

9.5 Conduct testing and ongoing monitoring

Before deploying an AI system for a material purpose, a company should assess its accuracy, reliability, security, data quality and suitability for the intended use. The assessment should be revisited when the system, data, business purpose or regulatory environment changes. An AI system that was appropriate for one task may not be appropriate for another.

9.6 Clarify vendor accountability

Contracts with AI providers should address data use, confidentiality, security, audit rights where appropriate, incident notification, system updates, access to records, allocation of responsibilities and remedies for breach. Contractual protections cannot eliminate all risk, but they can reduce uncertainty and support effective oversight.

9.7 Integrate AI into existing risk and compliance systems

AI governance should not sit separately from enterprise risk management, internal audit, data protection and cybersecurity. Companies should consider whether their existing board committees and reporting lines are adequate to supervise material AI risks. Listed entities should assess the relevance of applicable SEBI requirements.

9.8 Issue practical regulatory guidance

The Ministry of Corporate Affairs, SEBI and other competent regulators, within their respective mandates, could consider issuing practical guidance on board oversight of material AI use. Guidance could address risk assessment, documentation, human review, incident escalation and director training. A proportionate approach would be preferable to imposing identical requirements on every company, regardless of size, sector or risk.

9.9 Avoid automatic liability

Regulatory clarity should not make directors strictly liable merely because an AI-assisted decision results in loss. Liability should continue to depend on the applicable legal duty and the facts, including the reasonableness of the decision-making process. The purpose of governance is to encourage responsible oversight, not to punish every unsuccessful business judgment.

10. Conclusion

AI can improve the quality and efficiency of corporate governance, but it also makes it easier for decision-makers to rely on outputs they may not fully understand. The central legal challenge is therefore not whether AI should be used in companies, but how directors can use it without abandoning their responsibilities.

Indian company law already contains important principles for addressing this challenge. Section 166 of the Companies Act, 2013, requires good faith, care, diligence, independent judgment and avoidance of conflicts. Judicial decisions on directors' fiduciary obligations and corporate responsibility provide further guidance. These principles can apply to AI-assisted decisions even though they were not developed specifically for AI. Their application, however, requires attention to the nature of the system, the significance of the decision, the quality of oversight and the information available to the director.

This paper's central argument is that AI should assist corporate judgment, not replace it. Directors should not be treated as guarantors of every algorithmic output, but neither should they be permitted to use technology as an excuse for failing to ask reasonable questions. A defensible approach is one of proportionate responsibility: stronger checks for higher-risk decisions, meaningful human oversight, appropriate testing, clear records, access to expertise and effective vendor arrangements.

India can build on its existing corporate-law framework by providing practical guidance on AI governance and integrating AI risks into established board and compliance processes. Such an approach would protect accountability while allowing businesses to benefit from innovation. Ultimately, good AI governance is not about transferring responsibility to machines. It is about ensuring that the people who make and approve corporate decisions remain capable of explaining, supervising and taking responsibility for them.

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