



Directors' Duties versus Shareholder Interests: A Critical Study under the Indian Corporate Law Framework

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Abstract

The question of whether directors must prioritise shareholder interests or act in the broader interests of the company represents one of the most fundamental debates in corporate governance. Traditionally, corporate law was built upon the principle of shareholder primacy, under which directors were viewed as fiduciaries whose primary obligation was to maximise shareholder wealth. However, modern corporate law, including the Indian Companies Act, 2013, reflects a shift toward a more nuanced approach that recognises directors' duties toward the company as a separate legal entity and acknowledges the relevance of stakeholder interests such as employees, creditors, and society. This research paper critically examines the legal framework governing directors' duties in India, focusing on statutory provisions, judicial interpretations, and comparative perspectives. It analyses the extent to which Indian corporate law balances shareholder interests with broader corporate and stakeholder considerations. The paper argues that Indian corporate law adopts a hybrid model that moves beyond strict shareholder primacy while still preserving shareholder centrality. It further highlights doctrinal ambiguities, enforcement challenges, and governance concerns, and proposes reforms to strengthen clarity, accountability, and sustainable corporate governance.

Keywords: Directors' duties, Shareholder primacy, Stakeholder theory, Corporate governance, Companies Act 2013, Fiduciary duty.

I. Introduction

Corporate governance involves the system by which companies are directed and controlled. At its core lies the relationship between directors, who manage the company, and shareholders, who provide capital and hold ownership interests. This separation of ownership and control creates potential conflicts of interest, as directors may pursue objectives that differ from shareholder expectations.¹

Historically, corporate law emphasised the doctrine of shareholder primacy, which viewed directors as agents of shareholders whose primary duty was to maximise shareholder wealth. However, modern corporate governance frameworks increasingly recognise that directors owe duties to the company as a separate legal entity rather than to individual shareholders.² This distinction is particularly significant in situations where shareholder interests conflict with long-term corporate sustainability or stakeholder welfare.

The Companies Act, 2013 introduced a comprehensive statutory framework governing directors' duties in India. Section 166 codifies directors' fiduciary duties and explicitly requires directors to consider not only shareholders but also employees, the community, and environmental protection.³ This represents a significant departure from the traditional shareholder-centric approach.

This paper critically examines the relationship between directors' duties and shareholder interests under Indian corporate law. It explores statutory provisions, judicial precedents, theoretical perspectives, and comparative models, and evaluates whether Indian law prioritises shareholder interests or adopts a broader stakeholder-oriented approach.

II. Theoretical Foundations of Directors' Duties

A. Separate Legal Personality and Corporate Autonomy

One of the foundational principles of corporate law is that a company is a separate legal entity distinct from its shareholders. This principle was established in the landmark case of *Salomon v Salomon & Co Ltd*, where the House of Lords held that a company possesses its own legal personality independent of its members.⁴

¹ Adolf A. Berle and Gardiner C. Means, *The Modern Corporation and Private Property* (Transaction Publishers, 1932) 6.

² Paul L. Davies, *Introduction to Company Law* (Oxford University Press, 2010) 85.

³ Companies Act, 2013, §166.

⁴ *Salomon v Salomon & Co Ltd* [1897] AC 22 (HL).

As a result, directors owe duties to the company itself rather than directly to shareholders. This distinction ensures that directors act in the best interests of the corporate entity rather than merely serving shareholder preferences. This principle is essential because shareholders may have diverse and conflicting interests. Directors must exercise independent judgment to ensure the long-term sustainability and success of the company.

B. Fiduciary Nature of Directors' Duties

Directors occupy a fiduciary position, which means they must act with loyalty, honesty, and good faith. Fiduciary duties arise because directors exercise control over corporate assets and decision-making powers entrusted to them.⁵

The key fiduciary duties include:

1. Duty to Act in Good Faith

Directors must act honestly and in the best interests of the company. Their decisions should aim to promote the company's success rather than personal benefit or the interests of specific shareholders. This duty ensures loyalty and integrity in corporate governance.

2. Duty to Act for Proper Purposes

Directors must use their powers only for legitimate purposes and not for personal gain or to unfairly influence control of the company. Misuse of authority, such as issuing shares to manipulate voting power, would violate this duty.

3. Duty to Avoid Conflicts of Interest

Directors must avoid situations where their personal interests conflict with the company's interests. They must disclose any potential conflicts and refrain from participating in related decisions to ensure impartiality.

4. Duty Not to Make Secret Profits

Directors must not earn undisclosed profits from their position or misuse company opportunities for personal gain. Any such profit must be returned to the company, ensuring transparency and accountability.

5. Duty to Exercise Reasonable Care, Skill, and Diligence

Directors must perform their duties with reasonable care, competence, and diligence. They are expected to stay informed and make responsible decisions to protect the company's interests.

These duties ensure that directors do not abuse their powers for personal benefit or to favour particular shareholders.

C. Shareholder Primacy Theory

Shareholder primacy theory argues that the primary purpose of a corporation is to maximise shareholder wealth. According to Milton Friedman, the social responsibility of business is to increase its profits within the bounds of law.⁶ Under this theory:

1. Directors Act as Agents of Shareholders

Under the shareholder primacy model, directors are considered agents of the shareholders, who are the owners of the company. Directors are entrusted with managing the company on behalf of shareholders and are expected to make decisions that reflect shareholder interests. This agency relationship creates accountability, ensuring directors act responsibly and do not misuse their powers.

2. Corporate Success is Measured by Shareholder Returns

In the shareholder-centric approach, the success of a company is primarily evaluated based on the financial returns generated for shareholders, such as dividends and increase in share value. Higher shareholder returns indicate effective management and corporate performance. This approach focuses on profit maximisation as the main objective of corporate activity.

3. Directors Must Prioritise Shareholder Interests

Directors are expected to prioritise the interests of shareholders when making corporate decisions. This means they must act in ways that maximise shareholder wealth and protect shareholder investments. However, this duty must be exercised within legal limits and in good faith to ensure the long-term sustainability of the company.

This theory dominated corporate governance for much of the twentieth century.

However, excessive focus on shareholder profits has been criticised for encouraging short-termism and neglect of stakeholder welfare.

D. Stakeholder Theory

Stakeholder theory challenges shareholder primacy by arguing that corporations must consider the interests of all stakeholders, including employees, creditors, customers, and society.⁷

This theory recognises that corporate decisions affect multiple groups and that long-term corporate success depends on balancing these interests.

Indian corporate law increasingly reflects stakeholder-oriented governance.

III. Statutory Framework under the Companies Act, 2013

The Companies Act, 2013 represents a significant reform in Indian corporate law, particularly in relation to directors' duties.

⁵ L.S. Sealy, "Fiduciary Relationships", 20 Cambridge Law Journal (1962) 69.

⁶ Milton Friedman, "The Social Responsibility of Business is to Increase its Profits", New York Times Magazine (1970) 32.

⁷ R. Edward Freeman, *Strategic Management: A Stakeholder Approach* (Cambridge University Press, 1984) 25.

A. Codification of Directors' Duties under Section 166

Section 166 of the Companies Act, 2013 codifies directors' duties for the first time in Indian statutory law.⁸ Previously, directors' duties were derived primarily from common law principles.

Section 166(2) provides that a director shall act in good faith to promote the objects of the company for the benefit of its members as a whole and in the best interests of the company, its employees, shareholders, community, and environment.

This provision reflects several important principles:

First, directors must act in the interests of the company rather than individual shareholders.

Second, directors must consider stakeholder interests.

Third, directors must balance competing interests responsibly.

This represents a shift toward stakeholder-oriented corporate governance.

B. Duty to Exercise Independent Judgment

Section 166(3) of the Companies Act, 2013 requires directors to exercise independent judgment while performing their duties. This means directors must make decisions based on their own analysis and understanding, rather than blindly following the instructions of majority shareholders, promoters, or other external parties. This duty ensures objectivity, prevents undue influence, and protects the company's interests by promoting fair and responsible decision-making.

C. Duty to Exercise Care, Skill, and Diligence

Directors must act with reasonable care, skill, and diligence while managing the company's affairs. This requires them to remain informed, attend meetings regularly, and make decisions carefully and responsibly. The standard of care depends on the director's knowledge and experience. Failure to act with due care or negligence may result in liability for breach of duty.

D. Duty to Avoid Conflict of Interest

Section 166(4) requires directors to avoid situations where their personal interests conflict with the interests of the company. Directors must not use their position for personal benefit or engage in activities that compromise their loyalty to the company. This duty ensures honesty, fairness, and transparency in corporate governance.

E. Liability for Breach of Duty

Section 166(7) provides that directors who violate their duties may face legal consequences, including penalties. This provision ensures accountability and discourages misconduct, negligence, and abuse of power by directors. It strengthens corporate governance by holding directors responsible for their actions.

IV. Judicial Interpretation of Directors' Duties in India

Indian courts have played a crucial role in defining directors' duties and clarifying their relationship with shareholder interests.

A. Directors Owe Duties to the Company

In *Percival v Wright*, the court held that directors owe duties to the company rather than individual shareholders.⁹ This principle has influenced Indian corporate jurisprudence.

This ensures that directors prioritise corporate interests over individual shareholder demands.

B. Needle Industries Case

In *Needle Industries (India) Ltd v Needle Industries Newey (India) Holding Ltd*, the Supreme Court held that directors must act in good faith for the benefit of the company.¹⁰

The Court emphasised fairness and fiduciary responsibility.

It also recognised the importance of protecting minority shareholders.

C. Bajaj Auto Ltd v N.K. Firodia

The Supreme Court held that directors have discretion in corporate decision-making and must act in the company's best interests.¹¹

The Court recognised that directors are not bound to follow shareholder wishes blindly.

D. Tata Sons Ltd v Cyrus Investments Pvt Ltd

This landmark case clarified directors' fiduciary duties and corporate governance principles.¹²

The Supreme Court held that directors must act in the interests of the company rather than individual shareholders.

The Court reaffirmed director independence and corporate autonomy.

This case represents a major development in Indian corporate law.

E. Cook v Deeks and Corporate Opportunity Doctrine

In *Cook v Deeks*, directors diverted a corporate opportunity for personal benefit.¹³ The court held that directors breached their fiduciary duties.

This case established the principle that directors cannot misuse corporate opportunities.

⁸ Companies Act, 2013, §166.

⁹ *Percival v Wright* (1902) 2 Ch 421 (CA).

¹⁰ *Needle Industries (India) Ltd v Needle Industries Newey (India) Holding Ltd*, AIR 1981 SC 1298.

¹¹ *Bajaj Auto Ltd v N.K. Firodia*, AIR 1971 SC 321.

¹² *Tata Sons Ltd v Cyrus Investments Pvt Ltd*, (2021) SCC Online SC 272.

¹³ *Cook v Deeks* [1916] 1 AC 554 (PC).

F. Regal (Hastings) Ltd v Gulliver

This case reinforced that directors must not profit from their position without company consent.¹⁴ It emphasised strict fiduciary standards.

V. Conflict between Directors' Duties and Shareholder Interests

Conflicts between directors and shareholders may arise in several contexts.

A. Short-Term vs Long-Term Interests

Shareholders often prefer immediate profits, such as higher dividends or short-term increases in share value. In contrast, directors may focus on long-term sustainability by reinvesting profits, expanding the business, or adopting strategies that ensure future growth and stability.

Directors have a duty to balance these interests carefully. They must consider both the short-term expectations of shareholders and the long-term success of the company, ensuring that decisions benefit the company as a whole rather than providing only temporary gains.

B. Majority vs Minority Shareholders

Majority shareholders often have significant voting power, which allows them to influence the appointment and decisions of directors. In some cases, they may use this influence to pursue their own interests, such as approving decisions that benefit them personally while ignoring the interests of minority shareholders. To address this issue, the Companies Act, 2013 provides remedies under Sections 241–242, which allow minority shareholders to approach the National Company Law Tribunal (NCLT) if the company's affairs are being conducted in an oppressive or prejudicial manner. The Tribunal has the power to pass appropriate orders to protect minority shareholders and ensure fair management of the company.

C. Stakeholder Interests vs Shareholder Profit

Directors may prioritise employee welfare or environmental protection when making corporate decisions, especially if such actions promote the long-term interests and sustainability of the company. This means directors are not required to focus solely on maximising shareholder profits but may also consider the well-being of employees, social responsibility, and environmental impact.

Section 166 of the Companies Act, 2013 explicitly recognises this broader responsibility by stating that directors must act in the best interests of the company, its employees, the community, shareholders, and the environment. This provision legally empowers directors to take decisions that balance economic goals with social and environmental concerns.

VI. Comparative Perspective: United Kingdom

The UK Companies Act, 2006 adopts the enlightened shareholder value approach, which means that directors must promote the success of the company primarily for the benefit of shareholders, but while also considering the interests of other stakeholders. This approach recognises that long-term shareholder value can only be achieved by taking into account the needs of employees, customers, suppliers, and society.

Section 172 of the UK Companies Act, 2006 specifically requires directors to act in good faith to promote the success of the company while considering factors such as employee welfare, environmental impact, and business relationships. This ensures that directors do not focus only on short-term profits but also on the long-term growth and sustainability of the company.

This approach creates a balance between shareholder interests and stakeholder welfare. It acknowledges that protecting stakeholder interests ultimately contributes to the company's overall success and stability.

India's Companies Act, 2013 adopts a similar model under Section 166, which requires directors to act in the best interests of the company, its shareholders, employees, community, and environment. This shows that Indian corporate law also supports a balanced and responsible approach to corporate governance.

This similarity between UK and Indian law demonstrates global convergence in corporate governance, where modern legal systems increasingly recognise the importance of balancing shareholder profit with stakeholder protection and long-term corporate sustainability.

VII. Critical Analysis

A. Hybrid Governance Model

Indian corporate law adopts a hybrid model, which means it recognises the importance of shareholders while also considering the interests of other stakeholders such as employees, creditors, and the community. This approach moves beyond the traditional concept of strict shareholder primacy and promotes balanced corporate governance.

Shareholders remain important because they invest capital in the company and have ownership rights, including voting and receiving dividends. However, they are not the sole focus, as directors are also required to consider broader factors like long-term growth, employee welfare, and environmental protection.

Directors must act in the best interests of the company as a whole, rather than favouring only certain shareholders. This ensures that corporate decisions promote overall corporate sustainability, fairness, and responsible management, in line with Section 166 of the Companies Act, 2013.

¹⁴ Regal (Hastings) Ltd v Gulliver [1942] 1 All ER 378 (HL).

B. Strengths of Indian Framework

Statutory Codification of Directors' Duties

The Companies Act, 2013 clearly defines directors' duties under Section 166, providing a legal framework for their roles and responsibilities. This statutory codification brings clarity, transparency, and accountability, ensuring that directors act in good faith and in the best interests of the company.

Recognition of Stakeholder Interests

Indian corporate law recognises that directors must consider not only shareholders but also other stakeholders such as employees, creditors, the community, and the environment. This promotes responsible corporate governance and ensures long-term sustainability rather than focusing only on profit maximisation.

Judicial Protection of Corporate Integrity

Indian courts play an important role in ensuring that directors act honestly and do not misuse their powers. Through various judgments, courts have reinforced fiduciary duties and protected companies from fraud, mismanagement, and abuse of authority, thereby maintaining corporate integrity.

Minority Shareholder Remedies

The Companies Act, 2013 provides legal remedies under Sections 241–242 to protect minority shareholders from oppression and mismanagement.¹⁵ Minority shareholders can approach the National Company Law Tribunal (NCLT) for relief, ensuring fairness and preventing misuse of power by majority shareholders.

C. Weaknesses and Challenges

Despite significant reforms under the Companies Act, 2013, several challenges still exist in the effective implementation of directors' duties. One major issue is the lack of clarity in balancing stakeholder interests, as the law does not clearly specify how directors should prioritise between shareholders, employees, creditors, and other stakeholders when conflicts arise.

Additionally, weak enforcement mechanisms reduce the effectiveness of these legal provisions. Regulatory bodies and enforcement authorities may face practical limitations, such as delays, procedural complexities, and limited oversight, which weaken accountability.

There is also limited accountability in practice, as directors are not always held responsible for poor decisions or misconduct unless clear violations are proven. This makes it difficult to ensure consistent compliance with fiduciary duties.

These issues create governance uncertainty, as directors may be unsure about their exact responsibilities, and stakeholders may lack confidence in the effectiveness of corporate governance and legal protections.

VIII. Recommendations

Legislative clarification is necessary to clearly define the scope and extent of directors' duties, especially in situations involving conflicts between shareholder and stakeholder interests. Clear legal provisions will help directors understand their responsibilities and reduce ambiguity in decision-making.

Corporate governance standards must be strengthened by improving transparency, accountability, and ethical practices within companies. This can be achieved through better compliance mechanisms, stricter regulations, and effective monitoring of directors' conduct.

Judicial guidance should be expanded through consistent and well-reasoned judgments that clarify the interpretation of directors' duties. This will help develop clear legal principles and ensure uniform application of corporate law.

Minority shareholder protection must be enhanced by improving access to legal remedies and ensuring effective enforcement against oppression and mismanagement. Strong protection mechanisms will promote fairness and investor confidence.

These reforms will improve corporate governance by ensuring accountability, protecting stakeholder interests, and promoting responsible and sustainable management of companies.

IX. Conclusion

The relationship between directors' duties and shareholder interests is a fundamental aspect of corporate governance because directors are responsible for managing the company, while shareholders are the owners who invest capital and expect returns. Ensuring that directors act responsibly and in alignment with corporate objectives is essential to maintain trust, transparency, and effective management. Over time, Indian corporate law has evolved to address this relationship more clearly, especially with the enactment of the Companies Act, 2013, which introduced comprehensive provisions governing directors' roles, responsibilities, and accountability.

Section 166 of the Companies Act, 2013 represents a significant reform because it formally codifies directors' duties for the first time in Indian statutory law. It requires directors to act in good faith and in the best interests of the company while also considering stakeholders such as employees, shareholders, the community, and the environment. This provision reflects a shift from a purely shareholder-focused approach to a broader stakeholder-oriented model of corporate governance.

¹⁵ Companies Act, 2013, §§241–242.

Judicial decisions have further strengthened this framework by consistently holding that directors owe their fiduciary duties to the company as a separate legal entity, rather than to individual shareholders. Courts have emphasised that directors must act honestly, avoid conflicts of interest, and ensure fairness in corporate decision-making, even when shareholder interests are involved.

Indian corporate law therefore adopts a balanced or hybrid approach that protects shareholder rights while also promoting long-term corporate sustainability and stakeholder welfare. However, despite these advancements, further reforms are necessary to improve clarity in legal provisions, strengthen enforcement mechanisms, and ensure greater accountability of directors. Such reforms will enhance corporate governance, protect stakeholder interests, and ensure responsible and sustainable corporate management.

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16. Companies Act, 2013, §§241–242.
17. Companies Act, 2006 (UK), §172.