

Invisible Influence and No Accountability: Addressing the Role of Shadow Directors in Startups

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Abstract—The rapid evolution of the startup ecosystem in India has ushered in flexible business models and informal governance structures, often deviating from conventional corporate practices. Startups often function in fast-paced, informal environments where decisions are made quickly, and structures evolve over time. In such settings, individuals who are not officially appointed as directors frequently influence crucial business decisions behind the scenes. These individuals, often called *shadow directors*, operate without formal designation but possess significant control over company affairs. While the Indian Companies Act, 2013¹, specifically Section 2(60)², makes a passing reference to those whose directions the board follows, there remains no direct legal framework that defines or governs the role and liability of shadow directors. This creates an accountability gap, especially in startups where mentors, investors, or founding members may exert substantial influence without assuming statutory responsibilities.

This research explores the grey zone surrounding shadow directorship in the Indian startup ecosystem. By examining statutory provisions, judicial interpretations, and regulatory responses, it identifies loopholes in existing laws. The paper also draws comparisons from jurisdictions like the UK, Australia and Singapore, where shadow directorship is more clearly recognized and regulated.

The study highlights the risks posed to stakeholders due to the unchecked influence of such individuals. It argues that the absence of clear rules leads to moral hazards, conflicts of interest, and potential legal abuses. Finally, the paper proposes legal reforms and policy recommendations aimed at ensuring transparent governance, ethical leadership, and a more accountable startup ecosystem in India.

Index Terms—Shadow Directors, Startup Governance, Corporate Accountability, Companies Act, 2013, Informal Control, Regulatory Reform.

I. INTRODUCTION

The Indian startup ecosystem has seen an extraordinary boom over the past decade, with new ventures emerging rapidly across technology, finance, healthcare, and other sectors. In their early stages, startups often operate with lean teams, minimal bureaucracy, and informal decision-making structures. While this agility fuels innovation, it also creates governance challenges. One of the most overlooked yet pressing concerns in this context is the growing influence of *shadow directors*.

Unlike formally appointed directors, shadow directors work in the background, often in the form of founding members who exit from legal roles, influential investors, or senior advisors. They may not be listed on official company records, but their directions are followed by the board, making their influence legally and ethically significant. The problem arises because Indian company law does not clearly define or regulate such figures. Section 2(60)³, offers a vague mention of individuals "*in accordance with whose directions or instructions the Board of directors is accustomed to act*", but this has not translated into concrete legal accountability or judicial consistency.

This gap has major implications for corporate governance, especially in startups where a single individual's decisions can impact multiple stakeholders. Without a clear legal framework, these shadow directors evade responsibility in the event of mismanagement, fraud, or ethical breaches. Their

¹ *Companies Act, No. 18 of 2013, Acts of Parliament, 2013 (India).*

² *Companies Act, No. 18 of 2013, § 2(60), Acts of Parliament, 2013 (India).*

³ *Ibid.*

invisible hand may shape the company's direction, but they remain shielded from statutory duties and liabilities that formal directors must bear.

This paper seeks to address this regulatory blind spot by exploring the extent and impact of shadow directorship in startups. It aims to critically assess existing Indian laws, evaluate how other jurisdictions manage this issue, and propose reforms to ensure that those who exercise real control over companies are also held accountable. The objective is to strike a balance between encouraging entrepreneurial freedom and ensuring responsible governance in one of India's most dynamic economic sectors.

II. RESEARCH OBJECTIVES

- To define and contextualize the concept of shadow directors within the startup ecosystem.
- To analyse the legal position of shadow directors under the Companies Act, 2013⁴ and related judicial interpretations.
- To identify the gaps and ambiguities in existing Indian corporate governance laws concerning informal control and influence.
- To compare international legal frameworks, such as the UK and Australia, for regulating shadow directors.
- To evaluate the risks and implications of unregulated shadow directorship on stakeholders and startup operations.
- To propose legal and policy reforms that bring greater transparency, accountability, and formal recognition of shadow directors in India.

III. RESEARCH GAP

Although the role of shadow directors in corporate governance has drawn academic and judicial attention in developed jurisdictions, its specific manifestation within the Indian startup ecosystem remains significantly underexplored. Most existing scholarship focuses on board accountability in large, listed

companies, with little academic engagement devoted to informal power structures that dominate early-stage startups. Among the few notable contributions are *"The Concept of Shadow Directors in Indian Company Law"* by Arora and Jain⁵, and *"Unaccountable Controllers: Regulatory Concerns in Startups"* by Menon⁶.

Arora and Jain provided a foundational analysis of shadow directorship by unpacking Section 2(60) of the Companies Act, 2013⁷, and highlighting the interpretative challenges courts face in determining who qualifies as a shadow director. However, their study remains limited to statutory interpretation and does not explore sector-specific issues such as the startup environment, where non-board actors frequently influence critical decisions. Menon's work offers a broader regulatory critique of accountability in startup governance, identifying the potential misuse of informal authority by advisors and investors. Nevertheless, his research lacks a doctrinal and comparative lens and falls short of offering actionable reform proposals.

Indian corporate law, while progressive in director accountability and stakeholder protection, lacks clarity on the status, duties, and liabilities of individuals who exert de facto control without formal appointment. Unlike jurisdictions such as the UK, Singapore or Australia, which provide judicial tests and regulatory guidelines for identifying and disciplining shadow directors, India's legal framework remains vague, reactive, and inconsistent in enforcement.

Building on the foundation laid by earlier scholars, this paper adopts a focused, startup-specific perspective to examine the role of shadow directors in India. It addresses doctrinal ambiguities, explores international regulatory benchmarks, and proposes statutory, and policy reforms tailored to India's unique startup landscape. By bridging legal theory with practical implications, this study contributes meaningfully to the limited body of scholarship and offers concrete recommendations to enhance transparency and accountability in early-stage corporate governance.

⁴ *Companies Act, No. 18 of 2013, Acts of Parliament, 2013 (India).*

⁵ *Riya Arora & Kunal Jain, The Concept of Shadow Directors in Indian Company Law, 14 Indian J. Corp. L. 88 (2021).*

⁶ *Harish Menon, Unaccountable Controllers: Regulatory Concerns in Startups, 11 NALSAR Bus. L. Rev. 210 (2022).*

⁷ *Companies Act, No. 18 of 2013, § 2(60), Acts of Parliament, 2013 (India).*

HYPOTHESIS

The existing Indian corporate legal framework, particularly under the Companies Act, 2013⁸, lacks the clarity and specificity required to address the complex and evolving issue of shadow directorship, especially in the startup ecosystem. The absence of an explicit legal definition or regulatory mechanism for identifying and holding shadow directors accountable creates a governance vacuum where individuals can influence critical decisions without assuming statutory responsibility. This legal gap increases the risk of ethical misconduct, mismanagement, and stakeholder harm. While *Section 2(60)*⁹ indirectly touches upon the concept by referring to persons “*in accordance with whose directions the Board is accustomed to act,*” its application remains inconsistent and poorly enforced. Moreover, the current framework fails to address the startup-specific realities where founders, investors, and advisors often play dominant but unofficial roles. In contrast, jurisdictions like the UK, Australia and Singapore, have implemented clearer legal standards and enforcement mechanisms for shadow directorship, which could serve as potential models for reform in India. Therefore, the introduction of a targeted and comprehensive legal framework, i.e., defining, recognizing, and regulating shadow directors, is critical for promoting transparent governance and safeguarding stakeholder interests in India's dynamic startup landscape.

BACKGROUND

To understand the problem of shadow directorship in Indian startups, it is important to first examine the nature of startup governance itself. Startups typically emerge in fast-paced, high-growth environments where formal governance structures are minimal or still evolving. These ventures often rely on small founding teams, external advisors, and early investors who play key roles in strategic decision-making. Due to this informal nature of operations, individuals who are not officially appointed as directors frequently influence company policies, management, and critical

decisions without any statutory obligation or disclosure.

The concept of “*shadow directors*” refers to such individuals who exercise significant control over a company's affairs without being formally listed on its board. This phenomenon is not new to corporate law. In fact, the Companies Act, 2013, under Section 2(60)¹⁰, makes a passing mention of such persons whose directions the Board habitually follows. However, the statute stops short of providing a clear legal definition, tests of identification, or liability framework for such actors. This becomes particularly problematic in the context of startups, where informal influence is both common and culturally normalized. Globally, the issue of shadow directorship has been recognized and addressed more systematically. For example, the UK's Company Directors Disqualification Act, 1986¹¹, and Australia's Corporations Act, 2001¹², include detailed provisions that hold individuals accountable even without formal appointment, based on the substance of their control. Such regulatory clarity is largely absent in India, allowing shadow directors in startups to operate without transparency or consequence. This research aims to uncover how this gap in Indian law can be bridged by examining the startup ecosystem through a doctrinal and comparative legal lens.

RESEARCH METHODOLOGY AND SCOPE OF STUDY

This research adopts a doctrinal and comparative legal methodology, focusing on the interpretation, analysis, and critique of statutory provisions, judicial decisions, and regulatory practices relevant to the concept of shadow directors. The primary sources include the Companies Act, 2013¹³, along with judgments from Indian courts and relevant foreign case laws from jurisdictions that recognize and regulate shadow directorships, such as the United Kingdom, Australia, and Singapore.

The study is supported by secondary materials, including peer-reviewed academic journals, corporate

⁸ *Companies Act, No. 18 of 2013, Acts of Parliament, 2013 (India).*

⁹ *Companies Act, No. 18 of 2013, § 2(60), Acts of Parliament, 2013 (India).*

¹⁰ *Ibid.*

¹¹ *Company Directors Disqualification Act 1986, c. 46 (UK).*

¹² *Corporations Act 2001 (Cth) s 180 (Austl.).*

¹³ *Companies Act, No. 18 of 2013, Acts of Parliament, 2013 (India).*

law commentaries, government reports, startup policy documents, and publications from regulatory bodies such as the Ministry of Corporate Affairs (MCA) and the Securities and Exchange Board of India (SEBI). Special emphasis is placed on analysing how Indian legal norms compare with international practices to identify gaps in accountability and enforcement related to informal corporate influence.

A comparative legal framework has been employed to understand how other jurisdictions legally define shadow directors, determine liability, and ensure accountability in startup and private company contexts. This cross-jurisdictional analysis provides valuable insights for proposing reforms suited to India's unique startup ecosystem. The study is situated within a critical-descriptive framework, aiming not only to describe the current legal landscape but also to critically evaluate its effectiveness in addressing shadow directorship. It considers real-world startup dynamics where mentors, advisors, or investors may influence decisions without bearing legal responsibilities.

The scope of this research is limited to shadow directorship in private companies and startups. It does not extend to corporate governance issues in listed companies or non-corporate entities. The paper is focused on addressing the regulatory vacuum and legal ambiguity concerning shadow directors and proposing reformative solutions for improved transparency and accountability in early-stage ventures.

IV. UNDERSTANDING SHADOW DIRECTORSHIP IN STARTUPS

4.1 Meaning and Functional Characteristics of Shadow Directors

The concept of *shadow directors* finds its root in the recognition that some individuals, though not officially designated as directors, exercise significant influence over the board and corporate decisions. A shadow director is typically defined as *a person in accordance with whose directions or instructions the board of directors of a company is accustomed to act*. This definition is encapsulated in **Section 2(60)(v) of**

*the Companies Act, 2013*¹⁴, which includes a shadow director within the scope of an “*officer who is in default*.” Although Indian company law recognizes the concept, it does so narrowly and lacks operational clarity, particularly in identifying or enforcing accountability.

Shadow directors often operate informally, such as through economic leverage, close personal relationships, or strategic advisory roles, especially in startups where legal formalities take a backseat to growth and investor pressure. Their instructions may not always be overt or coercive; often, they stem from an implicit authority, reputation, or control over resources essential for the company's survival. The risk here lies not merely in their hidden involvement, but in their ability to steer company affairs without the legal responsibilities or liabilities imposed on officially appointed directors.

4.2 Shadow Directors vs. De Facto Directors vs. Nominee Directors

4.2.1 Shadow Directors vs. De Facto Directors

While both may not be officially appointed, a de facto director performs the functions of a director and participates actively in the decision-making process of the company. In contrast, a shadow director does not act as a director themselves but exerts indirect influence over those who do. A de facto director assumes a role that is indistinguishable in practice from that of a formally appointed director, for instance, attending board meetings, signing resolutions, and representing the company. Courts generally look at the substance of conduct over formal title to classify someone as a de facto director. Thus, while shadow directors influence the board from behind the scenes, de facto directors step into the shoes of a director in all but name.

4.2.2 Shadow Directors vs. Nominee Directors

A nominee director is a person formally appointed to the board by a specific stakeholder, typically a financial institution, investor, or creditor, to represent its interests. Unlike shadow directors, nominee directors hold an official position and have fiduciary duties toward the company, though they may also be expected to report to or protect the interests of the

¹⁴ *Companies Act, No. 18 of 2013, § 2(60), Acts of Parliament, 2013 (India)*.

entity that appointed them. The key distinction lies in legal recognition and accountability. Shadow directors, although influential, are not recorded in the company's official registers and thus often remain invisible to regulatory scrutiny. Nominee directors, on the other hand, are clearly identifiable and bound by the same legal obligations as any other director under the Companies Act. However, even nominee directors may risk becoming shadow directors themselves if they begin issuing instructions beyond their formal role and the board routinely acts on them.

In essence, while *de facto directors* derive their legal liability from acting as a director, and *nominee directors* derive their status from formal appointment, *shadow directors* derive their power from habitual and influential instructions—without any accompanying legal responsibility unless proven otherwise. This makes the role of shadow directors particularly elusive and dangerous, especially in startups where informal influence often overshadows formal governance structures.

4.3 Role and Influence in Startup Ecosystems

In startup ecosystems, shadow directorship emerges more frequently due to the informal, mentor-driven, and investment-heavy structure of governance. Startups often rely on incubators, accelerators, angel investors, or founding members who may not hold board positions but continue to dictate business strategy, financial decisions, or hiring. Examples include:

- A former founder who exits the company officially but retains operational control informally.
- A venture capitalist who regularly participates in strategy meetings and whose approval is mandatory for funding decisions or major business moves.
- A mentor who directs the CEO or CTO on key operational matters, without any official designation.

Such informal influence bypasses the corporate governance structure and compromises board independence, stakeholder protection, and accountability standards. The dynamic is compounded by power asymmetry between startups and investors, making early-stage ventures particularly vulnerable to shadow control.

4.4 Indicators of Shadow Control or Influence

Identifying a shadow director requires more than casual involvement; it hinges on demonstrable patterns of control or influence over the decision-making processes of the company's board. Courts and regulators typically look for specific indicators that suggest a person's directions or instructions are not mere suggestions but are habitually followed by the formal board. One key indicator is *habitual obedience*, i.e., when the board routinely acts on the person's advice or instructions, not as a matter of discretion or mutual agreement, but out of a pattern of deference or dependency. This does not require every decision to be influenced, but a consistent pattern where the individuals will significantly shape company policy is sufficient. Another significant marker is *control over critical resources*. In startup ecosystems, this may take the form of investors or founders who control funding, key technologies, or market access, leveraging this control to indirectly dictate board actions. Similarly, *informal veto powers*, such as the ability to block major decisions or influence appointments, can also suggest shadow directorship. The *use of intermediaries* is also common; individuals may exert their influence through nominee directors or loyal insiders who act as proxies on the board.

Furthermore, *access to confidential internal information* without holding any official role, *participation in strategic meetings*, and *approval of high-value decisions* without formal board membership are red flags. Courts also look at *email correspondences*, *internal memos*, and *meeting records* to assess whether a person's inputs were regularly sought and followed in a manner that goes beyond mere consultation. Importantly, *lack of independent judgment* by the board, strengthens the case for identifying shadow influence.

Taken together, these indicators underscore a functional reality where legal titles are disregarded, and power is exercised through informal but effective means. The recognition of such patterns is critical in ensuring accountability in corporate governance, particularly in startups where informal hierarchies are prevalent and often opaque.

V. LEGAL AND JUDICIAL FRAMEWORK

5.1 Section 2(60) of the Companies Act, 2013

The Companies Act, 2013¹⁵, introduces the concept of shadow directors indirectly through Section 2(60)¹⁶, which defines an "officer who is in default." Clause (viii) under this section includes any person "in accordance with whose directions or instructions the Board of Directors of the company is accustomed to act," thereby acknowledging the existence of individuals who exercise de facto control without holding formal positions. While this provision stops short of expressly defining "shadow directors," it is a critical legal foothold for holding such individuals liable in cases of non-compliance or corporate misconduct. However, this inclusion is narrow and conditional. It applies only when a consistent pattern of influence can be proved, i.e., casual advice or one-off instructions are insufficient. Furthermore, the term "accustomed to act" has been interpreted by the Indian and foreign courts to mean *habitual compliance*, which must be shown through consistent conduct. Without legislative guidelines or tests to ascertain this "accustomed conduct," establishing liability under this clause remains evidentially burdensome.

5.2 Other Applicable Provisions of the Companies Act, 2013

While Section 2(60)¹⁷ provides a starting point, other provisions of the Companies Act¹⁸ can be interpreted to include or extend accountability to shadow directors in specific contexts:

Section 166 – Duties of Directors

Section 166 of the Companies Act, 2013¹⁹ lays down the fiduciary duties of directors such as acting in good faith, avoiding conflicts of interest, and exercising reasonable care, skill, and diligence. Although this provision is directly applicable to formally appointed directors, Indian courts have in certain cases extended

these fiduciary standards to individuals who exert significant influence over the board's decisions without being formally appointed—that is, shadow directors.

When shadow directors guide or dictate board decisions, especially those that harm the company or its stakeholders, they may be treated as de facto fiduciaries. For instance, if a shadow director was involved in authorizing transactions that amounted to oppression of minority shareholders or mismanagement of company funds, courts may read fiduciary obligations into their conduct to hold them accountable.

Section 2(59)²⁰ – Definition of Officer

This section defines "officer" to include "any person in accordance with whose directions or instructions the Board of Directors is accustomed to act." This overlaps with Section 2(60)²¹, which defines "officer in default." The significance lies in how the law acknowledges the existence of influential actors outside the boardroom.

This inclusion strengthens the legal framework for recognizing shadow directors as officers, thereby making them potentially liable under other provisions that apply to company officers, such as those related to fraud or breach of duties. This definition also forms the basis for including such individuals in enforcement actions or regulatory probes.

Section 2(78)²² – Definition of Promoter

A promoter is someone who has been instrumental in setting up the company or has control over its affairs directly or indirectly. In many startup ecosystems, initial founders or investors, even after stepping down from directorship, continue to wield significant control over management decisions—often qualifying as shadow directors.

Promoters could be regarded as shadow directors, especially when their instructions are routinely followed by the board. This is crucial in startups where

¹⁵ Companies Act, No. 18 of 2013, Acts of Parliament, 2013 (India).

¹⁶ Companies Act, No. 18 of 2013, § 2(60), Acts of Parliament, 2013 (India).

¹⁷ *Ibid.*

¹⁸ Companies Act, No. 18 of 2013, Acts of Parliament, 2013 (India).

¹⁹ Companies Act, No. 18 of 2013, § 166, Acts of Parliament, 2013 (India).

²⁰ Companies Act, No. 18 of 2013, § 2(59), Acts of Parliament, 2013 (India).

²¹ Companies Act, No. 18 of 2013, § 2(60), Acts of Parliament, 2013 (India).

²² Companies Act, No. 18 of 2013, § 2(78), Acts of Parliament, 2013 (India).

founders may continue to influence strategic decisions despite not holding formal titles.

Section 447 – Punishment for Fraud

Section 447²³ penalizes fraud committed by “*any person*” in relation to the affairs of the company. This includes knowingly making false representations, diverting funds, or misleading investors or regulators. Shadow directors involved in fraudulent schemes, such as siphoning off funds or manipulating financial statements, can be held criminally liable under this section. Courts do not insist on formal designation; if intent, knowledge, and involvement can be shown, shadow directors can be prosecuted.

Section 339 – Personal Liability for Fraudulent Conduct

This section²⁴ provides that if it appears a company’s business was conducted with intent to defraud creditors or for any fraudulent purpose, the court may declare that any person knowingly involved in the misconduct shall be personally liable without any limitation of liability.

Shadow directors can be held liable under this section if it is proven they were knowingly directing or facilitating fraudulent operations, even if they held no official designation. This provision is particularly important in insolvency and winding-up proceedings where the veil of incorporation is lifted to expose real actors behind the fraud.

Section 149 – Composition of Board of Directors

Section 149²⁵ mandates the inclusion of independent directors on the boards of listed and certain public companies to ensure better governance and transparency. It aims to prevent undue influence from promoters, major shareholders, or hidden actors.

While the intent is to counter shadow control, in practice, mere compliance with board composition requirements may not prevent informal control. This highlights the limitations of formal structures in detecting or curbing the influence of shadow directors, who may still operate behind the scenes.

Section 170²⁶ – Register of Directors and Key Managerial Personnel

Companies are required to maintain a register of their directors and key managerial personnel, which ensures transparency regarding who is responsible for management.

Shadow directors are by nature absent from this register, but failure to disclose persons exercising effective control may trigger scrutiny under this provision. Regulatory authorities, during audits or investigations, may flag inconsistencies between decision-making influence and formal registry entries, helping identify shadow involvement.

Companies (Appointment and Qualification of Directors) Rules, 2014

The *Companies (Appointment and Qualification of Directors) Rules, 2014*²⁷ contain procedural safeguards around director appointments and related disclosures, with indirect relevance to shadow directorship. In particular:

- *Form DIR-2 and DIR-12* filings mandate companies to disclose consent of newly proposed directors, and file appointment forms within thirty days with the Registrar.²⁸ Non-disclosure or misfiling can raise red flags where boards “*appoint*” directors to serve as proxies for dominant influencers operating behind the scenes.
- Indirectly, recognition of “*small shareholders’ director*” under *Rule 7* provides transparency but does not extend to informal influencers. This lacuna highlights the need for rules requiring disclosure of persons exerting control without formal appointment, especially in private startups where shadow directorship is common.²⁹

While these Rules do not explicitly refer to shadow directors, gaps in disclosures and mechanisms for appointment can obstruct the ability of regulators or stakeholders to detect informal directorship or influence.

2.3 NCLT and NCLAT Interpretations

²³ *Companies Act, No. 18 of 2013, § 447, Acts of Parliament, 2013 (India).*

²⁴ *Companies Act, No. 18 of 2013, § 339, Acts of Parliament, 2013 (India).*

²⁵ *Companies Act, No. 18 of 2013, § 149, Acts of Parliament, 2013 (India).*

²⁶ *Companies Act, No. 18 of 2013, § 170, Acts of Parliament, 2013 (India).*

²⁷ *Companies (Appointment and Qualification of Directors) Rules, 2014 (India).*

²⁸ *Companies (Appointment and Qualification of Directors) Rules, 2014, r. 8, Form DIR-2/DIR-12.*

²⁹ *Id. r. 7 (Small shareholders’ director mechanism).*

The Indian tribunals, the *National Company Law Tribunal (NCLT)* and the *National Company Law Appellate Tribunal (NCLAT)*, have progressively addressed the concept of shadow directorship by applying statutory provisions to uncover informal influence. Notably, the tribunals have looked beyond formal titles to assess whether individuals functionally direct company affairs.

In *Bhavesh Harkishandas Mehta v. Kookmin Bank & Anr.*, the NCLT explicitly recognized that a person who is not formally appointed to the board but whose instructions the board habitually follows, unless given in a professional capacity, may be treated as a shadow director and deemed an “*officer in default*” under the Companies Act.³⁰ This formulation aligns with *Section 2(60)(viii)*³¹ and the broader definition in *Section 2(59)*³² that encompasses persons whose directions the board routinely obeys.³³

Similarly, in *Air India Ltd. v. Cochin International Airport Ltd. (2019)*, officials from the Ministry of Civil Aviation were held to a shadow-directorship standard when they repeatedly issued board-level instructions to Air India’s board. The Tribunal found that these ministers were effectively shadow directors, even without formal appointment, due to their habitual and direct involvement in corporate decision-making.³⁴

In *Raj Chawla v. SEBI*, the Delhi High Court considered the “accustomed to act” test under *Section 2(59)*³⁵. While Chawla was exonerated, the Court emphasised that *mere advice or influence is insufficient* unless the directors consistently act in alignment with the individual’s directions.³⁶ The Court’s analysis reinforces that shadow directorship depends on behavioural patterns rather than isolated interventions.

Moreover, in *Cyrus Investments v. Tata Sons & Ors.*, the NCLT differentiated between an “*officer in default*” and a true shadow director, noting that the latter term implies *secretive control* and conduct leading to corporate decisions adverse to stakeholders. The tribunal held that subtle influence in connection with wrongdoing could meet the threshold, even if the individual was never formally appointed.³⁷

Finally, in *In Re: Swastik Textile Mills Ltd. (1983)*, though not directly under NCLT jurisdiction, the Bombay High Court articulated that whether directors are “accustomed to act” in the direction of another can be determined based on “*instances of past behaviour or other material facts*,” not mere presumption.³⁸ This evidentiary standard has permeated tribunal reasoning in subsequent NCLT/NCLAT orders.

VI. ACCOUNTABILITY, ETHICS, AND LEGAL RISKS

6.1 Shadow Directors and Breach of Fiduciary Duties
While statutory fiduciary duties are explicitly imposed on formally appointed directors under *Section 166 of the Companies Act, 2013*³⁹, shadow directors operate in a grey zone. Courts have increasingly recognized that when individuals exercise decisive influence over the board’s decisions, they may be held to similar fiduciary standards. These duties include acting in good faith, avoiding conflicts of interest, and exercising due care and diligence. The Supreme Court in *MCD v. Gurnam Kaur*⁴⁰ observed that a person exercising de facto power should also be responsible for consequences, reinforcing this principle in governance. If a shadow director instructs the board to undertake an act that results in prejudice to the company or its shareholders, especially minority ones, such conduct may be construed as a breach of fiduciary

³⁰ *Bhavesh Harkishandas Mehta v. Kookmin Bank & Anr., NCLT (Mumbai), Company Appeal (AT) (Insolvency) No. 75 of 2024 (India).*

³¹ *Companies Act, No. 18 of 2013, § 2(60), Acts of Parliament, 2013 (India).*

³² *Companies Act, No. 18 of 2013, § 2(59), Acts of Parliament, 2013 (India).*

³³ *Companies Act, 2013 §§ 2(59), 2(60)(viii) (India).*

³⁴ *Air India Ltd. v. Cochin Int’l Airport Ltd., NCLT (Mumbai), CA 3641/1999 (India).*

³⁵ *Companies Act, No. 18 of 2013, § 2(59), Acts of Parliament, 2013 (India).*

³⁶ *Raj Chawla v. SEBI, 2010 SCC OnLine Del 90 (India).*

³⁷ *Cyrus Investments v. Tata Sons & Ors, Company Appeal (AT) No. 254 of 2018 (India).*

³⁸ *In re: Swastik Textile Mills Ltd., SCC OnLine Bom 367 (1983) (India).*

³⁹ *Companies Act, No. 18 of 2013, § 166, Acts of Parliament, 2013 (India).*

⁴⁰ *MCD v. Gurnam Kaur, (1989) 1 S.C.C. 101 (India).*

responsibility. This trend aligns with the broader judicial approach of substance over form, ensuring those in de facto control do not escape liability.

6.2 Corporate Veil and its Misuse

The doctrine of lifting of corporate veil, as enshrined in *Solomon v. A. Solomon & Co. Ltd.*⁴¹, creates a distinction between the company and its members or controllers. However, this corporate veil can be pierced in cases of fraud, improper conduct, or when the company is used as a façade. Shadow directors, though not officially recorded, may use this veil to shield themselves from liability while exercising significant influence. Indian courts, particularly under *Section 339 of the Companies Act, 2013*⁴², have allowed piercing of the corporate veil in situations where shadow directors used the company to defraud creditors or mislead regulators. In *Delhi Development Authority v. Skipper Construction Co. (P) Ltd.*⁴³, the Supreme Court held that the veil of incorporation can be lifted where it is used for fraudulent purposes.

6.3 Shadow Influence in Fraud, Insider Trading, and Misreporting

Shadow directors pose a heightened risk in white-collar offences, including financial fraud, insider trading, and misreporting of financial statements. Since their roles are unofficial, oversight mechanisms like board disclosures, audit trails, and regulatory inspections may not detect their involvement in time. If a shadow director directs a company officer to manipulate earnings, trade on non-public information, or commit accounting fraud, they may be found liable under laws including the *Companies Act, 2013*⁴⁴, *SEBI (Prohibition of Insider Trading) Regulations, 2015*⁴⁵, and the *Prevention of Money Laundering Act,*

2002⁴⁶. In *N. Narayanan v. Adjudicating Officer, SEBI*⁴⁷, the Court observed that persons who wield actual power behind the scenes cannot escape liability merely by not holding a formal designation. Their informal status does not exempt them from being prosecuted as “*officers in default*” under *Section 2(60)*⁴⁸.

6.4 Case Law Illustrations on Abuse of Position

In *Official Liquidator v. T. Venkateshwaran*⁴⁹, the Madras High Court held individuals who exert control over company decisions, despite lacking formal designations, are accountable for mismanagement. Similarly, in *In re: Neesa Leisure Ltd.*⁵⁰, the NCLT observed that promoters who continued to exercise decision-making authority after their resignation could be treated as shadow directors and held liable for lapses in financial compliance. In *In re: A. Raghuram v. R. Ananda Babu*⁵¹, the Tribunal recognised that shadow directors who took key financial decisions in a defunct company may be personally liable for losses caused to creditors.

6.5 Ethical Considerations in Corporate Influence

From an ethical standpoint, shadow directors challenge principles of corporate transparency and accountability. Their influence often escapes scrutiny, creating opacity in governance. Startups particularly suffer when founders or investors unofficially dictate decisions without corresponding accountability. This undermines stakeholder trust, diminishes board independence, and allows circumvention of checks such as conflict disclosures or audit review. Ethical corporate governance requires that all individuals exercising meaningful influence over decisions should be identifiable and subject to oversight, principles that

⁴¹ *Solomon v. A. Solomon & Co. Ltd.*, [1897] A.C. 22 (H.L.) (U.K.).

⁴² *Companies Act, No. 18 of 2013, § 339, Acts of Parliament, 2013 (India).*

⁴³ *Delhi Dev. Auth. v. Skipper Constr. Co. (P) Ltd.*, (1996) 4 S.C.C. 622 (India).

⁴⁴ *Companies Act, No. 18 of 2013, Acts of Parliament, 2013 (India).*

⁴⁵ *Securities & Exchange Board of India (Prohibition of Insider Trading) Regulations, 2015, Gazette of India, Extraordinary, Pt. III, sec. 4, Jan. 15, 2015 (India).*

⁴⁶ *Prevention of Money Laundering Act, No. 15 of 2002, Acts of Parliament, 2002 (India).*

⁴⁷ *N. Narayanan v. Adjudicating Officer, SEBI*, (2013) 12 S.C.C. 152 (India).

⁴⁸ *Companies Act, No. 18 of 2013, § 2(60), Acts of Parliament, 2013 (India).*

⁴⁹ *Official Liquidator v. T. Venkateshwaran*, (2006) 131 Comp. Cas. 648 (Mad.) (India).

⁵⁰ *In re: Neesa Leisure Ltd.*, (2019) SCC OnLine NCLT 13007 (India).

⁵¹ *In re: A. Raghuram v. R. Ananda Babu*, (2020) SCC OnLine NCLT 606 (India).

shadow directorship often violates. The *Kotak Committee on Corporate Governance (2017)*⁵² recommended the need for enhanced disclosures regarding persons exercising significant influence, even if not designated as directors, reflecting ethical imperatives.

6.6 Reputational and Financial Risks for Startups

Startups are especially vulnerable to the risks posed by shadow directors. The Bombay High Court in *Ajay Agarwal v. SEBI*⁵³ highlighted how undisclosed influence over management decisions can adversely affect corporate compliance and stakeholder confidence. When key decisions are driven by informal actors, whether founders, investors, or advisors, the company may engage in conduct that violates legal or ethical norms without appropriate documentation or oversight. This not only invites litigation and regulatory sanctions but also damages the firm's reputation in the eyes of investors, partners, and consumers. Moreover, undisclosed influence can derail funding rounds, delay compliance processes, and strain internal dynamics, ultimately affecting the company's valuation and long-term viability.

VII. COMPARATIVE ANALYSIS: GLOBAL REGULATORY APPROACHES

7.1 United Kingdom

The United Kingdom provides one of the most robust frameworks for the regulation of shadow directors. The *Companies Act, 2006*⁵⁴ and the *Company Directors Disqualification Act, 1986*⁵⁵ (CDDA) both include references to shadow directors and impose obligations and liabilities akin to those applicable to de jure directors.

Under *Section 251(1) of the Companies Act, 2006*⁵⁶, a "shadow director" is defined as "a person in accordance with whose directions or instructions the directors of the company are accustomed to act."⁵⁷ However, this excludes professional advisors or persons giving advice in their professional capacity. This definition sets a clear benchmark for determining shadow directorship through behavioural patterns rather than formal appointment.

The *CDDA, 1986*, under *Section 22(5)*⁵⁸ also adopts a similar definition and subjects shadow directors to disqualification proceedings where necessary. This shows the legislative intent to hold such individuals accountable when they act in a managerial capacity without formal title.

In *Re Hydrodam (Corby) Ltd*⁵⁹, the court clarified that mere influence does not qualify a person as a shadow director; the instructions must be acted upon by the majority of the board. The case emphasized the need to establish that directors were accustomed to act on the directions of the alleged shadow director. This approach was upheld in *Secretary of State for Trade and Industry v Deverell*⁶⁰, where the Court of Appeal widened the interpretation by emphasizing the distinction between consultation and control.

Furthermore, UK law imposes fiduciary and statutory duties under *Sections 170-177 of the Companies Act, 2006*⁶¹, which courts have occasionally extended to shadow directors, especially when they have participated in fraudulent or oppressive management.

7.2 Australia

Australia's *Corporations Act, 2001*⁶² provides a detailed and functionally aligned regulatory framework. *Section 9*⁶³ of the Act defines a director to include a person not formally appointed but who acts in the position of a director (de facto) or in accordance

⁵² SEBI Committee on Corporate Governance, Report of the Committee on Corporate Governance under the Chairmanship of Shri Uday Kotak (Oct. 2017), https://www.sebi.gov.in/reports/reports/oct-2017/report-of-the-committee-on-corporate-governance_36177.html.

⁵³ *Ajay Agarwal v. SEBI*, (2015) SCC OnLine Bom 4343 (India).

⁵⁴ *Companies Act 2006*, c. 46 (UK).

⁵⁵ *Company Directors Disqualification Act 1986*, c. 46 (UK).

⁵⁶ *Companies Act 2006*, c. 46, § 251 (U.K.).

⁵⁷ *Ibid.*

⁵⁸ *Company Directors Disqualification Act 1986*, c. 46, § 22(5) (UK).

⁵⁹ *Re Hydrodam (Corby) Ltd*, [1994] 2 BCLC 180 (Eng.)

⁶⁰ *Secretary of State for Trade and Industry v. Deverell* [2001] Ch. 340 (Eng.)

⁶¹ *Companies Act 2006*, c. 46, § 170-177 (UK).

⁶² *Corporations Act 2001 (Cth) s 180* (Austl.)

⁶³ *Corporations Act 2001 (Cth) s 9* (Austl.).

with whose instructions or wishes the directors are accustomed to act (shadow director).

In *Grimaldi v Chameleon Mining NL (No 2)*⁶⁴, the Full Federal Court explicitly affirmed the fiduciary obligations of shadow directors. The court found that a corporate advisor who exercised influence over the board was effectively a shadow director and liable for breaches of fiduciary duty.

Australia's regulatory body, the *Australian Securities and Investments Commission (ASIC)*, has also taken proactive steps to investigate and prosecute shadow directors in cases involving mismanagement or deceit. *ASIC Regulatory Guide 217* outlines the enforcement strategies against such hidden controllers, emphasizing deterrence and transparency.

7.3 Singapore

Singapore's *Companies Act (Cap. 50)*⁶⁵ recognizes shadow directors under *Section 4(1)*⁶⁶, which defines a director to include a person "in accordance with whose directions or instructions the directors of a corporation are accustomed to act." The definition is closely modelled on UK legislation.

In *Ho Kang Peng v Scintronix Corp Ltd*⁶⁷, the Court of Appeal considered the liability of a person alleged to be a shadow director and emphasized the role of factual influence in determining shadow control. The case reaffirmed that even informal authority could result in personal liability where management decisions are significantly influenced by the individual.

Regulatory interventions by the *Accounting and Corporate Regulatory Authority (ACRA)* aim to ensure accurate disclosures and reduce shadow control in listed entities. Singapore's courts also emphasize corporate transparency and board autonomy.

⁶⁴ *Grimaldi v. Chameleon Mining NL (No. 2) (2012) 200 FCR 296 (Austl.)*

⁶⁵ *Companies Act 1967, Cap. 50 (Sing.)*.

⁶⁶ *Companies Act 1967, Cap. 50, § 4(1) (Sing.)*.

⁶⁷ *Ho Kang Peng v. Scintronix Corp Ltd., [2014] SGCA 22 (Sing.)*.

⁶⁸ *Companies Act, No. 18 of 2013, Acts of Parliament, 2013 (India)*.

⁶⁹ *Ibid.*

⁷⁰ *Companies Act, No. 18 of 2013, § 2(60), Acts of Parliament, 2013 (India)*.

VIII. KEY TAKEAWAYS FOR INDIAN LEGAL REFORM

Despite growing judicial recognition of the concept of shadow directorship, the Indian legal framework remains under-equipped to comprehensively regulate it. While de jure directors are bound by clearly codified fiduciary duties, those who operate without formal appointment and yet wield considerable influence continue to escape scrutiny due to a legislative blind spot.

India's Companies Act⁶⁸ currently does not explicitly mention "shadow directors," and the term has no statutory definition. Instead, India relies on related concepts like "officer in default" to reach undeclared directors. For example, the Act's⁶⁹ definition of "officer who is in default" (section 2(60)⁷⁰) essentially covers anyone whose instructions the board customarily follows⁷¹. In practice, regulators have applied this notion to influential shareholders and promoters. Notably, in the *Sahara case (In Re: OFCDs by Sahara India Real Estate Co., SAT (2011))*⁷², the Securities Appellate Tribunal treated Mr. Subrata Roy, a major shareholder who effectively commanded company decisions, as an officer in default because the board habitually took his directions. This suggests that Indian law can reach shadow director conduct under the broad "officer" definition, but only by analogy rather than direct rules.

One of the most glaring omissions in the current regulatory regime is the absence of a requirement to disclose individuals who act as informal influencers. Neither the Companies Act nor the SEBI (Listing Obligations and Disclosure Requirements) Regulations⁷³ mandate the reporting of such de facto controllers. This lack of transparency impedes

⁷¹ *Nishith Desai Associates, The Unseen Influencers: Shadow Directors, Yes, Governance Matters (Jan. 5, 2024)*,

https://www.nishithdesai.com/fileadmin/user_upload/Html/Hotline/Yes_Governance_Matters_Jan0524_M.htm

⁷² *Sahara India Real Estate Corp. Ltd. v. Sec. & Exch. Bd. of India, (2013) 1 S.C.C. 1 (India)*.

⁷³ *Securities & Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015, Gazette of India, Extraordinary, Pt. III, sec. 4, Sept. 2, 2015 (India)*.

corporate governance and weakens shareholder oversight. It also makes it difficult for creditors, regulators, and stakeholders to determine who is truly responsible for the company's strategic direction and compliance posture.

In practice, imposing fiduciary duties on de facto controllers would improve accountability. For example, India could follow Singapore's lead by clarifying that persons who control the board (e.g. a majority of directors) are automatically treated as directors for purposes of duties and liabilities. Similarly, codifying a definition akin to UK s.251⁷⁴ would prevent powerful outsiders from evading responsibility. In short, the comparative review suggests that Indian law would benefit from explicitly recognizing shadow directors. This could entail a statutory definition (or an expanded "officer" definition) and making clear that hidden influencers owe the same duties and disqualification risks as ordinary directors⁷⁵. The absence of a definition not only leads to interpretational inconsistencies but also allows persons with significant but informal control to evade liability by simply denying formal association. If we were to consider the situation of startups in India; they present a unique challenge. Founders, early-stage investors, mentors, and accelerators often assume central roles in decision-making despite lacking formal designations. This informality is often celebrated as agility, but it can quickly become a liability when disputes arise, or when regulatory scrutiny is triggered. Sector-specific governance codes should be developed to identify when informal roles turn into actionable responsibilities. Guidelines must outline when advisory input becomes controlling behavior, how such individuals should disclose conflicts of interest, and what fiduciary standards they may be held to if found to exert de facto control. Such a framework would protect startups from unintentional violations and reduce risks for both founders and investors.

Such reforms would bring Indian corporate law in line with global standards, ensuring that de jure loopholes cannot be used to shirk directorial accountability.

IX. RECOMMENDATIONS AND POLICY PROPOSALS

Addressing the legal opacity surrounding shadow directors in India demands a multi-pronged reform strategy that combines statutory clarity, regulatory action, and practical implementation mechanisms. As India's corporate and startup ecosystem grows in complexity and global interconnectivity, the risks posed by unaccountable informal controllers, particularly in startups and family-run businesses, are no longer hypothetical. It is now critical to move beyond ad hoc judicial recognition and piecemeal interpretation toward a cohesive governance framework that ensures accountability, transparency, and legal predictability.

First, a statutory recognition of the concept of shadow directorship must be introduced into the Companies Act, 2013⁷⁶. This would bring Indian company law in line with jurisdictions such as the United Kingdom, where the Companies Act 2006⁷⁷ defines a shadow director as "a person in accordance with whose directions or instructions the directors of a company are accustomed to act." The absence of such recognition in India not only impairs enforcement but also creates a legal vacuum that emboldens covert influence and indirect manipulation. A statutory definition would set the stage for regulating such influence and applying fiduciary responsibilities to those behind the scenes who, while not officially appointed, essentially shape the company's affairs.

Second, a system of mandatory disclosures should be introduced. Informal influencers such as startup advisors, venture capital representatives, and founding family members often play a pivotal role in governance without assuming formal titles. It is recommended that the *Companies (Appointment and*

⁷⁴ *Companies Act 2006, c. 46, § 251 (U.K.).*

⁷⁵ *Nishith Desai Associates, The Unseen Influencers: Shadow Directors, Yes, Governance Matters (Jan. 5, 2024),*
https://www.nishithdesai.com/fileadmin/user_upload/

Html/Hotline/Yes_Governance_Matters_Jan0524_M.htm

⁷⁶ *Companies Act, No. 18 of 2013, Acts of Parliament, 2013 (India).*

⁷⁷ *Companies Act 2006, c. 46 (U.K.).*

*Qualification of Directors) Rules, 2014*⁷⁸ be amended to mandate disclosures of individuals who are not formally designated directors but whose instructions are routinely followed by the board. Annual reports and the Register of Directors and Key Managerial Personnel should include a separate section identifying such individuals based on objective criteria such as the frequency and nature of their involvement in decision-making.

Third, clear and measurable thresholds must be established to differentiate between casual advisory roles and those amounting to shadow directorship. The mere provision of advice, particularly in a consultative capacity, should not attract liability. However, repeated involvement in core decisions, such as financial structuring, strategic partnerships, policymaking, or boardroom appointments, should constitute an adequate threshold for regulatory scrutiny. This could be operationalized through judicial guidelines, SEBI advisory notes, or circulars by the Ministry of Corporate Affairs, offering a fact-based checklist for regulators and courts to assess whether the role of an individual meets the threshold of a de facto or a shadow directorship.

Fourth, specific governance guidelines should be developed for venture capitalists, angel investors, and incubators. These stakeholders often occupy dual roles, providing capital and strategic input, making it easy for the line between oversight and control to blur. It is recommended that DPIIT (Department for Promotion of Industry and Internal Trade) and SEBI jointly issue sector-specific codes of conduct that outline the permissible scope of investor involvement in governance and clarify when such involvement triggers disclosure obligations or fiduciary duties. These guidelines should also include conflict-of-interest protocols and internal governance audits.

Fifth, regulatory awareness and training initiatives are essential. Many startup founders and directors, particularly in early-stage companies, are unaware of the legal implications of informal influence. Governmental and industry bodies, such as the MCA,

Startup India, NASSCOM, and TiE, could develop accessible training modules and handbooks explaining the concept of shadow directorship, its risks, and compliance measures. Law schools and professional institutes can also integrate these subjects into their corporate governance subjects, thereby nurturing a culture of proactive compliance.

Sixth, the Ministry of Corporate Affairs should consider publishing a Model Governance Code for startups and private companies. This code can provide sample board charters, advisory engagement contracts, disclosure templates, and red flags for identifying shadow directorship and their influence over any such organisation. A voluntary but widely adopted governance model would standardize best practices across the ecosystem and serve as a benchmark for companies, auditors, investors, and courts alike.

Finally, a coordinated response from multiple regulatory bodies is required. The SEBI must update its Listing Obligations and Disclosure Requirements (LODR) to capture and disclose shadow influence in listed companies. The MCA should issue explanatory circulars, FAQs, or amendments clarifying when shadow directors can be held liable under Sections 166⁷⁹, 2(60)⁸⁰, and 447⁸¹ of the Companies Act. DPIIT should incorporate governance metrics into its Startup India recognition scheme to incentivize transparency. Such synergy across regulators will ensure that reforms are not merely theoretical but embedded into practice, enforcement, and compliance culture.

Conclusively, addressing the problem of shadow directors is not just a matter of legal reform, it is a governance imperative for India's evolving corporate landscape. The recommendations proposed here aim to strike a balance between entrepreneurial flexibility and regulatory accountability, empowering startups to thrive while ensuring that no person wields power without responsibility.

⁷⁸ *Companies (Appointment and Qualification of Directors) Rules, 2014, Gazette of India, Extraordinary, Pt. II, sec. 3(i), Mar. 26, 2014 (India).*

⁷⁹ *Companies Act, No. 18 of 2013, § 166, Acts of Parliament, 2013 (India).*

⁸⁰ *Companies Act, No. 18 of 2013, § 2(60), Acts of Parliament, 2013 (India).*

⁸¹ *Companies Act, No. 18 of 2013, § 447, Acts of Parliament, 2013 (India).*

X. CONCLUSION

The analysis of shadow directorship in the Indian corporate landscape reveals a persistent legal grey zone, wherein individuals exert decisive influence over company affairs without formal accountability. The Companies Act, 2013⁸², while comprehensive in addressing the role and duties of officially appointed directors, remains insufficient in tackling the reality of informal or indirect control. Judicial interpretations have occasionally extended fiduciary duties to such actors, but the absence of statutory recognition, clear reporting norms, and enforcement mechanisms weakens their impact. Comparative insights from jurisdictions like the UK, Australia, and Singapore further highlight the gap between India's legal infrastructure and evolving global standards.

Legal Recognition vs. Practical Enforcement

Recognizing shadow directors through statutory amendments is a necessary first step, but recognition without enforcement has limited value. The Indian regulatory system must evolve to balance form with substance. Regulatory bodies such as the MCA, NCLT, and SEBI must play a more proactive role, not only by interpreting the law dynamically but also by deploying investigative and compliance tools to uncover indirect control structures. Similarly, corporations must embed governance protocols that identify, record, and monitor informal influencers, moving from reactive compliance to preventive governance.

Reinforcing Accountability without Stifling Innovation

Startups, by nature, operate in fast-paced, flexible environments where advisors, mentors, and investors often blur formal governance lines. Over-regulation risks deterring mentorship and strategic support that many early-stage companies rely on. Therefore, any reform must be proportionate, establishing thresholds and clarity on when involvement crosses into liability, without penalizing genuine advisory roles. Encouraging disclosure, setting industry-specific governance standards, and providing clarity on

obligations will go a long way in ensuring innovation and compliance are not viewed as mutually exclusive.

Final Thoughts on a Balanced Regulatory Framework
Ultimately, shadow directorship is a challenge not of legality alone, but of corporate ethics and accountability. A well-rounded legal framework must recognize the nuanced nature of corporate influence while holding power to account, regardless of title or designation. By aligning statutory language with commercial realities, enhancing transparency requirements, and cultivating a culture of responsible governance, India can ensure that corporate control is exercised with integrity, fairness, and legal responsibility, while paving the way for robust, ethical, and investor-friendly business environments.

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