

ARTIFICIAL INTELLIGENCE AS A CORPORATE DIRECTOR – FEASIBILITY AND LIABILITY

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ABSTRACT

The acceleration of artificial intelligence (AI) development has prompted a good deal of speculation about future possibilities for AI in Relation to corporate governance and notable whether AI system will ever serve as corporate directors. This dissertation investigates whether AI, as a decision making machine with advanced predictive analytics and remarkable operational efficiencies could sensibly participate in decisions made in a boardroom. In so doing the research contemplates the legal, ethical and practical dimensions associated with the inclusion of AI, including responsibilities, accountability, fiduciary duties and corporate misconduct or negligence. In order to evaluate the ability of AI in a directorship capacity, this research evaluates the law and governance surrounding corporation in a critical manner to assess whether they can be accommodated. Comparative consideration should also be taken in regard to different jurisdictions that are experimenting with AI and important perspective from the global level can be implemented. In conclusion, this research identifies both the potential opportunities and the inherent challenges proposing AI as an actual corporate director, while cautiously concluding that while it can potentially bring significant transparency and efficiencies to recognised corporate governance, it still presents a dilemma given the lack of accountability and legal identity presently contemplated for AI to assume role as a director. This research will offer recommendations as to regulatory changes, hybrid governance structure and accountability as a strategy moving forward, so that corporation can still benefit from innovation, while advancing corporate accountability and responsibility.

INTRODUCTION:

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The swift advancement of Artificial Intelligence (AI) is reshaping business decision-making, spanning predictive analytics to automated compliance. In relation or within corporate governance, there will be discussions on whether AI can go from being a tool to being a decision-maker at the board level. Can an AI system fulfill the role of a corporate director, responsible for fiduciary duties and oversight of strategy that has historically been allocated to humans? If the answer is yes, where does responsibility lie when decisions made by AI lead to corporate success or failure? AI is front of mind in discussions around operational contexts, but the exploration of AI in governance and liability frameworks is limited. There will be discussions on whether AI can be used as a corporate director and then liability will stem from that. And whether reforms in law and/or governance frameworks are needed to accommodate AI taking on decision-making authority.

LITERATURE REVIEW:

The study concludes that under Indonesian law, Artificial Intelligence (AI) cannot serve as a company director because it is legally classified as an object under human supervision (Civil Code Article 1367) and directors must be natural persons with legal capacity (Company Law Article 93). While AI can assist in data analysis and decision-making it lacks free will, conscience, and emotional intelligence needed for corporate governance. Therefore, AI is better suited as a support tool for human directors rather than a legal subject occupying the role itself.

The research "Using Artificial Intelligence as a Corporate Director" assesses whether AI could serve as adherent to the duties of care and loyalty as a member of a board of directors. The researchers focus on competency as it pertains to fiduciary duties in corporate governance and explores if AI can fulfill the same legal responsibilities as humans. This paper holds the position that if AI is neutral, fast, and competent, then it can provide value to corporate governance and decision-making as AI can mitigate the biases and conflicts of interest that humans face as board members. The researchers clarify that the practical ability of AI alone will not allow AI to serve in the role of director; therefore, regulations must define who is authorized as a director and what duties AI must adhere to in such role. If developed appropriately, AI should meet the "duties of care" and loyalty when serving as a director. However, the accountability of AI remains challenging because the algorithms often lack transparency. The paper contemplates two constructs of responsibility: one being a legal model of responsibility, wherein liability rests with

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the developers and/or company thus holding the corporations responsible for AI's actions; and the second assumes a model of compensatory responsibility acknowledging the challenges of assigning liability. Ultimately, significant reforms to policy and regulation will be necessary for AI to act as directors of corporations, particularly in areas of government-appointed commissions, with human resources challenges to address.

The article Artificial Intelligence as a Director of a Limited Liability Company from a Legal Perspective analyzes whether AI could serve as a director for a limited liability company, with focus on PT Suryadhamma Investama (PT SI) in Indonesia that tried to appoint the AI system called Ardi. The authors note that the current Indonesian company law requires that the director be a natural person with legal capacity and AI cannot be because AI is a legal object instead of a legal subject. While AI may provide data analysis to assist with decision-making and risk assessment, it does not satisfy the legal status and obligations of a director when it comes to liability. The article describes a lack of regulatory framework liabilities around accountability and transparency about interactions with AI. The authors say AI can complement but cannot act as a director within the existing laws before other reforms are made.

RESEARCH OBJECTIVES:

Under what legal, ethical, and operational frameworks could an Artificial Intelligence achieve the functional responsibilities of a corporate director in a company, and what are the primary governance challenges to its implementation?

To what extent can existing legal frameworks for director liability accommodate an artificial intelligence acting as a corporate director

Who should be held legally liable for the acts or omissions of an AI director—the developers, the deploying company, or the board collectively?

RESEARCH METHODOLOGY:

This study employs a doctrinal research method to analyze the legal feasibility and liability of artificial intelligence (AI) serving as a corporate director within the framework of Indonesian law. Using secondary data sourced from legal statutes, academic literature, and international case

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studies. The study adopts a qualitative supplemented with comparative and analytical methods. The research is exploratory in nature, seeking to examine the feasibility of Artificial Intelligence (AI) being appointed as a corporate director and to evaluate the potential liabilities associated with such an appointment.

COMPANY DIRECTOR:

In simple terms, the 'director' is the supreme executive authority in the company, who is entrusted with the management and control of the company's affairs. Generally, a company has a team of directors, which are ultimately responsible for the entire management of the company's state of affairs. These teams of directors are collectively known as the Board of Directors'. In Ideal corporate governance practice, it is the team of directors that ensures the protection of the stakeholders of the company and of other members of the company.

This institution of the formulation of a team of members, known as directors, was based on the foundation that a company must have a team of faithful, trustable, and respectable members who work for the betterment of the company. They are appointed to work for the company's best interests. It is pertinent to mention here that the directors do not work in an individual capacity, unless specifically said so, in any board resolution meeting. It means that all the directors have to work collectively. The work done by any director in its individual capacity is not binding on the company.

The term 'director' is defined under Section 2(34) of the Companies Act 2013 (hereinafter referred to as the 2013 Act). It states that a 'director', "means a director appointed to the board of a company. The definition provided under the 2013 Act is not an exhaustive one. This section corresponds to Section 2(13) of the Companies Act, 1956. It defines a director as "any person occupying the position of director by whatever name called"

According to Section 5(2) of the Small Coins (Offences) Act, 1971 (repealed), the term 'director' in relation to a firm is said to be the partner of the firm. Whereas, if the term is used in relation to a society or association, It connotes the person who has been conferred with the management and control of the affairs of that particular society or association under the concerned rules.

In the case of *Agrawal Trading Corpa v. Collector of Customs* (1972), It was held by the Apex Court that the meaning of the term 'director' in relation to a firm connotes to the partner of that firm.

In conclusion, the term director connotes a person who has been elected or appointed in accordance with the law and who has been conferred with the task or function of managing and directing the affairs of a company. Directors are often regarded as the brains of a company. They hold a pivotal position in a company's structure as they make important decisions for the company in board meetings or in special committee meetings organised for certain particular purposes. Also, It is noteworthy that a director has to work in compliance with the provisions of the 2013 Act.

ARTIFICIAL INTELLIGENCE TRAINING MODELS:

When businesses talk about AI, they often talk about “training data.” But what does that mean? Remember that limited-memory artificial intelligence is AI that improves over time by being trained with new data. Machine learning is a subset of artificial intelligence that uses algorithms to train data to obtain results. In broad strokes, three kinds of learnings models are often used in machine learning:

Supervised learning is a machine learning model that maps a specific input to an output using labeled training data (structured data). In simple terms, to train the algorithm to recognize pictures of cats, feed it pictures labeled as cats.

Unsupervised learning is a machine learning model that learns patterns based on unlabeled data (unstructured data). Unlike supervised learning, the end result is not known ahead of time. Rather, the algorithm learns from the data, categorizing it into groups based on attributes. For instance, unsupervised learning is good at pattern matching and descriptive modeling.

In addition to supervised and unsupervised learning, a mixed approach called semi-supervised learning is often employed, where only some of the data is labeled. In semi-supervised learning, an end result is known, but the algorithm must figure out how to organize and structure the data to achieve the desired results. Reinforcement learning is a machine learning model that can be broadly described as “learn by doing.” An “agent” learns to perform a defined

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task by trial and error (a feedback loop) until its performance is within a desirable range. The agent receives positive reinforcement when it performs the task well and negative reinforcement when it performs poorly. An example of reinforcement learning would be teaching a robotic hand to pick up a ball.

ANALYSIS:

Exploring the potential of AI as a corporate director:

AI has the ability to sift through vast amounts of data much quicker than human directors. With tools like predictive analytics, market forecasting, and risk assessment, it can enhance the decision-making process for boards. Unlike humans, AI isn't swayed by personal biases, fatigue, or conflicts of interest.

However, current corporate laws around the globe still view directors as natural persons with legal standing. Directors are expected to uphold fiduciary duties—like loyalty, care, and diligence—that AI simply can't fulfill in a legal or moral sense. Some places, like Saudi Arabia and certain free zones in the UAE, have started to explore limited legal roles for AI, but we're not at the point of having AI as full-fledged directors just yet.

Instead, AI could function as a valuable advisory tool or a “shadow director,” supporting boards without taking their place. A hybrid board, combining human insight with AI efficiency, could strike the perfect balance between effectiveness and accountability.

LIABILITIES ISSUES:

Human directors have a responsibility to act with care, loyalty, and good faith towards shareholders. Since AI doesn't have legal personhood, it can't be held accountable for any breaches of duty. So, if an AI director makes a decision that leads to harm, who takes the fall? Is it the company, the programmers or developers, or perhaps the board members who decided to use the AI? Current corporate governance frameworks, like the Companies Act in India, the UK Companies Act, and US Corporate Law, still don't recognize AI as directors. The use of AI in decision-making raises some important questions.

In terms of carrying out a legal act, Article 1329 of the Civil Code specifies that "every person is capable of making obligations, unless he is determined to be incapable by law." Essentially, everyone has rights and obligations as legal entities; however, not everyone has the legal capacity to do legal acts.

CONCLUSION:

The primary difficulty in appointing an AI to the board of directors of a corporation is that everywhere in the world, legal frameworks only recognize natural persons, or some other type of legal entity (corporation), as directors. Directors are charged with very substantial decisions, including the duty of care and the duty of loyalty; neither is something that an AI has the legal capacity to fulfill. Directors have a legal requirement to act in the best interest of the company and its shareholders, and amount of sophistication an AI might have, could never have an "interest" or a conscience, and therefore cannot become subject to any moral and ethical obligations that could attach to a person. A human director can be made personally liable for breaches of duty, negligence, or illegal acts. When an AI makes a decision that is harmful or flawed, it is difficult, if not impossible, to assign liability. Is it the programmer? The data provider? The entity deploying the AI? This legal vacuum is unacceptable for shareholders or the public. Finally, a large number of AI models, particularly the more complex such as deep neural networks, are essentially "black boxes" to an extreme degree. They make a decision in a very precise but vague manner and it is incredibly difficult to explain what rationale led to a particular decision. This conflicts with the legal requirement for directors to have a justification for their actions and decision-making process.

SUGGESTION:

Let's establish some legal and regulatory guidelines that clearly outline the roles and responsibilities of both the human board and the AI system. This framework should make it clear who's liable, ensure transparency in AI algorithms, and require regular audits of how AI makes decisions. It's crucial that policies and laws specify who is responsible when an AI system causes harm. This might mean creating new legal concepts that hold the AI developer accountable as a "producer" or placing "user" liability on the company's human leaders for not properly supervising the AI tool.

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Companies and governments should also invest in training for directors so they can grasp the capabilities and limitations of AI. This way, human directors can effectively oversee operations and make informed choices instead of just following an AI's suggestions without question.

Given the wide range of AI applications, a one-size-fits-all approach simply won't cut it. Regulations need to be customized for specific industries, like finance and healthcare, to tackle their unique risks and ethical challenges.

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Surden, H. (2020). Artificial Intelligence and Corporate Governance. *University of Miami Law Review*, 74(4), 1011–1054.

This article examines the possibility of AI being integrated into corporate decision-making, the legal recognition of AI as directors, and the potential issues of accountability, fiduciary duty, and liability. It also explores the feasibility of AI in governance structures compared to human directors.