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# CONTRACTUAL POWER AND CORPORATE DUTY: GOVERNING DOWNSIDE PROTECTIONS AND BOARD-LEVEL CONFLICTS IN PRIVATE EQUITY

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## ABSTRACT

Private equity investors in India use contractual safeguards to reduce the risk of losing their money especially when investors own only a share of a company. These safeguards include liquidation preferences, anti-dilution rights, veto rights for decisions the right to appoint directors and exit rights such as put options and drag-along rights. Even though these rights come from agreements the company's directors must still follow the legal duties set out in the Companies Act 2013. The main issue is where an investor's contractual rights end and a director's legal responsibilities begin. Indian law has set rules for enforcing investor rights. These rules require looking at the company's articles of association foreign investment rules under FEMA and other company law requirements. However, the role of a nominee director remains a concern. A nominee director is chosen to represent the investor's interests. The nominee director must also carry out the duties that all directors owe under Section 166 of the Companies Act 2013. This can lead to conflicts especially when the investor's interests do not match the company's interests. The problem gets worse when a company is in trouble. Investor veto rights can then slow decisions and raise questions about possible liability under the Insolvency and Bankruptcy Code 2016. Indian cases, like the Tata–Mistry litigation along with approaches from Delaware and the United Kingdom can show possible solutions. These solutions include rules on conflicts that involve nominee directors, better alignment between shareholders' agreements and the articles of association, procedures that let directors' step back from conflicted decisions safeguards that control access to confidential information and clearer drafting of investor veto rights and exceptions when a company is, in distress.

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## 1. INTRODUCTION

Private equity is now a way for Indian businesses to get growth capital. Of buying a whole company, a fund usually takes a small part of the company using equity shares or mandatory convertible preference shares or convertible debentures. Then the fund puts money into a business that is managed by the people who started it hoping that the business will grow. Foreign investors need to follow Indias rules about money moving out of the country including the Foreign Exchange Management (Non-debt Instruments) Rules from 2019 as amended. Investment funds from within the country that collect money from people can work as Alternative Investment Funds, called AIFs under the SEBI (Alternative Investment Funds) Regulations, from 2012 as amended. Recent data highlights the scale of this market. Bain & Company's India Private Equity Report 2026 estimates that India's PE-VC investments fell by about 17% to US$36 billion in 2025, although deal volume increased by around 10%. [2] Also, the EY-IVCA report recorded US$20.5 billion in PE-VC investments across 604 deals in the first half of 2026, a 36% fall in investment value compared with the first half of 2025.[3] These figures show why the private equity market remains important to Indian businesses and why its legal framework deserves careful study.

A minority investor writes a large cheque but holds little day-to-day control. That mismatch explains why investors negotiate so hard. Before investing they run due diligence, and after investing they rely on contracts: liquidation preferences for the downside, anti-dilution protection against later cheap issues, veto rights over important decisions, board seats, and exit rights such as put options and drag-along clauses.[4]These terms are not peculiar to India. Empirical work on venture capital contracts shows the same pattern of staged financing, control rights and exit protections across markets.

### 1.1 Meaning and Purpose of Contractual Downside Protections

[2]Bain & Co. & Indian Venture & Alternate Cap. Ass'n, *India Private Equity Report 2026* (2026).
[3]EY & Indian Venture & Alternate Cap. Ass'n, *PE/VC Investments in India Reach US$20.5 Billion Across 604 Deals in 1H2026* (July 31, 2026).
[4] Steven N Kaplan and Per Strömberg, 'Financial Contracting Theory Meets the Real World: An Empirical Analysis of Venture Capital Contracts' (2003) 70 *Review of Economic Studies* 281.


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A downside protection is a contractual right that helps an investor reduce potential losses or gain some control when a business performs poorly. These clauses address several common risks.

- **Information asymmetry:** The promoter usually knows more about the business than the investor. Economists have long shown that when one side knows more, the other side prices in the risk or builds in safeguards.[5]Veto rights over related-party transactions and access to company information can help reduce this gap.
- **Valuation uncertainty:** It is difficult to value young, unlisted companies, so the initial investment price may later prove inaccurate. Anti-dilution rights and ratchets allow the parties to adjust the investor's financial position if the company performs below expectations.
- **Minority ownership:** A fund holding 15 or 25 per cent of a company may not have enough votes to outvote the promoter. Reserved-matter and board-nomination rights give the investor a say in important decisions that could affect its investment, such as issuing new shares, changing the articles of association, taking on large borrowings or selling major assets.

In short, these clauses help investors protect their money and influence important decisions in businesses they do not directly manage. The difficulty arises when that influence conflicts with a director's duty to the company.

### 1.2 The Core Tension: Investor Rights vs. Directors' Statutory Duties

Investor rights in equity transactions are usually set up through agreements made in contracts. On the hand directors' responsibilities come from company law. This can lead to a problem where the protections that an investor tries to get do not match the duties that a director has to the company.

The Companies Act 2013 gives duties to every director, no matter who put them in the position. Section 166(2) says a director must act honestly and work to help the company's goals so that all the members of the company benefit. The director must also act in the interests of the company, its workers, owners, the local area and the environment. Section 166(3) says the director must use care, skill and effort and must make decisions on their own.

[5]Ronald J Gilson, 'Engineering a Venture Capital Market: Lessons from the American Experience' (2003) 55 Stanford Law Review 1067.



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Section 166(4) stops a director from being in a situation where their own interests could clash with the company's interests.[6] These duties are important, in equity transactions because the interests of an investor might not always match the long-term needs of the company.

The conflict becomes very clear when a private equity fund puts a nominee director on the board of the company, they have invested in. The fund expects the director to protect their investment. The law says the director must make decisions on their own and act in the company's interest. English law has understood this difference for a time. A director still has duties to the company even if a shareholder put them on the board.[7] The same issue has arisen in Delaware, particularly where preferred shareholders' financial interests differ from those of ordinary shareholders. In In re Trados Inc. Shareholder Litigation, the Delaware Court of Chancery examined a transaction in which preferred shareholders received the benefit of their liquidation preference while ordinary shareholders received nothing.[8] This case illustrates how the allocation of financial benefits among different classes of shareholders can raise questions about directors' fiduciary duties. India has no comparable decision tackling this squarely, and the Act does not distinguish nominee from other directors.

Another challenge is whether the protections in contracts can be enforced. Private equity investors often get voting rights; special matters they can decide on the right to choose board members and other protections through agreements between shareholders. Just because there is a contract does not mean it can change the rules in the Companies Act or the company's articles. In a case called V.B. Rangaraj v. V.B. Gopalakrishnan, the Supreme Court said that rules about selling shares that're not in the articles can't be used against the company or the shareholders in that situation.[9] Later decisions like Messer Holdings Ltd. V. Shyam Madanmohan Ruia, looked at how agreements between shareholders the articles and the law work.[10] The Supreme Court's decision in the Tata–Mistry case also shows how important the articles of association and the right to vote are in disputes at the board level. [11] These authorities should not, however, be read as establishing that every provision in a shareholders' agreement is automatically unenforceable unless reproduced in the articles;

[6]Companies Act, No. 18 of 2013, § 166(2)– (4) (India).
[7]*Kuwait Asia Bank EC v. Nat'l Mut. Life Nominees Ltd*. [1991] 1 AC 187 (PC) (appeal taken from N.Z.); *Hawkes v. Cuddy* [2009] EWCA (Civ) 291 (Eng.).
[8]*In re Trados Inc. S'holder Litig*., 73 A.3d 17 (Del. Ch. 2013).
[9]*V.B. Rangaraj v. V.B. Gopalakrishnan*, (1992) 1 SCC 160 (India).
[10]*Messer Holdings Ltd. v. Shyam Madanmohan Ruia*, (2010) 5 Bom. C.R. 589, 2010 SCC OnLine Bom 1178 (Bom.) (India).
[11]*Tata Consultancy Servs. Ltd. v. Cyrus Invs. Pvt. Ltd*., (2021) 9 SCC 449 (India).


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enforceability depends on the nature of the right, the agreement, the articles and the applicable statutory framework. [12]

Financial distress can intensify these conflicts. Investor protections may delay emergency financing, restructuring or rescue efforts, while nominee directors may face scrutiny over their knowledge, decisions and duties to the company. Insolvency laws may also apply where transactions are alleged to be avoidable, fraudulent or wrongful.[13] The main question is not just if the investors protection in a contract is allowed. It is also, about how that protection can be used without making the director break the law.

## 2. UNDERSTANDING DOWNSIDE PROTECTIONS IN PRIVATE EQUITY

Most private equity (PE) investments in India are not plain purchases of equity. A fund typically subscribes to compulsorily convertible preference shares (CCPS) or compulsorily convertible debentures (CCDs), securities that carry a priority claim now and convert into equity later.[14]This structure is partly a product of foreign exchange rules, which treat instruments that are not fully and mandatorily convertible as debt, and partly a matter of commercial design: preference rights are easier to attach to preference shares than to ordinary shares.[15] Under the Companies Act, 2013, preference shares carry a priority claim on dividend and capital, but they are redeemable within a fixed period and generally vote only on matters that directly affect them.[16]That structure explains the purpose of downside protections. The investor holds a minority stake, knows less than the promoter, and cannot easily price a growing company. Rather than rely on trust alone, it negotiates rights that fall into three families: economic, control and exit.

### 2.1 Major Forms of Contractual Investor Protection

- **Economic protections:**A liquidation preference allows an investor to get its investment back, usually with an agreed return, before other shareholders when the company is sold

[12]Arjya B. Majumdar, *The Enforceability of Investor Rights in Indian Private Equity*, IndiaCorpLaw (May 28, 2019), https://indiacorplaw.in/2019/05/28/enforceability-investor-rights-indian-private-equity/
[13] Insolvency and Bankruptcy Code, 2016, §§ 43, 45, 66, No. 31 of 2016, Acts of Parliament, 2016 (India); Nishith Desai Assocs., *Safeguarding Nominee Director's Interest in Private Equity Investments: Avoidable Transactions Under the Insolvency Code* (July 10, 2023), https://nishithdesai.com/research-and-articles/hotline/private-equity-corner/safeguarding-nominee-directors-interest-in-private-equity-investments-avoidable-transactions-under-the-insolvency-code-10664.
[14] Kaplan & Strömberg, Supra Note 3
[15]Foreign Exchange Management (Non-Debt Instruments) Rules, 2019, Rule 2(k), Gazette of India, pt. II, sec. 3(ii) (Oct. 17, 2019) (India).
[16]Companies Act, 2013, §§ 43, 47, 55.


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or wound up. Under a non-participating preference, the investor chooses between receiving the preference amount or its share of the sale proceeds. Under a participating preference, it receives the preference amount first and then shares in the remaining proceeds. Anti-dilution protection adjusts the investor's conversion price if the company later issues shares at a lower price. A broad-based weighted average formula softens the adjustment, while a full ratchet resets the price entirely to the lower level.[17] Valuation ratchets are linked to the company's performance and may give the investor additional shares if agreed targets are not met.

- **Control rights and board oversight:**Investor veto rights require prior approval for major decisions, such as issuing shares, amending constitutional documents, incurring substantial debt, selling significant assets, or changing the business's nature. Board nomination rights allow investors to appoint directors or observers, sometimes making their presence necessary for valid board meetings. These rights enable investors to influence key corporate decisions even with a minority stake.
- **Exit and liquidity mechanisms:**Drag-along rights allow an investor to force other shareholders to sell their shares when the company is sold. Tag-along rights protect minority shareholders by allowing them to sell their shares on the same terms. Put options allow investors to require the promoter or company to buy their shares, while call options allow the buyer to purchase shares under agreed terms. Redemption rights require the company to buy back its securities. These exit rights are subject to strict regulations, particularly for foreign investors, including pricing rules, lock-in requirements and restrictions on guaranteed returns.

These protections serve commercial purposes but carry specific legal limits. Economic protections, such as liquidation preferences, prioritise investors in a sale or winding up but rank below creditors in insolvency. Anti-dilution clauses and ratchets protect against dilution but are subject to FEMA pricing and conversion rules for non-resident investors.

Control rights, including reserved matters and investor vetoes, can restrict board decisions, with enforceability depending on their inclusion in the articles. Nominee directors provide investors with influence and information but remain bound by Section 166 duties to the company, creating potential conflicts of loyalty and liability.

[17]Brad Feld & Jason Mendelson, *Venture Deals: Be Smarter Than Your Lawyer and Venture Capitalist* (4th ed. 2019).



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Exit rights facilitate share sales but are also regulated. Drag-along rights enable collective sales, while tag-along rights protect minority shareholders; both may require inclusion in the articles to bind the company. Put options, call options and redemption rights provide exit routes but may strain company finances and are subject to FEMA, SEBI and Section 55 of the Companies Act, 2013.

### 2.2 Shareholders' Agreements vs. Articles of Association

Most of these protections begin life in a shareholders' agreement (a private contract among the investor, the promoters and the company). Their legal strength, however, often depends on whether they also appear in the company's articles of association (AoA). The articles bind the company and its members under Section 10 of the Companies Act, 2013.[18]In practice, deal lawyers therefore draft the SHA and then amend the articles to mirror its key terms, with shareholders approving the changes by special resolution.[19]

Two statutory points help in this situation Section 5 permits entrenchment provisions, which allow certain articles to be changed only on conditions stricter than a special resolution, and which fit the logic of investor vetoes.[20] And Section 58(2) provides that contracts between persons on transfer of securities are enforceable as contracts even in a public company.[21]Even so, incorporation does not cure everything. A clause in the articles cannot override the Act, and a clause left only in the SHA may bind the parties without binding the company, as the next chapters examine.

## 3. THE INDIAN LEGAL FRAMEWORK GOVERNING INVESTOR RIGHTS AND DIRECTORS' DUTIES

### 3.1 Statutory Framework: Overriding Provisions, Articles of Association and Shareholder Rights

The Companies Act, 2013 is the starting point for resolving conflicts between investor rights and directors' duties. Section 6 states that the Act overrides anything inconsistent with it in the company's memorandum, articles, agreements or resolutions, unless the Act provides

[18]Companies Act, 2013, § 10.
[19]Id. § 14.
[20]Id. § 5(3) – (5)
[21] Id. § 58(2)


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otherwise.[22]Therefore, a shareholders' agreement cannot override a statutory duty simply because the parties have agreed to it.

The Act also provides ways to protect investors. Section 43 recognises equity and preference shares, with preference shares carrying priority in dividend payments and repayment of capital during winding up.This provides the legal basis for liquidation preferences. However, Section 55 requires preference shares to be redeemable within the prescribed period, while Section 47 limits their voting rights to specified matters, including those directly affecting their rights.[23]

Sections 10 and 166(1) explain the relationship between the company's articles and its directors. Under Section 10, the articles bind the company and its members, while Section 166(1) requires directors to act in accordance with them.[24]A right included only in a shareholders' agreement generally binds its parties but does not automatically have the same effect as a provision in the articles. Section 58(2), however, recognises that contracts between persons concerning the transfer of securities are enforceable as contracts, subject to the Companies Act.[25]This makes the position on transfer restrictions more nuanced, than the earlier view that transfer restrictions must always be included in the articles.

### 3.2 Directors' Duties under Section 166 of Companies Act, 2013

Section 166 of the Companies Act, 2013 sets out the duties of every director. Under Section 166(2), directors must act in good faith and in the best interests of the company, its members and other stakeholders, including employees, the community and the environment. Section 166(3) requires them to exercise reasonable care, skill, diligence and independent judgment. Section 166(4) prohibits conflicts between a director's personal interests and those of the company. Section 166(5) prohibits undue personal gain, while Section 166(7) provides a penalty for contravention.[32][26]

Indian courts have also recognised that directors must use their powers for proper purposes and must not misuse them to favour particular shareholders or protect their own

[22]Id. § 6.
[23] Id. §§ 43, 47, 55.
[24] Id. §§ 10, 166(1).
[25]Id. § 58(2); *Rangaraj*, (1992) 1 S.C.C.
[26]Id. § 166(2)–(5), (7).


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positions.[27][33] The Act applies these duties equally to all directors, including those nominated by investors. Although a nominee director may consider the investor's interests, they must exercise their own judgment and act in accordance with their duties to the company. These principles provide the legal basis for examining the investor protections discussed in the previous chapter.

### 3.3 Conflict Safeguards and Minority Remedies

The Companies Act, 2013 provides safeguards to manage conflicts of interest. Under Section 184, directors must disclose any direct or indirect interest in a contract or arrangement with the company and, where required, abstain from participating in the discussion.Section 188 requires board approval for specified related-party transactions and shareholder approval for transactions exceeding prescribed limits. The related party must not vote on the relevant resolution. However, transactions conducted in the ordinary course of business and at arm's length are generally exempt from these approval requirements.[28]

These provisions are important for private equity-backed companies when the investor, its affiliates or other portfolio companies enter into transactions with the investee company, such as management agreements, supply contracts or loans. Whether the investor or its nominee director qualifies as a related party under Section 2(76) depends on the circumstances and must be examined carefully.

If these safeguards fail, Sections 241 and 242 allow eligible members to approach the National Company Law Tribunal (NCLT) when the company's affairs are conducted oppressively or in a manner prejudicial to the company or its members. The Tribunal may order appropriate relief, including regulating the company's affairs.[29]Section 244 sets out the eligibility requirements for bringing such a petition. Both promoters and investors may seek this remedy, including minority investors whose rights have been unfairly undermined. However, ordinary disagreements over business decisions do not automatically amount to oppression. The Supreme Court's decision in the Tata–Mistry litigation, which set aside the

[27]*Needle Indus. (India) Ltd. v. Needle Indus. Newey (India) Holding Ltd.*, (1981) 3 SCC 333 ;*Dale & Carrington Inv. Pvt. Ltd. v. P.K. Prathapan*, (2005) 1 SCC 212
[28]Companies Act, 2013, §§ 2(76), 184, 188
[29] Id. §§ 241–244.


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NCLAT's ruling in favour of Cyrus Mistry, illustrates the courts' cautious approach to such claims.[30]

### 3.4 Regulatory Framework: FEMA and SEBI

Company law is only one part of the legal framework governing private equity investments. Foreign investors must also comply with the Foreign Exchange Management Act, 1999 (FEMA) and the Foreign Exchange Management (Non-debt Instruments) Rules, 2019. These rules regulate pricing when shares are issued to or transferred between residents and non-residents. In general, a foreign investor cannot be guaranteed an assured exit price and must comply with the applicable pricing requirements when exiting the investment. This can create difficulties for liquidation preferences and put options that promise a fixed return. Such exitoptions are permitted only subject to the applicable conditions, including restrictions on assured returns and lock-in requirements, where applicable.[31]

A separate regulatory framework applies to companies that are listed or planning to go public. SEBI's Listing Obligations and Disclosure Requirements Regulations, 2015, as amended, regulate special rights granted to shareholders, including certain nomination and voting rights. Some rights require shareholder approval by special resolution at prescribed intervals. The SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018 also regulate aspects of a company's capital structure when it issues securities to the public.[32]Therefore, private equity investors should consider whether their negotiated veto rights and other special protections can continue after listing, as some may need approval, modification or termination under the applicable rules.

## 4. CONTRACTUAL FREEDOM AND ENFORCEABILITY OF DOWNSIDE PROTECTIONS

Private equity investors negotiate contractual protections to reduce their risks. However, a company is a separate legal entity governed by the Companies Act and its articles of

[30]*Tata Consultancy Servs. Ltd. v. Cyrus Invs. Pvt. Ltd*., (2021) 9 SCC 449.
[31]Foreign Exchange Management Act, No. 42 of 1999, § 6 (India); Foreign Exchange Management (Non-Debt Instruments) Rules, 2019, rr. 9, 21 (India); Parag Bhide & Mitali Kshatriya, Ensuring Liquidation Preference to Protect Investor Rights, Bharucha & Partners (Feb. 7, 2024), https://www.bharucha.in/ensuring-liquidation-preference-to-protect-investor-rights/
[32]Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015, regs. 31B, 30(6), sched. III, pt. A, para. 5, Gazette of India, Extraordinary, pt. III, sec. 4 (Sept. 2, 2015) (India), as amended; Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018, sched. VI (India), as amended.


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association. Therefore, an agreement between shareholders does not automatically bind the company. The key question is how far Indian law allows shareholders to decide how a company is governed and where the law sets limits. This requires examining the relationship between shareholders' agreements and the articles of association, whether investors can use voting rights to influence board decisions without interfering with the board's legal duties, and what remedies are available when a clause is not included in the articles, conflicts with the law, or is misused.

### 4.1 Contractual Freedom and Its Legal Limits

Private equity investors and promoters are generally free to negotiate the terms of their investment. However, a company is a separate legal entity, and its internal affairs are governed by the Companies Act, 2013 and its articles of association.[33] Therefore, the key question is not simply whether a clause is valid between the parties who signed the agreement, but whether it can also be enforced against the company.

In V.B. Rangaraj v. V.B. Gopalakrishnan, the Supreme Court held that a restriction on share transfers that was not included in the articles could not be enforced in the circumstances of that case.[34]Later decisions took different approaches to the relationship between shareholders' agreements and the articles. In Messer Holdings Ltd. v. Shyam Madanmohan Ruia, the Bombay High Court considered the contractual rights of shareholders, while in World Phone India Pvt. Ltd. v. WPI Group Inc., the Delhi High Court refused to enforce an affirmative-voting right that had not been incorporated into the articles.[35]

The Companies Act, 2013 provides further guidance. Section 58(2) recognises that agreements between persons concerning the transfer of securities can be enforced as contracts, subject to the Act. Sections 5 and 14 also allow companies to include investor protections in their articles, subject to statutory requirements.[36] Legal commentary on private equity in India highlights that provisions such as special quorum requirements and affirmative voting rights may be recognised when properly included in the articles, although

[33]*Salomon v. A. Salomon & Co.*, [1897] A.C. 22 (H.L.) (appeal taken from Eng.); Companies Act, No. 18 of 2013, §§ 10, 166.
[34]*V.B. Rangaraj v. V.B. Gopalakrishnan*, (1992) 1 S.C.C. 160
[35]*Messer Holdings Ltd. v. Shyam Madanmohan Ruia*, (2010) 5 Bom. C.R. 589, 2010 SCC OnLine Bom 1178]; *World Phone India Pvt. Ltd. v. WPI Group Inc.*, (2013) 178 Comp. Cas. 173 (Del.).
[36]Companies Act, No. 18 of 2013, §§ 5, 14, 58(2) .


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the enforceability of other contractual protections can depend on the circumstances.[37] For this reason, investors commonly include important protections in both the shareholders' agreement and the articles.

### 4.2 Investor Veto Rights and the Board's Powers

Investor veto rights allow an investor to approve or block certain important company decisions. Their enforceability is generally stronger when they are properly included in the articles, which bind the company and its members. The Tata–Mistry dispute illustrates the importance of these provisions. The Supreme Court examined the affirmative-voting rights in Tata Sons' articles when considering the allegations of oppression and mismanagement.[38]

However, investor veto rights must operate within the limits of company law. Section 179(1) gives the board authority to exercise the company's powers, subject to the Act, the memorandum, the articles and matters reserved for the general meeting. Section 180 requires a special resolution for specified decisions, including certain sales of undertakings and borrowings beyond prescribed limits.[39] A veto right may restrict how a decision is made, but it cannot override mandatory legal requirements.

Two important limits follow. First, a nominee director cannot blindly follow the investor's instructions if doing so would conflict with the director's statutory duties under Section 166. Second, a veto cannot override the Companies Act, which prevails over inconsistent provisions under Section 6. A veto over a major asset sale may be a legitimate investor protection, but a clause that prevents the company from complying with the law or responding to a serious crisis may be difficult to enforce. English law recognises a similar distinction: shareholders may agree how they will exercise their voting rights, but a company cannot contract away its statutory powers.[40]

### 4.3 Consequences of Invalid or Improperly Used Clauses

A contractual protection that is missing from the articles or conflicts with the Companies Act is not necessarily worthless. It may still be enforceable against the parties who signed the agreement. If a party breaches it, the investor may claim damages under Section 73 of the

[37] Majumdar, *supra* note 11.
[38] *Tata Consultancy Servs. Ltd. v. Cyrus Invs. Pvt. Ltd.*, (2021) 9 S.C.C. 449
[39] Companies Act, No. 18 of 2013, §§ 179(1), 180(1).
[40] *Russell v. N. Bank Dev. Corp. Ltd.*, [1992] 1 W.L.R. 588 (H.L.) (appeal taken from N. Ir.).


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Indian Contract Act, 1872, or seek specific performance or an injunction where the requirements of the Specific Relief Act, 1963 are met.[41]The availability of these remedies depends on the terms of the agreement and the circumstances of the breach.

However, enforcing a contractual right against a promoter is different from enforcing it against the company. A breach of a shareholders' agreement does not automatically invalidate a corporate decision or make it unenforceable against third parties. Where the protection is also included in the articles, a breach may raise issues concerning compliance with the company's constitution and may support a claim for appropriate relief.

In serious cases, eligible members may approach the National Company Law Tribunal under Sections 241 and 242 if the company's affairs are conducted oppressively or in a manner prejudicial to the company or its members.[42]Such statutory proceedings are generally not suitable for resolution through arbitration, although separate contractual disputes may still be arbitrable depending on their nature.

Investor rights must also be exercised fairly. A veto used to obtain an improper personal advantage or unnecessarily delay an urgent rescue may invite legal challenge. The practical approach is to include key protections in the articles as well as the shareholders' agreement, preserve appropriate contractual remedies, and consider carefully drafted exceptions for financial distress. These measures can protect investors without unnecessarily restricting the company's ability to operate or recover from difficulties.

## 5. BOARD-LEVEL CONFLICTS: BALANCING INVESTOR PROTECTION AND CORPORATE DECISION-MAKING

Board-level conflicts in equity happen when a fund's return relies on a choice that is not clearly best for the company for example a rescue financing, an exit or a veto. A nominee director's legal duties under Section 166 are put to the test in those moments and the risk for both the director and the fund rises sharply when the company is, in distress.

### 5.1 Divergenceof Investor Interest and Corporate Welfare

[41]Indian Contract Act, No. 9 of 1872, § 73 (India); Specific Relief Act, No. 47 of 1963, §§ 10, 14, 16 (India).
[42]Companies Act, No. 18 of 2013, §§ 241–242 (India); *Vidya Drolia v. Durga Trading Corp.*, (2021) 2 S.C.C. 1,*see also Rakesh Malhotra v. Rajinder Malhotra*, 2014 SCC OnLine Bom 1146 (India).


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Board-level conflicts arise when an investor's financial interests may not align with the company's interests. Common examples include decisions on funding rounds, company sales, rescue financing, related-party transactions and investor vetoes. While PE funds seek returns within a limited investment period, companies may need to prioritise long-term growth and survival.

Nominee directors must exercise independent judgment despite being appointed by investors. Section 166(2)– (4) of the Companies Act, 2013 requires directors to act in good faith, protect the company's interests and avoid conflicts of interest.English courts have similarly recognised that nominee directors owe duties to the company, not merely to the investor who appointed them.[43]Therefore, each decision must be independently assessed in light of the company's interests.

### 5.2 Information Sharing and Recusal

A nominee director may report to the PE fund, but must also protect the company's confidential information. The Companies Act, 2013 does not set out a specific rule for sharing board information with the appointing investor. Any sharing should therefore be consistent with the director's duties and the company's confidentiality arrangements. For listed companies, SEBI's insider-trading rules further restrict the sharing of unpublished price-sensitive information, allowing it only in permitted circumstances.[44]Conflicts also arise when the fund or its affiliate transacts with the company. Section 184 requires disclosure of specified interests and restricts participation in relevant board discussions, while Section 188 regulates related-party transactions.[45]As these provisions may not cover every conflict involving an investor's wider interests, investment documents should establish clear disclosure and recusal procedures.

### 5.3 Illustrative Conflict Scenarios

- **Investor veto during a crisis:** Suppose a company needs emergency financing, but the investor vetoes the proposal to protect its preferential repayment rights. The Companies Act regulates board borrowing powers and certain borrowing decisions requiring

[43]*Kuwait Asia Bank E.C. v. National Mutual Life Nominees Ltd*., [1991] 1 A.C. 187 (P.C.); *Hawkes v. Cuddy [2009] EWCA (Civ) 291 (Eng.).*
[44]Companies Act, No. 18 of 2013, § 166(2)– (3) (India); Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 2015, reg. 3(1), 3(2), 3(5C) (India)
[45]Companies Act, No. 18 of 2013, §§ 184, 188 (India)


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shareholder approval; it does not automatically validate every investor veto.[46] A nominee who supports a veto without considering the company's financial position risks breaching the duty to exercise independent judgment. In serious cases, affected members may also seek relief for oppression or mismanagement.[47]

- **Investor-led exit.:**A PE fund nearing the end of its investment period may seek to force a sale under a drag-along clause, even when other shareholders believe the company is undervalued. In In re Trados Inc. Shareholder Litigation, the Delaware court examined a sale that favoured preferred shareholders while common shareholders received nothing.[48] Although the decision is not binding in India, it illustrates why contractual exit rights should not replace proper consideration of conflicts and directors' duties.

### 5.4 Distress and Liability Exposure

A nominee director's responsibilities become especially important when the company approaches insolvency. Section 66(2) of the Insolvency and Bankruptcy Code, 2016 allows the adjudicating authority to impose personal contribution liability where a director knew or ought to have known that insolvency could not reasonably be avoided and failed to take due diligence steps to minimise creditor losses. Sections 43 and 45 address preferential and undervalued transactions, respectively.[49]PE investors may also face exposure if their involvement goes beyond ordinary investor protections. Under Section 2(60)(v) of the Companies Act, a person whose directions or instructions the board is accustomed to follow may qualify as an "officer who is in default," subject to the statutory exception for advice given in a professional capacity.[50] The distinction is between exercising negotiated rights, such as reserved-matter vetoes, and directing the company's day-to-day decisions.

## 6. JUDICIAL APPROACH AND CRITICAL ANALYSIS

### 6.1 From Formal Rules to Greater Contractual Flexibility

Indian courts have taken different approaches to enforcing shareholders' agreements (SHAs). In V.B. Rangaraj v. V.B. Gopalakrishnan, the Supreme Court held that a share-transfer restriction not included in the articles of association could not be enforced in the

[46]Id. §§ 179(1), 180(1)(c).
[47]Id. §§ 241–242.
[48]*In re Trados Inc. S'holder Litig*., 73 A.3d 17 (Del. Ch. 2013).
[49]Insolvency and Bankruptcy Code, No. 31 of 2016, §§ 43, 45, 66(2).
[50]Companies Act, No. 18 of 2013, § 2(60)(v).


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circumstances of that case.[51]This raised concerns about investor protections contained only in private agreements.The Delhi High Court's decision in World Phone India Pvt. Ltd. v. WPI Group Inc. is also discussed in this context.[52] As a result, investors often sought to include important rights, such as vetoes and special voting arrangements, in the articles as well as the SHA.

Later decisions adopted a more flexible approach to agreements between shareholders. In Messer Holdings Ltd. v. Shyam Madanmohan Ruia, the Bombay High Court considered the enforceability of arrangements between shareholders. [53]Vodafone International Holdings B.V. v. Union of India is also discussed in relation to shareholder agreements, but its observations should not be treated as a direct ruling on the enforceability of investor vetoes.[54]These decisions do not establish one rule for every investor protection. Enforceability depends on the nature of the right, the wording of the articles and whether enforcement is sought against the company or another party to the agreement.[55]

### 6.2 Directors' Duties, Board Independence and the Tata–Mistry Decision

The Supreme Court's decision in Tata Consultancy Services Ltd. v. Cyrus Investments Pvt. Ltd. is important to understanding investor rights and minority protection. The Court set aside the NCLAT's order granting relief for oppression and mismanagement. It emphasised that a shareholder's disappointment or loss of influence does not, by itself, establish oppression under Sections 241–242 of the Companies Act, 2013.[56] However, the decision does not validate every investor veto; the outcome depends on the relevant articles and facts.

Other decisions, including Needle Industries and Dale & Carrington, show that directors must exercise their powers for proper purposes and cannot misuse them to strengthen their own control.[57] Although these cases do not directly address PE nominee directors, they reinforce the importance of independent decision-making. English authority also supports the principle

[51]*V.B. Rangaraj v. V.B. Gopalakrishnan*, (1992) 1 SCC 160.
[52]*World Phone India Pvt. Ltd. v. WPI Group Inc*., (2013) 178 Comp. Cas. 173 (Del.)
[53]*Messer Holdings Ltd. v. Shyam Madanmohan Ruia*, (2016) 11 SCC 484.
[54]*Vodafone International Holdings B.V. v. Union of India*, (2012) 6 SCC 613.
[55]Majumdar, *supra* note 11.

[56]*Tata Consultancy Services Ltd. v. Cyrus Investments Pvt. Ltd*., (2021) 9 SCC 449
[57]*Needle Industries (India) Ltd. v. Needle Industries Newey (India) Holding Ltd.*, (1981) 3 SCC 333*; Dale & Carrington Investment (P) Ltd. v. P.K. Prathapan*, (2005) 1 SCC 212.


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that a nominee director owes duties to the company rather than solely to the appointing investor.[58]

### 6.3 Critical Appraisal

Three issues remain unresolved. First, Indian case law has not clearly established how a nominee director should respond when the fund's instructions conflict with the company's interests. Section 166 applies to directors generally, but there is limited direct guidance on this specific situation.[59]

Second, the enforceability of shareholders' agreements remains dependent on the right involved, the articles and the parties against whom enforcement is sought. Investors should therefore ensure that important protections are properly reflected in the company's constitutional documents where necessary.

Third, remedies may be fragmented. Contractual disputes may be referred to arbitration, while oppression and mismanagement claims fall within the statutory framework of Sections 241–242. Whether a particular dispute is arbitrable depends on its nature and the applicable law; Vidya Drolia v. Durga Trading Corp. provides the general test for determining arbitrability.[60]

## 7. COMPARATIVE PERSPECTIVES AND REGULATORY IMPLICATIONS

### 7.1 Delaware and the United Kingdom

Delaware and the United Kingdom offer useful comparisons for India's approach to PE investor rights and nominee directors. In Delaware, directors owe fiduciary duties to the corporation even when they are appointed by particular investors. In Weinberger v. UOP, Inc. and In re Trados Inc. Shareholder Litigation, courts examined conflicts involving directors and preferred shareholders. In Trados, the court applied the entire-fairness standard to a merger that left common shareholders with nothing, but found no liability because the common shares had no economic value.[61]

[58] *Kuwait Asia Bank E.C. v. National Mutual Life Nominees Ltd.*, [1991] 1 A.C. 187 (P.C.) (appeal taken from N.Z.).
[59] Lakshita Mohan, *Nominee Director Crisis Indian Law Refuses To Confront*, LiveLaw (July 19, 2026), https://www.livelaw.in/articles/nominee-director-crisis-indian-law-refuses-confront-541760.
[60] *Vidya Drolia*, (2021) 2 SCC 1
[61] *Weinberger v. UOP, Inc.*, 457 A.2d 701, 710 (Del. 1983).


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Delaware has also addressed the tension between investor agreements and board powers. In West Palm Beach Firefighters' Pension Fund v. Moelis & Co., the court found that certain contractual approval rights improperly restricted the board's statutory authority. Delaware subsequently amended its General Corporation Law to expressly permit specified governance agreements, subject to statutory limits.[62]This shows how legislation can clarify investor rights rather than leaving their validity to uncertain case-by-case decisions.

The United Kingdom takes a more direct statutory approach. The Companies Act 2006 requires directors to promote the company's success, exercise independent judgment, avoid conflicts and disclose interests in proposed transactions. These duties apply to nominee directors as well.[63]English case law also recognises that a nominee director's primary duty is to the company, not simply to the person who appointed them.[64]The UK further regulates shadow directors and provides for wrongful-trading liability in insolvency, helping address situations where investor exercises influence beyond its formal board rights.[65]

### 7.2 Gaps in the Indian Framework

Comparing with these systems, India faces three main gaps.

First, Section 166 of the Companies Act, 2013 applies the same duties to all directors but provides little specific guidance for nominee directors facing conflicting demands. Section 184 addresses disclosure of a director's interests, but it does not fully resolve conflicts arising from the relationship between a fund and its nominee.

Second, the enforceability of investor rights remains uncertain. Unlike Delaware, which introduced an express statutory provision for certain governance agreements, India relies heavily on the wording of the articles and the circumstances of each case. This can make it difficult for investors and boards to know whether a particular veto or approval right will be enforceable.

Third, Indian law could provide clearer guidance on information-sharing and the point at which a fund's influence becomes sufficient to attract responsibility for the company's

[62]*In re Trados Inc. S'holder Litig*., 73 A.3d 17 (Del. Ch. 2013).
[63]*Kalisman v. Friedman*, C.A. No. 8447-VCL, 2013 WL 1668205 (Del. Ch. Apr. 17, 2013).
[64]*West Palm Beach Firefighters' Pension Fund v. Moelis & Co*., 311 A.3d 809 (Del. Ch. 2024); Del. Code Ann. tit. 8, §§ 122(18), 141(a) (2025).
[65]Elizabeth Pollman, Startup Governance, 168 U. Pa. L. Rev. 155 (2019); Jesse M. Fried & Mira Ganor, Agency Costs of Venture Capitalist Control in Startups, 81 N.Y.U. L. Rev. 967 (2006)


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decisions. Clearer rules would help protect investors while preserving directors' duties and creditors' interests.

## 8. RECOMMENDATIONS

India should clarify the legal position of nominee directors. Section 166 could expressly state that nominee directors owe the same duties as other directors, may consider the appointing investor's views where appropriate, but must exercise independent judgment. A clear procedure for authorising conflicts, with safeguards for unconflicted decision-making, would also help boards manage difficult situations.

The law should also clarify when a shareholders' agreement can bind the company. Delaware's approach under Section 122(18) of its General Corporation Law offers one possible model: recognise specified contractual governance rights while preventing agreements from overriding mandatory legal requirements.[66] Any Indian reform should protect minority shareholders and creditors and account for the additional rules applicable to listed companies.

Finally, clearer guidance is needed on when a PE fund's influence may expose it to liability for the company's decisions, particularly during financial distress. This would help distinguish legitimate investor oversight from taking effective control of the company.[67]

Until the law changes, companies can reduce risk through better board procedures and clearer investment documents. Boards should adopt written conflict policies, require disclosure of relevant interests and use independent directors to review transactions involving the fund or its affiliates. Agreements should also specify what board information can be shared with the investor and for what purpose. Recording the reasons for important decisions can help demonstrate that directors exercised independent judgment.Reserved matters should be clearly defined, with objective financial thresholds where possible. Deadlock provisions should provide a process for resolving disagreements, while emergency financing clauses should prevent investor vetoes from unnecessarily obstructing steps needed to protect the company. Key protections should be reflected in the articles where required, with the shareholders' agreement setting out the parties' contractual rights and remedies.

[66] *Re Hydrodam (Corby) Ltd*., [1994] 2 B.C.L.C. 180 (Eng.)
[67] Paul L. Davies & Sarah Worthington, *Gower's Principles of Modern Company Law* (11th ed. 2021).


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## 9. CONCLUSION

Private equity investors rely on contracts to protect their investments, but directors remain bound by their statutory duties. These interests may align during normal business operations and diverge when a company faces a funding crisis, a related-party transaction or pressure to exit.Indian law recognises directors' duties and provides some guidance on enforcing investor rights, but the position of nominee directors remains unclear in difficult situations. Investors may have negotiated vetoes and preferential rights, yet those rights do not remove a director's obligation to exercise independent judgment. The risks become greater when the company approaches insolvency, potentially affecting both directors and investors who exercise excessive control.Clearer statutory rules, better drafting and consistent board procedures would help balance investor protection with the interests of the company, minority shareholders and creditors. Addressing these gaps would make the framework more predictable without undermining legitimate private equity investment.



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