Balancing Representation with Responsibility: The Nominee Director's Dual Allegiance Dilemma

The appointment of a Nominee Director is a common feature in Indian corporate governance, primarily seen when financial institutions, major investors (like Private Equity, Private Credit or Venture Capital funds), or the government seek to safeguard their interests in a company. While the role serves the legitimate purpose of oversight and representation, it inherently creates a conundrum: reconciling the director's statutory fiduciary duty to the company with their loyalty to the nominating entity, the Sponsor.

The law is unequivocal: once seated at the table, a nominee director's first duty is to the company and its stakeholders and not the nominating sponsor. The art of the role lies in reconciling these two realities i.e. representation and responsibility.

The legal north star: Fiduciary responsibilities of directors under Indian law

In India, directors' fiduciary duties are codified primarily in the Companies Act, 2013, that emphasize accountability to a broad range of stakeholders. Section 166 outlines these duties explicitly:

- **Duty to act in good faith and promote company objectives**: Directors must act in good faith to promote the company's objects for the benefit of its members as a whole. This includes considering the best interests of the company, its employees, shareholders, the community, and environmental protection.

- **Duty of care, skill, and diligence**: Under Section 166(3), directors are required to exercise due care, skill, and diligence, applying independent judgment. This is akin to the "business judgment rule," where decisions are protected if made reasonably and in good faith.

- **Avoiding conflicts of interest**: Section 166(4) prohibits directors from involving themselves in situations where they have a direct or indirect interest conflicting with the company's interests. They must not achieve undue gains for themselves or associates.

- **Duty of loyalty**: Directors owe a fiduciary duty of loyalty to the company, prioritizing its interests over personal or third-party gains. This is reinforced by common law precedents, though the Act does not exclude them entirely.

These duties extend to all directors, including nominees, without exception. The Act adopts a stakeholder-oriented approach, differing from shareholder primacy in some jurisdictions, by mandating consideration of wider interests like employees and the environment. Breaches can lead to penalties under Section 166(7), including fines up to INR 500,000, and potential civil liabilities.

Indian jurisprudence in Dale & Carrington Investments v. P.K. Prathapan (2004) and Tata Sons–Cyrus Mistry decision (2021), reinforces these principles. Taken together, the law and cases make it clear: a nominee director is not an agent of the sponsor within the boardroom.

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Listed businesses: SEBI's LODR considerations

For listed entities, compliance with SEBI LODR Regulations adds further nuance:

- Nominee directors do not qualify as independent if their appointment stems from a representational role tied to a promoter, major shareholder, or institution with significant influence (e.g., private equity nominees or bank-appointed representatives). This creates a direct conflict with the "no promoter/group" criterion.

- Nominees are typically classified as non-executive directors unless they hold an executive position (e.g., a sponsor's employee serving as a functional head). This classification counts toward the 50% non-executive threshold, helping companies meet composition norms. For instance, government or institutional nominees (common in PSUs) are non-executive and can serve on boards without diluting the executive/non-executive balance. However, if a nominee transitions to an executive role, reclassification is required, with disclosures in corporate governance reports

- In board committees, nominee directors who are non-executive can play a supportive role but cannot be chairperson or be counted as independent. Example in Risk Management Committee, nominees (and non-executive) can join for risk oversight aligned with sponsor interests but limited to 1/3rd slot meant for non-independent directors. Similarly, for Audit Committee, provided the nominee director is financially qualified, he/she can be counted towards non-executive, non-independent director threshold, and cannot chair or form the majority. The appointment is useful for sponsor oversight (e.g., lender nominees monitoring finances) but the nominee must recuse from conflicted matters (e.g., related-party transactions)

- Managing Unpublished Price-Sensitive Information (UPSI) is a critical responsibility for nominee directors in India, as they navigate their dual roles of representing the appointing sponsor (e.g., shareholder, lender, or institution) and upholding fiduciary duties to the company under the Companies Act, 2013, and the SEBI (Prohibition of Insider Trading) Regulations, 2015 (PIT Regulations). Nominee directors often face pressure to share boardroom insights with their sponsors, who may expect updates on company performance or strategic decisions to protect their investment or loan covenants. However, sharing UPSI without compliance, risks insider trading violations, personal liability, and reputational damage. Courts have emphasized that nominee directors are not exempt from these duties, and their allegiance lies primarily with the company. Nominee directors must understand what constitutes UPSI in board discussions and only share such information for a "legitimate purpose" such as fulfilling contractual obligations (e.g., loan covenant monitoring) or legal requirements. Nominee director can consult the company secretary and if required seek board approval for sharing such information.

Sponsor expectations

Typically, a nominee director is appointed to meet one or more of the following:

- **Monitor Performance:** Keep track of the company's financial and operational performance, especially if the Sponsor is a lender or significant investor.

- **Information Bridge:** Act as a conduit for a regular flow of information between the company and the Nominator. However, this is subject to the Nominee Director's duty of confidentiality to the company.

- **Veto Rights:** In many investment and joint venture agreements, the Nominee Director is given affirmative voting or veto rights over specific, pre-defined corporate actions (e.g., incurring new debt, major asset sales) to protect the Sponsor's investment.

- **Strategy and policy alignment**: Private Equity and Venture capital nominee directors bring strategic insights, often linked to their investment thesis. Similarly, JV / Strategic partner nominee directors require policy and reporting alignment to global / group policies. Special situation fund (turnaround funds), nominee directors keep special vigil on compliance, cash and turnaround plan implementation.

Why does the role feel so fraught?

Sponsors rightly expect their nominees to protect value: monitor performance, ensure covenants are respected, push for course-corrections, and safeguard exit pathways. But the nominee's vote is not a proxy vote. In hard moments, say a restructuring that benefits the company's survivability but defers the sponsor's exit, or a related-party contract involving the sponsor's group, the nominee must take decisions through the lens of the company's best interest, manage conflicts, and record the process.

Three practical "pressure points" recur:

- **Conflicts and recusals**: When the sponsor is counter-party (e.g., a financing amendment, security enforcement, or a commercial arrangement), the nominee should disclose interests, insist on independent evaluation (fairness opinions, external legal advice), and, where necessary, recuse.

- **Information rights and confidentiality:** Shareholder or financing documents may create information rights for sponsors; however, nominee directors cannot transmit board-confidential or UPSI beyond what is contractually permitted and consistent with the PIT Regulations and the company's legitimate-purpose policy. When in doubt, nominees must seek the Chair/Company Secretary's guidance and ensure NDAs are in place.

- **Special contexts: lenders, PE funds, and JV partners**

  - **Special Situation Fund nominees**: Such nominees often arrive during stress. Their role is to enhance oversight on compliance, cash controls, turnaround plans. They must ensure that while meeting their sponsor obligations they don't skew decisions solely to the lender's recovery at the expense of the company's viability or other stakeholders. The "company first" test applies.

  - **PE or venture nominees** bring strategy, governance muscle, and exit discipline. The line to watch is undue influence. That is, do not direct management beyond board remit or prioritise a fund's timetable over the company's medium-term interests.

- **JV/strategic partner nominees** navigate policy alignment with the global group versus local company realities (competition law, related-party norms, transfer pricing, etc.). Clear committee processes and independent reviews are indispensable.

Finding the right balance: playbook for nominee directors

- **Start with a crisp mandate but internalise the legal duty**

  Understand the sponsor's expectations (risk concerns, reporting cadence, investment thesis, exit priorities). Then explicitly recognise that Section 166 duties govern your vote and conduct. State this up front in conversations with the sponsor to avoid misaligned asks later.

- **Calibrate information sharing**

  Map what the shareholder agreement/financing documents permit, cross-check against the company's UPSI / legitimate purpose policy, and route sensitive updates through the Company Secretary. When the sponsor requests granular packs, ask: Is this within contractual rights? Is it UPSI? Has the board approved the sharing protocol?

- **Build a conflict-management routine**

  Maintain an updated Section 184 disclosure register; seek board clearance before engaging on sponsor-side matters; and recuse (ensure the recusal is recorded in minutes) where objectivity could be questioned.

- **Lean on independent processes**

  For significant related-party transactions, restructurings, or asset sales, push for independent valuations, fairness opinions, and audit/NR committee review. This is as much about getting to the right answer as it is about showing your route to it.

- **Minute with intent**

  Board minutes should capture disclosure of interests, the advice considered, key risks debated, and the rationale for decisions. If you dissent, record it courteously and precisely.

- **Respect the boundary between oversight and management**

  Nominee directors add real value by sharpening strategy, risk oversight, and governance—not by running the company. Micro-management blurs accountability and invites liability without commensurate control.

- **Be committee-savvy**

  Understand how SEBI LODR shapes committee composition and roles—particularly Audit, NRC, and Risk Committees—so you can influence governance architecture without stepping into "independence" shoes you do not wear.

- **Prepare for stress early**

  If performance wobbles, advocate for early independent business reviews, liquidity mapping, and turnaround options. Frame choices in terms of enterprise value and stakeholder fairness. In a crunch, this record of prudence matters.

A nominee director, will do well to remember that courts scrutinise process. So being diligent in disclosure, independent judgment, proper purpose, and reasoned decision-making will go a long way, if and when a conflict arises. Further, keep oneself abreast of evolving SEBI / Company law changes and insider trading rules.

The most effective nominee directors are candid with their sponsors: "I am here to represent your perspective, to insist on transparency, and to push for performance but my vote is governed by law and the company's long-term interest." That clarity, combined with rigorous process, is what separates a sponsor's eyes and ears from a sponsor's proxy. Handled well, nominee directorships improve governance quality, reduce surprises, and enhance trust among investors, lenders, and management.

Key references: Companies Act, 2013 (Sections 166, 184, 161(3)); SEBI LODR Regulations, 2015 (Regulations 16 and 17); SEBI PIT Regulations, 2015 (Regulation 3 on legitimate purpose/UPSI); Dale & Carrington Investments v. P.K. Prathapan (2004); Supreme Court judgment in the Tata Sons–Cyrus Mistry matter (2021).