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Metamorphosis in Corporate Governance Due to Artificial Intelligence

Simran Karkhur[a]

[a]Symbiosis Law School, Pune, India

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Technology is changing and evolving day by day. As new technologies emerge, AI systems are likewise evolving and adapting. This led to AI systems also becoming heavily involved in the job of corporate governance. Artificial intelligence (AI) is making its way into every sector of the economy. The study, development, and application of artificial intelligence (AI) are heavily influenced by companies, which has far-reaching consequences for the structure of society. This Article Examines the roles of AI, the Board of Directors, and their interplay, this article delves into how AI is changing corporate governance practices in response to its constant improvement and personalization. The article aims to explain why corporate board members need to know the basics of AI to fulfill their responsibilities and to talk about how AI is influencing corporate governance. It delves into the benefits and drawbacks of incorporating AI into corporate governance and decision-making at large. Finally, the article concludes by suggesting many avenues for future study in this developing field.

Keywords: *algorithm, artificial intelligence, board of directors, corporate governance.*

INTRODUCTION

Corporations are distinct legal entities from their shareholders and managers.[1] Their ability to own assets, sue and be sued, and exist independently from individuals is a result of their separate personalities. The appointment of VITAL, an algorithm, to the board of directors of Deep Knowledge Ventures, a venture capital firm based in Hong Kong, began discussions about the potential role of artificial intelligence in corporate governance in 2014.[2]

Investments in artificial intelligence (AI) have increased significantly over the years, in the field of the corporate world. Businesses are exploring ways to use AI to enhance corporate governance and streamline operations in response to the growing role of the board of directors (BoD) in the company.[3] Following the positive results shown in several case studies (covered in the article below), many academics and companies are looking forward to the potential future use of AI to enhance governance. Strategic decision-making also benefits from big data and algorithmic decision-making, which carry out small but time-consuming tasks like dealing with big numbers, classifying figures, etc. Meanwhile, using AI for corporate governance raises several possible issues, some of which might be more serious than others. This article delves into how the ever-changing landscape of artificial intelligence (AI) is impacting the way corporate governance is handled in India's legal system.

RESEARCH QUESTION

1. Whether the Companies Act, 2013 allows businesses to look into AI as a potential method to improve corporate governance.

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[1] Florian Möslein, 'Chapter 25: Robots in the Boardroom: Artificial Intelligence and Corporate Law' in Woodrow Barfield and Ugo Pagallo (eds), *Research Handbook on the Law of Artificial Eurasia: Intelligence* (ElgarOnline 2018)
[2] M.A. Tokmakov, 'Corporate Governance Modernization: Legal Trends and Challenges' (Eurasia: Sustainable Development, Security, Cooperation – 25 November 2019) <https://doi.org/10.1051/shsconf/20197104011> accessed 28 January 2024
[3] Martin Petrin, 'Corporate Management in the Age of AI' (2019) 3 Columbia Business Law Review 980-981 <https://doi.org/10.7916/cblr.v2019i3.5118> accessed 29 January 2024

2. How can we begin implementing AI while bearing in mind the numerous challenges that AI presents?

ROLE OF BOARD OF DIRECTORS

Understanding the role of a company's board of directors is a prerequisite to exploring how artificial intelligence (AI) and corporate governance (CG) interact. They should be adequately informed before making key choices on behalf of the company,[4] and they should prioritize the interests of the business and its investors.[5] Executives do not have the authority to assign tasks to individuals who are not also directors.[6] Therefore, it appears crucial to investigate the impact of AI on boardroom discussions.

ARTIFICIAL INTELLIGENCE

Artificial intelligence devices can be constructed using algorithms that incorporate deep learning, standards for interim analysis, and instructions for further actions to take based on the first evaluation. When it comes to corporate governance,[7] AI might be a game-changer. An entry-level form of automation, 'Robotic Process Automation' refers to the use of algorithms to simulate common human tasks like report creation. By simulating human actions on the screen, the machines can update themselves and retrieve data from networks.[8] This software is easy to understand and use. Data-driven decision-making is the primary use case for AI in businesses.

INTERSECTION OF AI & CORPORATE GOVERNANCE

Autonomous systems in organizations are expected to become more efficient shortly, adding to the daily advancements in AI and sophisticated algorithms that are already changing the face of

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[4] *McMullin v Beran* [2000] 765 A.2d 910, 921 (Del)
[5] *Frederick Hsu Living Trust v ODN Holding Corp*. [2017] CA No 12108-VCL (Del Ch)
[6] *Canal Capital Corp. v French* [1992] WL 159008 (Del Ch)
[7] Irina Ivashkovskaya, 'What Impact does Artificial Intelligence have on Corporate Governance?' (2020) 14(4) Journal of Corporate Finance Research 90, 92 <file:///C:/Users/aspin/Downloads/11252-%D0%A2%D0%B5%D0%BA%D1%81%D1%82%20%D1%80%D1%83%D0%BA%D0%BE%D0%BF%D0%B8%D1%81%D0%B8-26969-2-10-20210215.pdf> accessed 29 January 2024
[8] Joost N. Kok et al., 'Artificial Intelligence: Definition, Trends Techniques, and Cases' in Joost Nico Kok (ed), *Artificial Intelligence* (EOLSS)

business.[9] The topic of how AI and algorithms will function in boardrooms arose, nevertheless, as AI technology advanced. Since algorithms began to permeate all levels of an organization, from the most foundational (like 'Amazon's box-packing bots') to the most executive (like 'Vital'),[10] it is clear that this trend is here to stay. Modern artificial intelligence (AI) encompasses a wide range of tools and techniques, including symbolic logic, artificial neural networks (ANNs), fuzzy systems, evolutionary computing, intelligent agents, and probabilistic reasoning models. These enable AI to do tasks such as data analysis, forecasting, data consistency development, uncertainty quantification, data needs anticipation, information delivery in the best format, and course of action suggestions.[11] Helping humans to make decisions, particularly when faced with unknowns, or perhaps taking over entirely is one of the greatest contributions of AI made possible by the aforementioned methods and resources. As a result, it's reasonable to say that AI could help businesses by assuming control at every level. Nevertheless, a great deal of data is required for decision-making, and more data is required for complicated judgments. To clarify, AI helps to break down massive volumes of data into smaller pieces, which makes it easier to make decisions when faced with uncertainty. [12]

AI is increasingly examining industry practices. This is especially true for investment firms that want to know the social impact of the companies they own.[13] Companies can save money on administrative expenses by implementing AI into their corporate governance processes. Additionally, AI can help find anomalies more quickly and machine learning is better than humans at selecting board members.[14] According to many studies, it could help the board of

[9] Mihailis Diamantis, 'The Extended Corporate Mind: When Corporations Use AI to Break the Law' (2020) 97 North Carolina Law Review 893 <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3422429> accessed 31 January 2024
[10] Diamantis (n 9)
[11] Möslein (n 1)
[12] Ajay K. Agrawal et al., 'Exploring the Impact of Artificial Intelligence: Prediction Judgment' (2016) American Economic Association <https://www.aeaweb.org/conference/2017/preliminary/1426?page=2&per-page=50> accessed 31 January 2024
[13] Robert G. Eccles and Miriam Vogel, 'Board Responsibility for Artificial Intelligence Oversight' (*Harvard Law School Forum on Corporate Governance*, 05 January 2022) <https://corpgov.law.harvard.edu/2022/01/05/board responsibility-for-artificial-intelligence-oversight/> accessed 31 January 2024
[14] Isil Erel et al., 'Selecting Directors Using Machine Learning' (2018) Fisher College of Business Working Paper No 2018-03-005 <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3144080> accessed 29 January 2024

directors, auditors, and shareholders[15] move away from data sample evaluation methods and towards systems that continuously and in real-time examine all available data about a company.[16]

A robot named 'Vital' was appointed to the board of directors of Deep Knowledge Analytics, a venture capital firm based in Hong Kong.[17] For the board's investment decisions, Vital served as an analyst, which was essentially an algorithm that sifted through massive amounts of data to assess potential prospects. Marc Benioff, CEO of Salesforce, unveiled an artificial intelligence system he called 'Einstein' during his monthly staff meeting. As a follow-up to their conversations, Marc Benioff would inquire as to Einstein's thoughts on the topics covered. KPMG using AI to identify red flags in financial data that could indicate fraud.

Autonomous data analysis, according to some researchers, can both make better decisions and stop managers from abusing their power. Artificial intelligence (AI) has the potential to improve internal monitoring, which includes the audit quality mentioned earlier, and can aid in the detection of anomalies.[18] However, more than just the Board of Directors stand to gain from AI in the long run. Therefore, the author believes that algorithms and other forms of machine learning should work in tandem with human judgment, not in place of it. Directors must be aware of developments in artificial intelligence (AI) that could drastically alter the company's future or render some industries obsolete.

CHALLENGES OF AI-POWERED CORPORATE GOVERNANCE

Although AI has many more capabilities than humans when it comes to fast data analysis, it is important to acknowledge that it does have limitations. [19]The foundation of artificial intelligence

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[15] David Y Chan and Miklos A. Vasarhelyi, 'Innovation and practice of continuous auditing' (2011) 12(2) International Journal of Accounting Information Systems 152-160 <http://dx.doi.org/10.1016/j.accinf.2011.01.001> accessed 29 January 2024
[16] Juan Zhang et al., 'Toward effective Big Data analysis in continuous auditing' (2015) 29(2) Accounting Horizons 469-476 <http://dx.doi.org/10.2308/acch-51070> accessed 29 January 2024
[17] Deep Knowledge Group, https://www.dkv.global/about (last visited February 10, 2024)
[18] Danielle Lombardi et al., 'The Current State and Future of the Audit Profession' (2015) 9(1) Current Issues in Auditing 10-16 <http://dx.doi.org/10.2308/ciia-50988> accessed 29 January 2024
[19] 'The Impact of AI on Corporate Governance' (*ZZOOTA*, 10 September 2021) <https://zzoota.com/blog/2021/8/12/the-impact-of-ai-on-corporate-governance> accessed 29 January 2024

learning is derived from artificial input, which presents a distinct risk, and it may initially confront prejudice and human error. Because of the character of these environments, bias has a significant impact on education. This sparks the first fear about fully automated corporate governance systems. For all their work, algorithms depend on 'the data they lack'.[20]

Algorithm fairness and discrimination is a difficult topic in the modern world. One of the biggest problems with AI in corporate governance is biased decisions. For instance, racial bias in AI systems can lead to significant discrimination in society if, for instance, a system chooses white females for nursing recruitment or ignores African Americans when treating skin cancer. Artificial intelligence algorithms, according to studies, are biased toward using big and old data to discriminate against women and other historically oppressed groups. Put another way, AI systems pick up knowledge from human-made works. As an example of the correlation between data collection and biased decision-making, consider a mobile app that can identify flaws. The app would likely find more of these problems in the homes of the wealthy since they are more likely to own mobile phones. This explanation allows us to mention that AI algorithms will create their ideas based on acquired data, much of which comes from humans. Contrary to overt prejudice, however, AI-generated bias is subtle, counterintuitive, and hard to pin down. As a result, individuals may have trouble understanding that algorithms are biased against them, and it is also difficult to demonstrate that algorithms are biased. Nonetheless, there are still several ways to identify bias, such as through statistical analysis.

On top of that, AI cannot guarantee the company's smooth running or come up with an organizational and operational strategy. Creativity and resourcefulness are human traits that technology fails to account for. Obtaining support from executives is another challenge, especially if board members do not see AI as a tool to supplement their work. When it comes to responsibility, decisions made by unchecked AI should not replace or influence those made by human directors.

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[20] Betsy Anne Williams et al., 'How Algorithms Discriminate Based on Data They Lack: Challenges, Solutions, and Policy Implications' (2018) 8 Journal of Information Policy 78-115 <https://pdfs.semanticscholar.org/8dbc/2a67f0142104c82c32e1ebced118c8d69937.pdf> accessed 29 January 2024

AN INDIAN PERSPECTIVE ON AI'S ROLE IN BOARD MEETINGS

Despite AI's immense potential to revolutionize Indian boardrooms, its integration into the country's corporate governance framework has mostly gone unnoticed. The term 'director' is not defined in any detail in the Companies Act, 2013. Any person appointed to a company's Board of Directors is defined as a director under Section 2(34). Because only natural persons can be nominated as directors, no AI can be considered for a position on a board according to the regulations governing corporate governance in India. Only natural individuals are authorized to get limited director powers under the legislation.[21] Therefore, AI also cannot be given directorial powers.

It is not possible for AI to autonomously control a firm according to the Companies Act.[22] Consequently, artificial intelligence cannot carry out the duties of a director under the existing laws. 'Directors cannot deleverage themselves of the responsibility by assigning the whole administration to the agent and abstaining from any inquiries,' the court stated in **Re Central Calcutta Bank Ltd.** Consequently, directors cannot hand over their duties to AI; nevertheless, they can use AI as a helpful assistant to help them with their tasks.[23]

The Act only establishes liability for natural persons. Directors will be held responsible for the actions of AI if the board uses AI to assist in decision-making and the director follows AI's judgment after conducting proper checks. Additionally, the author would like to talk about the responsibilities of directors regarding artificial intelligence in the boardroom as outlined in the IT Act, 2000. The director is responsible for ensuring that all systems are properly installed, adequate, and performing to fulfill cyber security standards.[24]

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[21] Companies Act 2013, s 179

[22] Rongeet Poddar, 'The Prospect of AI in the 'Virtual' Corporate Boardroom' (*INDIACORPLAW*, 12 May 2020) <https://indiacorplaw.in/2020/05/the-prospect-of-ai-in-the-virtual-corporate-boardroom.html> accessed 29 January 2024

[23] Ashish Makhija, *Corporate Directors- Roles, Responsibility, Powers and Duties of Directors* (LEXIS NEXIS 2016)

[24] David R. Fontaine and John Reed Stark, 'Cyber security: The SEC's Wake-up Call to Corporate Directors' (*Harvard Law School Forum on Corporate Governance*, 31 March 2018) <https://corpgov.law.harvard.edu/2018/03/31/cybersecurity-the secs-wake-up-call-to-corporate-directors/> accessed 29 January 2024

FOUNDATION FOR THE GOVERNANCE OF AI

Whether the organization has sufficient data for the data mining needed by the particular AI technology is a major factor for any board considering AI implementation. Deploying AI will require meticulous information management. The board, in keeping with its duty of guidance and protection, needs to look into data collection and storage practices to see if AI can work or if more extensive changes are needed. Implementing AI will also necessitate evaluations to determine whether AI is accurately interpreting data and how to secure it from intruders. It is crucial that if a board does decide to use AI, the company does not outsource its fundamental management responsibilities and instead uses AI to make all of the firm's decisions. Delegating its responsibility in this way is strictly prohibited.

SUGGESTIONS

Based on the data presented above, the author offers some recommendations for how AI can be used in boardroom settings:

Essential steps for incorporating AI into executive meetings: First, AI should only be used for data analysis and conference planning, considered operational aspects of corporate governance. After a while, it can be entrusted with making strategic decisions. In addition, the directors can hand over control to AI once they're familiar with the concept.

Determining the legality and responsibilities of AI: A duly authorized national body in India should lay down the limits of what artificial intelligence (AI) is capable of doing. Indian law needs a definition for AI.

Educating directors on emerging technology practices: When it comes to technology, Indian directors are generally on the cautious side. Businesses in India need to adopt tech strategies driven by artificial intelligence if they wish to thrive going forward. A policy outlining the responsibilities of each director must be established before the use of artificial intelligence (AI) in boardrooms is considered. To prevent AI liability, the policy must address any risk and offer protection against it.

Chief Technology Officer (CTO): It is recommended that all companies employ a chief technology officer. The company's board of directors and upper management can benefit from this CTO's insight into how to make the most of new technologies.

CONCLUSION

The entrance of AI paved the way for the breakthroughs of today. Directors need to be aware of the hazards associated with the ever-changing landscape of AI as it permeates numerous companies. Therefore, boards need to have a basic understanding of AI and how it may be used in their unique business to comply with fiduciary requirements and practice efficient corporate governance. It is plausible to assume, based on the authors' reasoning, that contemporary technology will greatly improve the efficiency and speed of corporate governance. However, current legislation is not detailed enough to grant rights or impose obligations related to artificial intelligence.