



THE CONCEPT OF THE INTEREST OF A LEGAL ENTITY AND ITS PLACE IN THE SYSTEM OF FIDUCIARY DUTIES OF A DIRECTOR

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Abstract

This article is dedicated to one of the pressing issues of corporate law – the emergence of fiduciary duties of a director in business entities and the clarification of the essence of the concept of "legal entity interest." The study provides a comparative analysis of the "Shareholder Primacy," "Pluralist Approach" (Stakeholder Theory), and "Enlightened Shareholder Value" approaches. Specifically, scientific proposals for improving the corporate legislation of Uzbekistan have been developed based on the UK Companies Act 2006 and other foreign experiences. The article highlights the relationship between the director's discretionary powers and the Business Judgment Rule.

Keywords: Fiduciary duties, interest of the legal entity, director's liability, shareholder primacy, stakeholders, enlightened shareholder value, corporate governance.

Introduction

One of the most controversial and fundamental issues in modern corporate law concerns whose interests the individuals managing business entities—directors and members of management bodies—must pursue in the performance of their duties. In the management of a legal entity and the determination of corporate liability, the question "to whom are the director's fiduciary duties owed?" is of



crucial importance¹. The Civil Code of the Republic of Uzbekistan² and special corporate laws establish that a director must act in the interests of the company, with good faith and reasonableness. These general rules imply that a director is required to compensate for damages caused to the legal entity, signifying that fiduciary duties are owed directly to the legal entity itself—an independent subject of law.

However, the issue lies in the fact that the concept of "interest of the legal entity" itself is considered a rather abstract category in both legal doctrine and practice. A legal entity is a legal fiction and possesses no "personal" biological or psychological interests. Consequently, this concept is frequently subjected to critical analysis in legal literature, where it is emphasized that its content must be substantiated by the interests of specific groups of natural or legal persons. Each jurisdiction's legal system interprets the interest of the legal entity differently, depending on whom it recognizes as the "key participants" in corporate relations³.

The objective of this study is to analyze the main theoretical models established in global practice for defining the concept of "interest of the legal entity"—namely, Shareholder Primacy, the Pluralist Approach, and Enlightened Shareholder Value theories—and to determine their place within the corporate governance system of Uzbekistan. This article examines the issues of how a director resolves the clash of various interests during the decision-making process and what criteria legislation should establish in this regard.

RESEARCH METHODS

This study employs comparative-legal, logical-analytical, and systematic analysis methods. The institute of fiduciary duties in corporate governance and the category of "interest of the legal entity" were selected as the objects of the research.

Comparative-legal analysis: During the research, the norms of the Anglo-Saxon legal system, specifically the UK Companies Act 2006⁴, were analyzed. The

¹ Keay, A. (2013). *The Enlightened Shareholder Value Principle and Corporate Governance*. Routledge.

² Civil Code of the Republic of Uzbekistan (1995).

³ Freeman, R. E. (1984). *Strategic Management: A Stakeholder Approach*. Boston: Pitman.

⁴ Companies Act 2006. (UK Public General Acts). Section 172: Duty to promote the success of the company. legislation.gov.uk.



directors' duties enshrined in Section 172 of this Act and the mechanisms for taking into account the rights of stakeholders were studied. Additionally, the practical aspects of the "Stakeholder Theory" as applied in the USA and Continental European countries were examined.

Theoretical modeling: The strengths and weaknesses of the three existing main approaches for defining the interest of a legal entity—the Shareholder Primacy, Pluralist Approach, and Enlightened Shareholder Value models—were compared. The impact of each model on director liability and its role in the efficiency of corporate governance were evaluated.

Doctrinal analysis: The concept of "key participants" presented in legal literature and its characteristic of variability depending on time and space factors were studied.

In preparing the article, the degree of alignment between national legislative norms and international corporate governance principles (OECD Principles) was verified. The analysis primarily focused on the problems of legal regulation concerning the director's discretionary powers and the conflicts of interest arising during their implementation.

RESULTS

The analyses conducted indicate that there is no single universal approach to defining the interest of a legal entity; rather, three main concepts that have evolved over the course of history are in competition with one another.

1. Shareholder Primacy Approach According to the initial and most classical approach, the interests of the shareholders (members) fully reflect the interests of the legal entity. Under this theory, a company is a vehicle existing solely to satisfy the proprietary interests of its owners, the shareholders. Consequently, the primary duty of the director consists of maximizing shareholder profit (profit maximization) in the management of the company⁵. The analysis demonstrated that this approach requires the director to act in a manner that serves the general interests of all shareholders, rather than specific or privileged shareholders. The

⁵ Jensen, M. C. (2001). Value Maximization, Stakeholder Theory, and the Corporate Objective Function. *Journal of Applied Corporate Finance*, 14(3), 8-21.



advantage of this model lies in the clarity of the objective for the director (profit maximization) and the transparency of the criteria for evaluating their performance (financial indicators). However, this approach may lead to the pursuit of short-term profit (short-termism) and the neglect of other social interests⁶.

2. Pluralist Approach or Stakeholder Theory Modern economic reality demonstrates that a company is a center for harmonizing various interests. The activity of a legal entity affects not only shareholders but also other members of society. Consequently, the "Pluralist Approach" was formed. According to this approach, in managing the company, the director is required to take into account not the narrow interests of shareholders, but the interests of a broader circle of persons (stakeholders) affected by the activities of the legal entity. Results indicated that this category of persons includes company employees, customers, creditors (counterparties), the local community, and the environment. Here, the concept of Corporate Social Responsibility (CSR) takes a central position⁷. However, serious practical drawbacks of this approach have been identified. First, the boundaries of the circle of "stakeholders" are not clear, and there is no unified position in legislation regarding this matter. Second, the interests of different groups often conflict with one another. For example, while shareholders may be interested in increasing dividends by reducing costs, employees may demand higher wages. In such a situation, it remains open as to which interest the director should prioritize, which may create grounds for disarray in management or allow the director to evade liability.

3. Enlightened Shareholder Value (ESV) Approach

To address the limitations of the two aforementioned approaches, the "Enlightened Shareholder Value" approach is being proposed in the United Kingdom and developed countries. Research results have determined that this model is the most optimal solution. The essence of the ESV approach lies in

⁶ Berle, A. A., & Means, G. C. (1932). *The Modern Corporation and Private Property*. New York: Macmillan.

⁷ OECD (2015), *G20/OECD Principles of Corporate Governance*, OECD Publishing, Paris.



focusing primarily on increasing company profit from a long-term perspective, thereby excluding the strategy of short-termism⁸.

According to this model, if it serves to ensure the long-term activities of the company, the director may and must consider the interests of employees, as well as the interests of society and the environment. For instance, granting certain discounts to major counterparties for the purpose of maintaining long-term cooperation or introducing employee incentive systems is justified. However, the primary condition is that such "concessions" must be economically substantiated by serving the ultimate goal of the company's long-term stability and the enhancement of shareholder value.

DISCUSSION

The results obtained indicate that the "Enlightened Shareholder Value" (ESV) approach is the model best suited to the requirements of modern corporate governance in understanding the interest of a legal entity. This approach does not deny shareholder interests but rather re-examines them through the prism of long-term stability⁹.

Within the scope of a director's fiduciary duties, he or she must consider various factors to ensure the company's success. As established in Section 172 of the UK Companies Act 2006, when acting in the interests of the company, a director must take into account factors regarding employees, customers, counterparties, the community, and the environment. This list is not exhaustive, as key participants may vary depending on time and place.

Conflicts of Interest and the Business Judgment Rule The most important aspect of the ESV approach is that it grants the director discretionary power. The director determines what should be understood by the interest of the legal entity and which factors should be prioritized. In this process, the director's decisions must be protected by law. In global practice, this is implemented through the "Business Judgment Rule" (BJR).

⁸ Easterbrook, F. H., & Fischel, D. R. (1991). *The Economic Structure of Corporate Law*. Harvard University Press.

⁹ Stout, L. A. (2012). *The Shareholder Value Myth: How Putting Shareholders First Harms Investors, Corporations, and the Public*. Berrett-Koehler Publishers.



According to the BJR, if a director makes a decision without a conflict of interest, on an informed basis, in good faith, and with the belief that it is in the best interests of the company, courts will not re-examine their business decisions or hold them liable. This rule encourages the director not to fear risk-taking and to make long-term strategic decisions. Without the BJR, the director would always be forced to make "safe" decisions seeking short-term profit, which is contrary to the ESV principle¹⁰.

PROPOSALS FOR THE LEGISLATION OF UZBEKISTAN

In the corporate law of Uzbekistan, the concept of "interest of the legal entity" has not yet been fully elucidated. Although the Civil Code and the Law "On Joint-Stock Companies and Protection of Shareholder Rights" establish that a director must act in the interests of the company, the constituent elements of this interest (employees, creditors, the environment) have not been specified.

In our opinion, it is advisable to introduce elements of ESV into national legislation. This should include the following:

1. Directly indicating the obligation to take into account long-term development, as well as the interests of employees and creditors, within the norms defining the director's fiduciary duties.
2. Clearly defining mechanisms in the judicial practice of Uzbekistan for exempting a director from liability for an "honest business mistake."
3. Establishing a requirement to provide information in directors' annual reports not only on financial results but also on activities regarding social and environmental factors (ESG reporting).

CONCLUSION

The interest of a legal entity is not a rigid dogma, but a dynamic concept adaptable to the socio-economic development of society. Analyses have demonstrated that the pursuit of Shareholder Primacy alone does not align with the goals of modern business ethics and sustainable development. At the same time, an unbounded Pluralist Approach leads to uncertainty in governance.

¹⁰ Millon, D. (2011). Two Models of Corporate Social Responsibility. Wake Forest Law Review, 46, 523.



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The "Enlightened Shareholder Value" (ESV) approach should be recognized as the most optimal solution. This approach requires the director to maintain a balance among the interests of all participants—shareholders, employees, customers, and society—to ensure the long-term success of the company. The discretionary powers granted to the director and their protection through the Business Judgment Rule (BJR) constitute the legal guarantee for maintaining this balance. Implementing these theoretical models into national legislation is of significant importance in elevating the culture of corporate governance in Uzbekistan.

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