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Navigating the Legal Maze: Nominee Dilemma in Securities Ownership

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*This article delves into the intricate legal landscape surrounding the nomination of securities in India, focusing on the distinction between legal and beneficial ownership as outlined in the Companies Act 2013. The role of nominees in asset transfer after the owner's death raises significant legal questions, particularly regarding the rights of nominees versus rightful heirs. While nominees are initially recognised as the legal owners, they are required to hold the assets in trust for the legal heirs, who retain ultimate ownership rights. Key judicial rulings, including the Supreme Court's decision in **Shakti Yezdani v Jaayanand Jayant Salagaonkar**,¹ have affirmed that nomination does not supersede testamentary or intestate succession. This article explores these legal principles and landmark judgments, highlighting the nominee's fiduciary responsibilities and ensuring the protection of legal heirs' rights. A nuanced understanding of these issues is crucial for ensuring efficient asset transfer processes within the corporate and financial sectors in India.*

Keywords: *nomination, securities, legal ownership, nominee rights, beneficial ownership.*

¹ *Shakti Yezdani v Jaayanand Jayant Salagaonkar* (2023) SCC OnLine SC 1679

INTRODUCTION

In the realm of financial instruments, the concept of nomination plays a pivotal role in ensuring the seamless transfer of assets upon the death of the owner. However, this ostensibly straightforward mechanism masks a complex legal landscape, particularly within the context of Indian law. The Companies Act 2013, especially Section 72², provides the statutory framework governing the nomination of securities, yet it introduces a critical dichotomy between legal and beneficial ownership. This distinction raises significant legal challenges, as nominees, while recognised as the legal owners of the assets, do not possess beneficial ownership and are required to transfer these assets to the rightful legal heirs.

This longstanding debate on the conflict between the rights of nominees and legal heirs over the devolution of shares has always been a source of controversy and confusion. Despite the settled legal position holding the legal heir as the ultimate rightful owner of the property, the introduction of Section 109A by the Companies (Amendments) Act 1999³ revived the debate. The amendment under Section 109A and 109B⁴, which was re-enacted as Section 72 of the Companies Act 2013 allowed shareholders to appoint a nominee who would own the instrument upon the holder's death unless the nomination was varied or cancelled.

The controversy was further fueled by judicial interpretations. The Bombay High Court's ruling in *Harsha Nitin Kokate v The Saraswat Co-operative Bank Limited*⁵ held the nominee as the beneficial owner of shares after the death of the original owner, suggesting that nomination could override succession. However, this was later overturned in *Jayanand Jayant Salgaonkar v Jayshree Jayant Salgaonkar*⁶, where the Bombay High Court declared the Kolkata judgment per incuriam and affirmed that legal heirs, not nominees, hold ownership rights over shares. The Supreme Court ultimately settled the debate in *Shakti Yezdani & Anr v Jayanand Jayant Salgaonkar & Ors.*⁷, ruling that a nominee in shares or securities does not inherit them by

² Companies Act 2013, s 72

³ Companies (Amendments) Act 1999, s 109A

⁴ Companies Act 2013, s 109B

⁵ *Harsha Nitin Kokate v the Saraswat Co-operative Bank Limited* (2010) SCC OnLine Bom 615

⁶ *Jayanand Jayant Salgaonkar v Jayshree Jayant Salgaonkar* (2015) SCC OnLine Bom 1221

⁷ *Shakti Yezdani v Jaayanand Jayant Salagaonkar* (2023) SCC OnLine SC 1679

default. The Court clarified that the provisions relating to nomination under the Companies Act and the Depositories Act do not override the rules of succession under the Indian Succession Act 1925 or personal succession laws.

NOMINATION UNDER THE COMPANIES ACT 2013

Nomination under normal legal provisions entails the transfer of property, securities, bank deposits, or insurance amounts to the nominee's name. The responsibility of the company, depository, insurer, or banker is entirely fulfilled upon the transfer of securities or payment in the nominee's name. Nomination serves as a temporary arrangement to prevent assets from becoming ownerless while succession matters are resolved. It is a facilitative mechanism rather than a conclusive resolution. In the absence of a nomination, legal heirs may encounter complications in establishing their rights, and all assets, including mutual funds and insurance, will remain with the respective companies until succession issues are resolved.

Interestingly, the Companies Act 2013 has a different take on this matter. It addresses the issue of nominees in securities through Section 72⁸, providing a comprehensive framework for the nomination process and the subsequent rights and obligations of nominees. Section 72(1) explicitly empowers an individual to nominate a person to whom the securities shall *vest* in the event of their demise.⁹

However, Section 72(3)¹⁰ of the Act introduces a provision that, while streamlining the process of asset transfer through nomination, simultaneously presents challenges in determining the status of a nominee. The provision stipulates that, upon the death of the holder of securities or joint holders, the nominee becomes entitled to all the rights in the securities, excluding all other persons, unless the nomination is cancelled or varied in the prescribed manner.

This seemingly straightforward directive creates a potential problem when it comes to the status of the nominee. The exclusivity conferred upon the nominee, as outlined in Section 72(3), may lead to a situation where the nominee is perceived as the absolute owner of the securities despite

⁸ Companies Act 2013, s 72

⁹ Companies Act 2013, s 72(1)

¹⁰ Companies Act 2013, s 72(3)

the underlying principle that the nominee functions as a trustee for the legal heirs. This inherent conflict between the nominee's exclusive entitlement and the fiduciary role they are expected to fulfil raises questions about the clarity and balance in the legal framework.

JUDICIAL CLARIFICATIONS ON NOMINEE RIGHTS

Due to the ambiguous and unclear interpretation of Section 72(3) of the Act, the legal standing of nominees and whether nomination supersedes inheritance has been a subject of ongoing debate in India for an extended period. Various situations arise where individuals designate nominees, such as when acquiring an insurance policy, purchasing shares, or establishing a fixed deposit with a bank.

This dilemma was further clarified in 1984 in the case of *Sarbati Devi v Smt. Usha Devi*¹¹, wherein it was held that nomination does not confer on the nominee any beneficial interest in the amount payable under nomination. The nominee is a mere holder of the assets, and the true economic ownership lies with the legal heirs, who possess the ultimate right to claim their share in the deceased's estate. Although this judgment provided a robust legal precedent in determining the status of the nominee, it is essential to note that the case specifically pertained to insurance policies and aligned with Section 39 of the Insurance Act¹² as held in the case of *Aruna Oswal v Pankaj Oswal*,¹³ Section 39 of Life Insurance Act is different from the provisions under Section 72 of the Companies Act, 2013.

Strict Interpretation of the Non-Obstante Clause: Conversely, in disputes over the shares of a deceased person, courts have consistently upheld the non-obstante clause of Section 72(3)¹⁴ of the Act. In *Dayagen Private Limited v Rajendra Dorian Punj and Anr.*,¹⁵ the Delhi High Court provided a stringent interpretation of Article 109A of the Companies Act¹⁶ (now Section 72(3) of the Companies Act)¹⁷. The court stressed that the legislative intent is to supersede general

¹¹ *Sarbati Devi v Usha Devi* (1984) 1 SCC 424

¹² Insurance Act 1938, s 39

¹³ *Aruna Oswal v Pankaj Oswal* (2020) 8 SCC 79

¹⁴ Companies Act, 2013, s 72 (3)

¹⁵ *Dayagen Private Limited v Rajendra Dorian Punj and Anr* (2008) 105 DRJ 29

¹⁶ Companies Act 2013, s 109A

¹⁷ Companies Act, 2013, s 72(3)

succession laws, creating an exception for share and debenture nominations. Strict compliance with procedural requirements, such as proper attestation by a witness, is essential for the nomination to have an overriding effect. Similarly, in the 2010 case of *Harsha Nitin Kokate v The Saraswat Co-operative Bank Limited & Ors*¹⁸, the Bombay High Court clarified that Sections 109A of the Companies Act¹⁹ and 9.11 of the Depositories Act²⁰ are intended to transfer property rights, including ownership, to the nominee when the nomination follows the prescribed procedure. Consequently, a valid nomination leaves the legal heirs without a claim to the deceased's assets. Interestingly, in the case of *Aruna Oswal v Pankaj Oswal*²¹, it was initially indicated that, prima facie, the non-obstante clause in Section 72(3) of the Companies Act 2013²² results in an absolute vesting of shares in the nominee. On the surface, the nominee is considered the unequivocal owner of the securities based on the nomination. However, the final impact of the nomination might be determined in a civil suit.

Current Stance: In the recent ruling of the Apex Court in the case of *Shakti Yezdani v Jaayanand Jayant Salagaonkar*²³, it was clarified that a nominee is not the rightful owner of an asset but instead holds it in a fiduciary capacity for the benefit of the legal heirs, as determined by the will or applicable succession laws. The Court ruled that successors, not nominees, have a claim over shares and debentures. Therefore, even if a person is named as a nominee in a share or debenture certificate, they are not automatically entitled to inherit it. The succession of these financial instruments will be determined by the deceased's will or by succession laws.

The court further clarified that a valid nomination made by a shareholder under Section 109A of the Act, 1956 (corresponding to Section 72(3) of the Companies Act, 2013) and Bye-law 9.11 of the Depositories Act, 1996 does not act as a 'statutory testament.' This ruling emphasised that nomination does not override testamentary or intestate succession. Although the nomination process provides a discharge to the involved entity once the nominee is designated, it does not

¹⁸ *Harsha Nitin Kokate v Saraswat Coop. Bank Ltd* (2010) 3 Mah LJ 780

¹⁹ Companies Act 2013, s 109A

²⁰ Depositories Act 1996, s 9(11)

²¹ *Aruna Oswal v Pankaj Oswal* (2020) 8 SCC 79

²² Companies Act 2013, s 72 (3)

²³ *Shakti Yezdani v Jaayanand Jayant Salgaonkar* (2016) SCC OnLine Bom 9834

confer ownership of securities to nominees over legal heirs. Thus, the nomination process does not supersede succession laws, and nominees remain accountable to the legal heirs of the deceased.

Additionally, in the context of the case, the Court highlighted that the term 'vest' does not signify complete ownership of shares or securities. Rather, it acts as a provisional mechanism to mitigate uncertainties in shareholding after a shareholder's death, ensuring smooth corporate operations. The court stated that nominees serve as a facilitative arrangement, simplifying processes for companies, insurance firms, and banks to meet their obligations. The nomination allows these entities to fulfil their duties by holding the proceeds in a trustee capacity, ensuring compliance with intestate laws or a valid will to benefit the lawful heirs of the deceased.

CONCLUSION

In conclusion, the legal landscape surrounding the nomination of securities in India, as governed by the Companies Act 2013, demonstrates a complex interplay between legal and beneficial ownership. Although nominees are recognised as the legal owners of assets under Section 72(3), recent judicial rulings, such as the Apex Court's decision in *Shakti Yezdani v Jaayanand Jayant Salagaonkar*²⁴, have clarified that nominees hold these assets in a fiduciary capacity for the benefit of legal heirs.

In the Salagaonkar case, the Court highlighted the significant evolution of corporate instruments and securities. The focus of Sections 109A and 109B of the Companies Act, along with Bye-Law 9.11 of the Depositories Act, is not on the law of succession. Instead, these provisions are intended to provide companies or depositories with a legally valid discharge, ensuring they are not perpetually liable to multiple succession claims. This allows the liability to shift from the company or depository to the nominee.

The Supreme Court's decision has clarified the nominee's role, distinguishing it from that of an absolute owner. It is now clear that a nominee cannot be considered an heir upon the death of the instrument holder, as the nomination does not confer beneficial interest. The Court's analysis

²⁴ *Shakti Yezdani v Jayanand Jayant Salgaonkar* (2016) SCC OnLine Bom 9834

concluded that the vesting of assets in the nominee under the 1956 Act²⁵ was for a limited purpose. The interpretation of the non-obstante clause must reflect the statute's objectives, ensuring that legal heirs retain their claims over securities against the nominee.

Additionally, issues of wills, intestacy, and succession fall under Entry 5 of List III of Schedule VII of the Constitution of India²⁶, allowing both the State Legislature and Parliament to legislate on these matters. However, the Companies Act, enacted under Legislative Entries 43 and 44 of List I of Schedule VII²⁷, falls exclusively within the Parliament's jurisdiction, precluding the State Legislature from making amendments. Thus, the Companies Act cannot govern intestacy and succession matters, as it would infringe upon the State Legislature's legislative authority.

This judicial clarification affirms that the nomination process under the Indian Companies Act aims to streamline administrative procedures for companies and depositories while protecting the legal rights of heirs under succession laws. While the nomination process facilitates efficiency for financial entities, it does not absolve nominees of their responsibility to transfer assets to the lawful heirs.

²⁵ Companies Act 1956

²⁶ Constitution of India 1950

²⁷ *Ibid*