RIGHT OF NOMINATION V RIGHT OF SUCCESSION: A LACUNA IN COMPANIES ACT

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One of the recent lacunae in Companies Act,2013 is the issue regarding the right of legal heirs to shares as opposed to nominees. The position of the Supreme Court on this particular issue is still undecided, however there are binding judgments provided by the division bench of the Bombay High Court and a recent judgement by the National Company Law Appellate Tribunal (Hereinafter referred to as NCLAT) reiterated the same.

A nominee in common parlance shall be understood to be a beneficiary who is so nominated that he receives the benefit of an asset (money) upon the death of the individual who is the owner of that asset and who, in the relevant document, has appointed the nominee. A nominee's legal status has often been agreed to be that of an 'agent' or 'trustee' and appointment is not treated as an alternative to a succession rule.

The present issue arose due to two conflicting judgements of Single Judge Benches of the Bombay High Court in the decisions of ***Harsha Kokate v. The Saraswat Co-operative Bank Limited*** [i]and ***J. J. Salgaonkar v. J.J. Salgaonkar***[ii]**.**

In the Harsha Kotake v The Saraswat Co-operative Bank case (Hereinafter referred to as the Kotake Case) the relying primarily on Section 109A of the erstwhile Companies Act, 1956 (1956 Act)[iii], The Court held that the nominee would be entitled, to the exclusion of all other persons, to all rights in shares and debentures, including ownership rights. Thus, upon death of the shareholder, the securities would automatically get transferred to the nominee, and not the legal heirs. The Kotake case had created an ambiguity in law as it differed from the earlier stance taken by the Supreme Court that rights of succession would override and prevail over right of nomination.

However, in the decision of *J. J. Salgaonkar v. J.J. Salgaonkar* (Hereinafter referred to as Salgaonkar Case) the Single Judge Bench of Bombay High Court declared the Kotake Case to be per incurium and It was held that the legitimate heirs would inherit ownership of the shares, and not the nominees. Under existing succession rules, the nominees will merely keep the securities as a trustee on behalf of the claimants.

Therefore, due to two conflicting judgements of Single Judge Benches the issue was referred to a Division Bench of the Bombay High Court in the decision of ***Shakti Yezdani and Anr v. Jayanand Jayant Salgaonkar***[iv]. The Division Bench ruled that legal heirs and not the nominees will obtain the ownership rights of share certificates, effectively circumscribing the scope of the nomination of shares under the provisions of the Companies Act, 1956. The court observed that it is well recognized that the provision of nomination under th ese laws is solely for the security of the property of the Deceased pending the assertion and resolution by the heirs or descendants of the deceased of succession-related issues. The nominee does not get absolute title to the property, which is the subject matter of the nomination The explanation for this is, by its very nature, that when a shareholder or a deposit holder or an insurance policy holder or a member of a cooperative society makes an nomination in the course of his or her lifetime, he or she does not pass his or her interest to the nominee. It is always held that the nomination does not override the law in relation to testamentary or intestate succession.[v]

The decision of the Division Bench of the Bombay High Court was a welcome one because it removed the confusion caused by the earlier decisions and provided an affirmative view on the moot point. The issue again arose when the NCLAT in a landmark judgement reiterated the view of adopted by the division bench of the Bombay High Court and the matter was on appeal to the Supreme Court.

In the NCLAT, the case of ***Oswal Greentech* v *Mr Pankaj Oswal and Ors***[vi](Hereinafter referred to as Oswal Greentech case). The Facts of the Oswal Greentech case were as follows Mr Abhay Oswal (The Deceased) held 5,35,30,960 Shares in the Company. In 2015 the deceased filed a nomination under Section 72 of Companies Act,2013 in favour of Mrs Aruna Oswal (Nominee). After the death of the deceased the nominee filed for registration of the shares in her name and the same was granted. Thereupon Mr Pankaj Oswal (Legal Heir) filed a suit for partition in the High Court of Delhi for grant of 1/4th of the share in property in 2017.

While this suit was pending before the Delhi High Court, the Legal Heir filed another suit before the National Company Law Tribunal Claiming that the Company was acting in contravention of the laid down law and was engaging in acts of oppression and mismanagement. However, the condition for filing such a petition is that the Petitioner should have a 10% shareholding in the company and in the instant case the Legal Heir only had 0.33% shareholding.

The Legal Heir raised the contention that he was one of the Four Heirs of the Deceased and therefore he was entitled to a shareholding which was in excess of the requisite 10%. The NCLT Accepted this contention and held the case to be maintainable. Therefore, the Company filed an appeal with the NCLAT, claiming that as per conjoined reading of Section 72(1) & (3) of Companies Act, 2013 which is a non-obstante clause the contention raised by the legal heir is invalid and the petition is not maintainable.

The Appellants placed reliance on the decision of the Delhi High Court : ***Dayagen Private Limited v. Rajendra Dorian Punj,*** wherein the Court placed reliance on the Special law i.e. Companies Act and held it to override the General Law i.e. Law of Succession and stated that Section 72 overrides the general law of succession and confers upon the nominee, in respect of the shares, absolute and exclusive ownership rights.

However, the NCLAT took a contrary view and placed reliance on the landmark judgement of the Supreme Court in the Decision of ***World Wide Agencies Private Limited and Another v. Margarat T. Desor and Others***[vii], wherein the legal representatives had been given the right to maintain the application with respect to oppression and mismanagement. The NCLAT stated that *"The right arising out of an instrument does not vest with nominee automatically on the death of the original holder of the instrument. Nominee does not mean that the amount or the share belongs to the nominee. On the death of the holder of the instrument, the amount/ share vests with the legal heirs, the nominee merely holds the amount/ share herein till the matter of vesting is decided in favour of the legal heirs."*

An appeal was subsequently brought before the Supreme Court against the NCLAT order. Though addressing the issue in the Aruna Oswal v. Pankaj Oswal and Others case, the Supreme Court mainly addressed the issue of "whether the issue of inheritance of shares can be resolved under a company petition for oppression and mismanagement."

The SC noted that it was evident from the bare reading of the provisions of Section 72(1) of CA 2013 that any holder of securities is entitled, in the event of his death, to appoint any person to whom his securities are 'investing'. In the case of joint holders, they also have the right to appoint any person to whom, in the event of the death of all joint holders, 'all rights in securities shall be vested'. The SC noted that sub-section (3) of Section 72 of the CA 2013 includes a non-obstante clause in respect of anything contained for the time being in force in any other law or any provision, whether testamentary or otherwise, where there is a non-obstante clause in respect of anything contained for the time being in force in any other law.

The Supreme Court placed reliance on the decision ***Sangramsinh P. Gaekwad and Others v. Shantadevi P. Gaekwad (Dead) through LRs and Others***[viii] in which the Supreme Court had held that the dispute as to inheritance of shares is eminently a civil dispute and cannot be said to be a dispute as regards oppression and/ or mismanagement so as to attract company court's jurisdiction under Sections 397 and 398 of the Companies Act, 1956In view of the above ruling, the SC was of the opinion that, in the present case, the basis of the petition was the inheritance of one-fourth of the shareholding in order to constitute 10% of the shareholding, a right which cannot be determined in proceedings pursuant to Section 241 or 242 of the CA 2013. Therefore, the filing of a petition pursuant to Sections 241 and 242 requesting a waiver was a fallacy.

The decision of the court though it did not directly resolve the issue with respect to right of nomination viz-a-viz right of succession did establish the precedent that suits which are civil in nature cannot be instituted in other fora and they must be dealt with the civil court of competent jurisdiction.

Further though the Supreme Court did not lay down any ratio decidendi with respect to the lacuna of law under Section 72 of Companies Act the observations made by the Court do show that the Supreme Court clearly laid out the principles which governed Section 72 of the Companies Act and did draw a differentiation between Nomination under Companies Act,2013 and the nomination provided for under LIC Act, as this distinction was not drawn by the Division Bench of the Bombay High Court while deciding the case of ***Shakti Yezdani and Anr v. Jayanand Jayant Salgaonkar.*** The Supreme Court observed that Section 72 of Companies Act,2013 does not treat the nominee as merely an interim holder.

Currently the decision in the case of ***Shakti Yezdani and Anr v. Jayanand Jayant Salgaonkar*** pronounced by the Division Bench of the Bombay High Court is still valid in law and in force, but the sooner the issue is decided by the Supreme Court the better as there will be a binding authoritative take on this present lacuna which exists under Companies Act, 2013.

ENDNOTES

[i] 2010 (3) Mh. L. J 780
[ii] Notice of Motion No. 822 of 2014 in Suit No. 503 of 2014
[iii] Section 72 of Companies 2013 is in paramateria with Section 109A of Companies Act, 1956
[iv] Appeal No. 313 of 2015 in Suit No. 503 of 2014
[v] Para 34 of *Shakti Yezdani and Anr v. Jayanand Jayant Salgaonkar*
[vi] (Company Appeal (AT) No 410 of 2018)
[vii] (1990) 1 SCC 536
[viii] (2005) 11 SCC 314