

NOMINEE – BARE COLLECTOR OR EXCLUSIVE OWNER?

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ABSTRACT

They say when loving hearts are separated; it is not he who is exiled to heaven, but the survivor, who tastes the sting of death. A man's dying hence becomes more his survivors' affair than his own. Money is important; for it is a link between the present and the future. We do not exist in a utopia where sharing one's possessions is an earnest virtue. When the breadwinner dies, his family faces both personal grief and a plethora of legal troubles.

A very common practice is to appoint a nominee to one's properties. Nominee means a person appointed in the prescribed manner by a member of the fund to receive the amount which may be due to the member from the fund in the event of his death before the amount is paid to him'.¹ The word 'receive' has many connotations in different legislations where a nominee is concerned. Is he a mere holder or trustee, or is he vested

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¹P. RAMANATHAN AIYAR, *ADVANCED LAW LEXICON* (3rd ed., Wadhwa, 2005).

with rights exclusive to the other heirs? Is this differential treatment justified?

Therefore, we will discuss in detail the legal status, rights and duties of a nominee with reference to legal framework in India and in other countries. Essentially we will address the conflicting rights of nominee as under the Insurance Act, 1938 and what the family goes through when the person dies interstate, fails to update his will, when the will is not congruous with the testamentary disposition or, most importantly, whether different rights granted violates the essence of equality are all questions pertaining to such hassles. The paper shall enumerate the legal nuances relating to the subject matter.

I. NOMINEE UNDER SECTION 39 OF THE INSURANCE ACT, 1938

A. Object of the Act

Insurance is a contract wherein one party agrees to pay a sum to another upon happening of a contingency in the duration of human life. The primary function of insurance is to ensure equitable distribution of financial losses of insured through which the insurer and insured are benefited.² In a recent judgment, the Rajasthan High Court held:

The very purpose and object of the assured in taking policies from the LIC is with a view to safeguard interest of his dependants, viz.,

²M.N. SRINIVASAN, PRINCIPLES OF INSURANCE LAW 4 (2006).

wife and children, as the case may be, in the event of premature death of the assured as a result of the happening of any contingency. Thus, in that event, the nominees and the dependants may not be deprived of the dues payable under the policies to them, otherwise very legislative and beneficial object for taking such policies would stand lost and defeated.³

This clarifies the object of the legislation and the impact it has after a person's death on the family and explains the reasoning behind Section 39 of the Insurance Act. It can be construed that a nominee's right is subject to all the liabilities to which the insured party is subject, and is not transferable or heritable. His position is that of a receiver and he has a bare right to collect the policy money.⁴

B. Factual Situations

The aforesaid is analogous to the present legal framework which affirms that Section 39 merely provides for a limited and not an absolute right in exclusion to all other persons. Hence, reading of this section establishes that nomination "*only indicates the hand which is authorized to receive the amount*" can be explained with reference to factual situations which illustrate how other elements also aim at curbing the residual rights of nominee.

- a) Where the Wife is the Nominee but there are Pending Claims of the Creditors – In a case before the Calcutta High Court, wife claimed her rights along with the creditors counter claim. The honourable Court held that the insurance was part of the estate and that the creditors were entitled to such policy money.
- b) Where there is a Repayment of Loan/Mortgage/Security – Though assignment automatically cancels nomination, sub-section (4) of Section 39 indicates that when the insurer bears some risk at the time of assignment in consideration for a loan granted as security within its

³Santhosh Kumar Gupta v. LIC, A.I.R. 2000 Raj 327.

⁴Ram Ballav v. Gangadhar, A.I.R. 1957 Mad 115.

surrender value or reassignment on repayment, it shall not cancel the nomination.

- c) Where the Nominee and Assured Die at the Same Time – In a situation where the assured and his brother died around the same time, the wife of the assured and nominee were left behind fighting for such money. The judge preferred the claim of the nominee’s widow because it formed a part of the nominee’s estate.
- d) Whether the Nominee can Assign the Policy against Bank Debt –It was held by the Supreme Court that the assignment by nominee of his title, right and interest in favour of a debt or any such assignment is invalid. This is because he is a custodian of the money and nothing more than that. In other words, he holds the money for the benefit of the estate of the deceased assured.
- e) Whether a Portion of the Debt can be Assigned – The assignment is always held to be good in equity and passes property in that portion of the debt. In enforcing such a claim, it would be necessary to implead the owner of the other portion but apart from that there is no other objection in equity.
- f) Assured of a Life Insurance Policy Dies Intestate Leaving Behind him his Mother, his Widow, and a Son, but for the Purpose of Section 39 has Nominated his Widow alone –
- i. *Sarabati Devi Case*⁵ – A Judicial Landmark: The respondent, Usha Devi, the widow of one Jagmohan Swaroop, contested the suit claiming that she has the absolute right to the amounts to the exclusion of her son and her mother-in-law. The argument put forth in this case was whether the nominee gets an absolute right to the amount due under the life insurance policy on death of the assured. The Supreme Court asserted in the negative. It was held, “*The money remains property of the assured during his lifetime and forms part of his estate subject to the personal laws of*

⁵Sarabati Devi v. Usha Devi, [1984] A.I.R. 346.

*succession.*⁶ There have been few judgments in which the High Courts have taken a dissenting view but the Supreme Court has been expeditious in pronouncing a landmark judgment to this effect. In *Karuppa Gounder v. Palaniamma*,⁷ the Court held that the mother was not entitled to any portion of the insurance amount and the same was held in *Matin v. Mahomed Matin*.⁸ The latter has been overruled because it was a judgment prior to the amendment and the former has been overruled by the *Sarabati Devi case* itself. Reference has also been made to the observance of the Madras High Court suggesting that in case of a joint family it cannot be construed that the money will be divided among all the coparceners if the assured has expressly named his wife or children as his nominees irrespective of the fact that the premium paid was out of the funds of the entire family fund.

II. CORPORATE LAWS IN INDIA

In comparison to the insurance provisions, one line of thought that the Corporate laws hold shows a striking difference. Corporate laws which have reference to ‘nominee’ are – the Depositories Act, Government Securities Act, Security Exchange Board of India Act and most importantly the Companies Act. These Acts confer an exclusive right to the nominee of a share holder and make him the sole owner of the property after the death of the share-holder.

The status of the nominee even in the Companies Act was very contentious prior to 1999 when the amendment to this provision came into force. There have been a number of cases pointing out the

⁶Similar views have been held by both Madras High Court in *D. Mohanavelu Mudaliar v. Indian Insurance and Banking Corp. Ltd.*, [1957] 27 CompCas. 47 and Andhra Pradesh High Court in *M. Brahmamma v. Venkataramana Rao*, [1958] CompCas 57.

⁷*Karuppa Gounder v. Palaniamma*, A.I.R. 1963Mad 245.

⁸*Matin v. Mahomed Matin*, A.I.R. 1922 Lah145(Z14).

lacunae in section 39 of Insurance Act. One of the many issues pertaining to the same has been addressed in the following case laws:

1. In a matter before the Company Law Board it was observed that the deceased owned 33% of the company's shares and that had to be divided among 8 claimants of the family. It took months of litigation for the family to come to a settlement despite there being a Will. As of today, the company has also offered to consider the transmission of shares in case all the eight legal heirs agree for the suitable distribution of shares. By this amendment, the company aims its duties with regard to the nominee.
2. In a matter before the Company Law Board case⁹ it was held, "*The legal representative shall not have the status of member unless his name is entered in the register of members, as already stated*". This hampers the interest of the representative because it does not give him exclusive rights and is contrary to what is mentioned in Section 109. The view that the representative is not entitled to the rights merely because he is not an existing member is not a sound judicial proposition. Hence, the amendment aims at conveying certain rights to the nominee which he is otherwise being deprived of.

Post the amendment, SEBI came out with a report¹⁰ stating the causes for the amendment and clearly analysed the scope of Section 109A of the Companies Act, 1956 and such other provisions relating to the nominee. It refers to the problems faced by the investors, like, producing the probate of the will, obtaining surety or a NOC (No-Objection Certificate) from all the legal heirs, issuance of advertisement in the newspaper and in case the investor dies intestate, the applicant has to follow a cumbersome procedure and this process may sometimes exceed the value of shares. To quote the report in respect of this particular amendment, it says:

⁹Hemendra Prasad Barooah and Anr v. Bahadur Tea Company Co. P. Ltd., [1991] 70 CompCas 792(Gau).

¹⁰SEBI, *Report and Recommendations of the Group on Transmission of Shares* (Aug. 4, 2011), <http://www.sebi.gov.in/commreport/rep140807.pdf>.

Nomination is a very effective remedy to the situation. Once a share holder appoints a nominee, then as per the law, the company's liability towards the event stands discharged and that is the intention behind inserting such provisions. The facility of nomination is intended to make the company law in tune with the present day economic policies of liberalization and deregulation. This is also intended to promote investors' confidence in capital market and to promote the climate for inter corporate investment in the country.

This reflects the object of the legislation or in this case, objective to amend this section.

The High Courts in various cases suggesting status of nominee vis-a-vis the legal heir have taken Sarbatti Devi as a precedent relying on the ratio that “*nomination doesn't have the effect of conferring beneficial interest*” even in non-insurance contexts. But the Bombay High Court¹¹ in *Harsha Nitin Kokate case* has brought about a revelation by holding a view that:

Nomination under Section 109A of the Act does not entail mere payment of the amount of shares. It specifically vests the property in the shares in the nominee, in the event of the death of the holder of the shares. The analogy drawn from the judgment in the case of Sarbatti Devi is completely misplaced on the basis of difference in the language used in both the statutes and also the object of both the Acts.

III. GLOBAL SCENARIO

The rights bequeathed on a nominee by an insurance policy under the Indian legislations are restrictive in nature. However a strikingly different standpoint can be witnessed in many other countries as far as

¹¹Harsha Nitin Kokate v. Saraswat Co-op Bank Ltd. and Ors., [2010] SCC OnLine Bom 615.

the status of a nominee is concerned. Further the paper shall entail the statutory provisions of insurance nomination law and the rights conferred on a nominee on a comprehensive level along with that we shall also draw a divergence to our existing law.

A. Singapore

Under the Singaporean law there are two types of nominations: Trust nomination and revocable nomination, which accordingly confer different rights on the nominee which is at the discretion of the policy holder/insured unlike the Indian insurance where nominee is given a very insignificant role as far as the policy proceeds are concerned.

In a trust nomination the policy holder relinquishes all his policy rights and all the policy proceeds including both the death and living benefits belong to the nominee however the policy holder can reclaim the benefits with the consent of all the nominees. And only the spouse or a child of the policyholder is eligible to become a nominee.

In a revocable nomination, the policy holder retains full rights and ownership over the policy which includes changing or revoking a nomination at any point of time with or without the consent of the nominees. Only the death benefits can be accrued to nominee while the living benefits shall be accredited to the policy holder himself.

B. Common Law of England

The law in force has summarized this litigious issue on nomination in the Halsbury's Laws of England. There have been periodical changes in the position of nominee from making him a mere agent to an absolute beneficiary and then again an agent.

Firstly, nominee in this context becomes a third party because he is not privy to the contract which is in fact between the insurer and the insured. The policy money payable on the death of the assured may be expressed to be payable to a third party and the third party is then prima facie merely the agent for the time being of the legal owner and has his authority to receive the policy money and to give a good

discharge; but he generally has no right to sue the insurers in his own name. However, unless and until they are otherwise directed by the assured's personal representatives the insurers may pay the money to the third party and get a good discharge from him.¹²

In the later stages of development of the insurance industry, the attitude towards this issue has changed, and the nominee whose name is included in the proposal form would be regarded as an absolute beneficiary under the policy.¹³

Notwithstanding these developments, there was a paradigm shift from the aforementioned position wherein it was stated that “nomination does not, however, by itself, constitute the assured a trustee, nor, since the person nominated is a stranger to the contract, has he any remedy at law. The property in such a policy will therefore, pass notwithstanding the nomination, to the personal representatives of the assured on his death and the nominee has no rights whatsoever.”¹⁴ Besides the Common law of England and India, there are a substantial number of countries following a similar legal approach like United States of America and Australia.

C. *Islamic Law*

The nominee is a trustee and the governing principles of nominee under Islamic law could be derived from the doctrine of *al-amanah* which means reliability, trustworthiness, good faith, faithfulness, honesty, and fidelity.¹⁵ There are differences of opinion among the practitioners as well as Islamic scholars. Some claim that a nominee in an insurance policy should be regarded as the owner of the policy

¹²HALSBURY'S LAWS OF ENGLAND, Vol. 25, ¶579 (4th ed.).

¹³B.N.BANERJEE, LAW OF INSURANCE, Volume 1, 393 (4th ed., The Law Book Company Pvt. Ltd.) (1994),.

¹⁴D.Mohanavelu Mudaliar Alias D. v. The Indian Insurance and Banking, [1956] 2 MLJ 476.

¹⁵COWEN, J. MILTON, A DICTIONARY OF MODERN WRITTEN ARABIC, 278 (Hanossowitz, Wiesbadean, 1961).

who must have absolute right to be the beneficiary over the policy.¹⁶ The reasoning behind this is that policy holder pays the premiums and owing to principles of fair distribution i.e. *al-mirath* and *al-wasiyah*, the legal heirs are entitled to the policy benefits and not the nominee. The contrary view though existent but not accepted is that an insurance policy is *al-hibah* which is a gift given to the nominee by the assured which makes him an absolute beneficiary so as to enjoy perpetual ownership.

IV. CRITICAL ANALYSIS BASED ON DIFFERENTIAL TREATMENT

Let's consider a situation. A father dies intestate leaving behind immovable property, life insurance policy worth Rs 5 lakhs payable to A (nominee), and B as the nominee for shares valued at Rs 10 lakhs. In the given instance, A and B are brothers. The grievance that arises is that why A should pay a part of the insurance policy upon receipt of the nomination money on the death of the father to B as it is liable for partition but B can enjoy the entire value of shares individually as shares are not liable for partition? Is there a violation of Article 14 of the Indian Constitution? Why two legislations provide for different scope of the term nominee? How differently are they worded and how different are they as a matter of principle?

An in-depth analysis of the language used in the statutes discussed above and others will lead to following conclusions. Welfare legislations like The Payment of Gratuity Act, 1972 and The Employees Provident Fund and Miscellaneous Provisions Act, 1952 specifically require that a family member should be appointed as the nominee and no outsider is entitled to the money even if there is an

¹⁶Prof. Dr. Mohd. Ma'sum Billah, *Effect of 'Nomination in Life Policy' Insurance vs. Takaful Practices* (Aug. 4, 2011), http://www.panoramassicurativo.ania.it/get_file.php?id=14516.

outstanding credit. The member also has the discretion to decide before hand, the distribution of money between the survivors. The purpose of these enactments is to gratify the survivors of the deceased and hence this differentiates it from the Insurance Act, 1938 where one can even hold the policy as a security against debt. This makes it clear that Insurance Act is not just welfare legislation though it has almost the same objective.

The Public Debt Act, 1944 which is in consonance with the Companies Act, 1956 on this point confers on the nominee a vested right in exclusion to all other persons. The object of these enactments, as already mentioned, is to discharge the company/government, of its duties in order to expedite its work in the other respects. The same goes with The Cooperative Societies Act, 1912 which by default registers the nominee as a member on death of the actual member conferring upon him rights as if he is the member himself. Comparatively, they are materially distinct from the Insurance Act because this act came into force with a purpose to protect the survivors of the deceased and it is to note that inspite of being introduced in 1938 there haven't been any amendments to this effect.

V. CONSTITUTIONAL VALIDITY

Article 14 quotes equality before law but that doesn't mean that un-equals ought to be treated equally. All persons are not equal by nature and circumstances and this leads to classification among different groups of persons and differentiation between these classes.¹⁷ The question is whether the classification is reasonable or not. Here, the conflict is between the differential positions of a nominee. It is well established that in the absence of definition in the statute the words occurring will have to be understood with reference to objects of the

¹⁷PROF. M.P. JAIN, INDIAN CONSTITUTION LAW (5th ed., Lexis Nexus Butterworths, 2005).

Act and in the context in which they occur.¹⁸ Sometimes one finds two or more enactments operating in the same field and each containing a non-obstante clause. The conflict in such cases is resolved on consideration of purpose and policy underlying the enactments and the languages used in them.¹⁹

The object of the Insurance act is to assure that the survivors of the assured are being benefited by the insurance amount and the reason behind the amendment in the Companies Act or the other Acts mentioned is to get discharged of the duties. This affirms that there is a rational nexus with the object of the statute and hence this cannot be held arbitrary under Article 14 of the Constitution.

It is settled law that differentiation is not always discriminatory.²⁰ And if the purpose of the statute is achieved, then it does not violate the principles of Article 14 of the Constitution. Therefore, mere differentiation or inequality of treatment does not per se amount to discrimination within the inhibition of the equal protection clause.²¹

In conclusion to the above it is safe to say that Insurance Act and Companies Act are two enactments independent of each other and hence generalising the provisions of both on a level playing field will be unjust to the intention of the legislation.

VI. RECOMMENDATIONS

Having explained the various facets of a nominee, it is however not expected of a layman to understand the intricacies of law and the depth of such provisions. These are a few recommendations not only for the unwary investors but also for the property holders who leave

¹⁸D.P. MITTAL, INTERPRETATION OF STATUTES (2nd ed.).

¹⁹JUSTICE G.P. SINGH, PRINCIPLES OF STATUTORY INTERPRETATION (8th ed., Wadhwa and Company, 2001).

²⁰Union of India v. M.V.Valliappan, [1999] 6 SCC 259,269.

²¹K.Thimmappa v.Chairman, Central Board Of Directors, A.I.R. 2001 SC 467.

behind a lot many mouths to be fed after their death. Keeping in mind the need of the hour, we would find it apt to make certain recommendations.

A. Make a Will

When a person is well aware that his property can be a bone of contention among his children, however happy a family it is, by not making a will he shall only make relations sour amongst the legal heirs. A standing example in the Indian Commerce Industry will be the feud between the Ambani brothers which caused a lot of imbalance in the family, reliance industry, the share markets and the impact it had on the government cannot be overlooked. Hence it is submitted that differences which can at a later stage cause a menace should be nipped in the bud by making a proper testamentary disposition.

B. Update the Will

It is not only enough to make the will but keep it updated with the recurring changes in law and personal life. This measure of family welfare becomes an instrument of social strife and tears off the family fabric. One family member receives the money as a nominee and the other brothers and sisters want to share it. The mother of the deceased receives the money and the wife and the children are deprived of it. The wife receives the claim and the dependant mother does not get a share in it. The widow after getting of the claim money gets remarried leaving the children with the husband's family. These hard facts of life must be faced and hence one should write a solution to them during one's lifetime rather than leaving them unsettled and causing greater trauma and agony to the family subsequently. All these conditions are clearly avoidable through proper nomination on policies.²²

²²*Nominate Your Policy Correctly* (Aug. 6, 2011), <http://www.insuremagic.com/CONTENT/Articles/Life/nomination.asp>.

C. Appointment of a Nominee

If the nominee is a minor, a person who is a major should be appointed as an appointee and also a person who has an insurable interest in you should be nominated. Nominees should preferably be the legal heirs or a person in who trust is reposed to ensure the fair distribution to the real heirs.

D. Inputs from the Singaporean Laws of Insurance

As already stated, Singaporean laws of insurance ensure that the discretion lies with the policy holder to confer the rights and its extent. By giving an option to the policy holder it gives him the opportunity to make his own decision of whether he wants the nominee to be a mere agent or beneficiary and also bars the statute from providing a general clause.

E. Law Commission Report

The authors second the recommendations put forth by the Law Commission in its 190th Report²³ as regard the suggested amendment of Section 39 of the Insurance Act which is as follows. Recommendations of the Law Commission may be summarized as:

1. A clear distinction be made in the provision itself between a beneficial nominee and a collector nominee.
2. It is not possible to agree to the suggestion made by some of the insurers that in all cases the payment to the nominee would tantamount to a full discharge of the insurer's liability under the policy and that unless the contrary is expressed, the nominee would be the beneficial nominee.
3. An option be given to the policyholder to clearly express whether the nominee will collect the money on behalf of the legal representatives

²³Law Commission of India, *The Revision of the Insurance Act, 1938 and The Insurance Regulatory and Development Authority Act, 1999* (Aug. 4, 2011), <http://lawcommissionofindia.nic.in/reports/InsuranceReport-2nddraft1.pdf>.

(in other words such nominee will be the collector nominee) or whether the nominee will be the absolute owner of the monies in which case such nominee will be the beneficial nominee.

4. A proviso be added to make the nomination effectual for the nominee to receive the policy money in case the policyholder dies after the maturity of the policy but before it can be encashed.

F. Must Do's for Shareholders

Shareholders should regularly update their nomination of shares pro rata to the percentage mentioned in the will as nomination under Section 109A of the Companies Act, 1956 has an overriding effect on any kind of testamentary disposition. Every investor or policy holder should compulsorily propose a nominee as it eases the burden of producing thousands of documents after the death of the policy holder relating to the certification of succession, letters of administration, probate of will which are cumbersome, costly and time consuming which otherwise has to be borne by the survivors of the deceased.

VII. CONCLUSION

The position of the nominee is one that has different legal status under various legislations. This does not imply unequal treatment to people who come under such legislations or create special benefits for them. It is to be noted that the essence of these provisions are its very objective and amending them will hamper the intent of the legislation in making such provisions. Enhancing the status of nominees under the respective enactments would help comprehensively than just mere introducing amendments to bring everyone under the same footing.