

EN BANC

G.R. No. 207161 – Y-1 LEISURE PHILIPPINES, INC., YATS INTERNATIONAL LTD., AND Y-1 CLUBS AND RESORTS, INC., Petitioners, v. JAMES YU, Respondent.

Promulgated:

September 8, 2015

X-----*[Signature]*-----X

CONCURRING OPINION

LEONEN, J.:

I concur in holding petitioners Yats International Ltd., Y-1 Leisure Philippines, Inc., and Y-1 Clubs and Resorts, Inc. liable to refund respondent James Yu's investment of ₱650,000.00 with legal interest.

The facts, as summarized in the ponencia,<sup>1</sup> involve a creditor's claim against a corporation that sold all or substantially all of its assets to another corporation. Respondent James Yu filed a collection suit against Mt. Arayat Development Co. Inc. (MADCI) and its then President Rogelio Sangil for the ₱650,000.00 respondent James Yu invested in shares of MADCI's golf and country club project in Arayat, Pampanga that turned out to be non-existent.<sup>2</sup> He later amended his Complaint to implead petitioners after he had discovered that MADCI had already sold substantially all of its assets to petitioners.<sup>3</sup> The Regional Trial Court held that MADCI and Rogelio Sangil are solidarily liable to pay respondent James Yu's claim for refund, but dismissed the case against petitioners.<sup>4</sup> The Court of Appeals affirmed the trial court with modification in that petitioners are also liable to satisfy respondent James Yu's claim considering the transfer of MADCI's entire assets to petitioners.<sup>5</sup> The ponencia affirmed the Court of Appeals Decision in toto.<sup>6</sup>

The Regional Trial Court found that MADCI did not deny its contractual obligation with respondent James Yu.<sup>7</sup> The issue before us involves the liability of petitioners as purchasing corporations.

<sup>1</sup> Ponencia, pp. 2-6.

<sup>2</sup> Id. at 2; *Rollo*, pp. 32 and 61.

<sup>3</sup> Ponencia, p. 3; *Rollo*, pp. 35 and 64.

<sup>4</sup> *Rollo*, p. 76.

<sup>5</sup> Ponencia, p. 6; *Rollo*, pp. 53-54 and 56.

<sup>6</sup> Ponencia, p. 20.

<sup>7</sup> Id. at 5; *Rollo*, p. 72.

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Jurisprudence<sup>8</sup> reiterates this court's ruling in *Edward J. Nell Company v. Pacific Farms, Inc.*<sup>9</sup> that:

Generally where one corporation sells or otherwise transfers all of its assets to another corporation, the latter is not liable for the debts and liabilities of the transferor, except: (1) where the purchaser expressly or impliedly agrees to assume such debts; (2) where the transaction amounts to a consolidation or merger of the corporations; (3) **where the purchasing corporation is merely a continuation of the selling corporation**; and (4) where the transaction is entered into fraudulently in order to escape liability for such debts.<sup>10</sup> (Emphasis supplied)

The four exceptions enumerated find basis from the Civil Code and Corporation Code.<sup>11</sup> The third exception grounds on Section 40 of the Corporation Code governing the sale or other disposition of assets.

This provision requires the ratificatory vote of the stockholders representing at least two-thirds of the outstanding capital stock when the transaction amounts to a sale of “all or substantially all of [the corporation’s] property and assets.”<sup>12</sup> It contemplates a transfer of the entire business enterprise<sup>13</sup> since no such ratificatory vote is required if the sale or other disposition of property and assets “is necessary in the usual and regular course of business”<sup>14</sup> or “if the proceeds of the sale or other disposition of such property and assets be appropriated for the conduct of its remaining business.”<sup>15</sup> Thus, the scenario involves a purchaser corporation continuing the business of a seller corporation that no longer conducts such specific

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<sup>8</sup> See *Philippine National Bank v. Andrada Electric & Engineering Company*, 430 Phil. 882, 893 (2002) [Per J. Panganiban, Third Division] and *McLeod v. National Labor Relations Commission*, 541 Phil. 214 (2007) [Per J. Carpio, Second Division].

<sup>9</sup> 122 Phil. 825 (1965) [Per J. Concepcion, En Banc].

<sup>10</sup> Id. at 827.

<sup>11</sup> See discussion in J. Leonen, Dissenting Opinion in *Bank of Commerce v. Radio Philippines Network, Inc.*, G.R. No. 195615, April 21, 2014, 722 SCRA 520, 607–622 [Per J. Abad, Third Division].

<sup>12</sup> CORP. CODE, sec. 40.

<sup>13</sup> See Cesar Villanueva, PHILIPPINE CORPORATE LAW 679–680, 682, 686, 692–693 (2010), cited in J. Leonen, Dissenting Opinion in *Bank of Commerce v. Radio Philippines Network, Inc.*, G.R. No. 195615, April 21, 2014, 722 SCRA 520, 617 [Per J. Abad, Third Division], for its discussion on the three levels of Corporate Acquisitions and Transfers, namely: (1) pure assets-only transfer; (2) transfer of the business enterprise; and (3) equity transfer. It discussed that in a pure assets-only transfer, “the purchaser is only interested in the ‘raw’ assets and properties of the business, perhaps to be used to establish its own business enterprise or to be used for its on-going business enterprise.” In a transfer of business enterprise, “[t]he purchaser’s primary interest is to obtain the ‘earning capability’ of the venture.” An equity transfer is when “[t]he purchaser takes control and ownership of the business by purchasing the controlling shareholdings of the corporate owner.” In this case, “[t]he control of the business enterprise is therefore indirect [as] the corporate owner remains the direct owner of the business, and what the purchaser has actually purchased is the ability to elect the members of the Board of Directors of the corporation which runs the business.”

For the first and third type, the transferee shall not be liable for the debts and liabilities of the transferor except where the transferee expressly or impliedly agrees to assume such debts. The second type, the transfer of business enterprise, makes the transferee liable for the transferor’s liabilities.

<sup>14</sup> CORP. CODE, sec. 40.

<sup>15</sup> CORP. CODE, sec. 40.

business.

*Caltex (Phils.), Inc. v. PNOC Shipping & Transport Corp.*<sup>16</sup> discussed this third exception in holding that even without the Agreement of Assumption of Obligations, respondent was still liable to petitioner since “[t]he acquisition by the assignee of all or substantially all of the assets of the assignor necessarily includes the assumption of the assignor’s liabilities, unless the creditors who did not consent to the transfer choose to rescind the transfer on the ground of fraud.”<sup>17</sup>

Corporation law provisions and concepts reflect a concern for protecting corporate creditors. The trust fund doctrine,<sup>18</sup> for example, provides that “subscriptions to the capital of a corporation constitute a fund to which creditors have a right to look for satisfaction of their claims and that the assignee in insolvency can maintain an action upon any unpaid stock subscription in order to realize assets for the payment of its debts.”<sup>19</sup>

Section 43 of the Corporation Code provides that the Board of Directors may declare dividends only from unrestricted retained earnings.<sup>20</sup> The term “unrestricted retained earnings” substituted the old Corporation Code’s wording of “surplus profits arising from its business.”<sup>21</sup>

Section 122 of the Corporation Code on liquidation also provides that “[e]xcept by decrease of capital stock and as otherwise allowed by this Code, no corporation shall distribute any of its assets or property except upon lawful dissolution and after payment of all its debts and liabilities.”<sup>22</sup>

The provisions of law, and as applied and interpreted in jurisprudence, shape and govern the legal fiction of corporations. For one, the law vests in corporations a personality separate and distinct from those that represent them.<sup>23</sup> This separate personality, among other key features, sets the

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<sup>16</sup> 530 Phil. 149 (2006) [Per J. Carpio, Third Division].

<sup>17</sup> Id. at 159–160.

<sup>18</sup> The American case of *Wood v. Dummer* (3 Mason 308, Fed Cas. No. 17, 944) first enunciated this doctrine, which was later adopted in this jurisdiction with *Philippine Trust Co. v. Rivera*, 44 Phil. 469, 470 (1923) [Per J. Street, En Banc]. This was discussed in *Halley v. Printwell, Inc.*, 664 Phil. 361, 382 (2011) [Per J. Bersamin, Third Division].

<sup>19</sup> *Halley v. Printwell, Inc.*, 664 Phil. 361, 382–383 (2011) [Per J. Bersamin, Third Division], citing *Velasco v. Poizat*, 37 Phil. 802 (1918) [Per J. Street, En Banc].

<sup>20</sup> CORP. CODE, sec. 43.

<sup>21</sup> *Republic Planters Bank v. Hon. Agana, Sr.*, 336 Phil. 1, 10 (1997) [Per J. Hermosisima, Jr., First Division].

<sup>22</sup> CORP. CODE, sec. 122.

<sup>23</sup> *Solidbank Corporation v. Mindanao Ferroalloy Corporation*, 502 Phil. 651, 664 (2005) [Per J. Panganiban, Third Division], citing *Monfort Hermanos Agricultural Development Corporation v. Monfort III*, 478 Phil. 34, 42 (2004) [Per J. Ynares-Santiago, First Division], *Spouses Firme v. Bukal Enterprises and Development Corporation*, 460 Phil. 321, 345 (2003) [Per J. Carpio, First Division], and *People’s Aircargo and Warehousing Co. Inc. v. Court of Appeals*, 357 Phil. 850, 863 (1998) [Per J. Panganiban, First Division].

“economic superiority”<sup>24</sup> of a corporate legal structure among other business associations.<sup>25</sup> This attracts investors by allowing small capital contributors to be part of a big business endeavor through the aggregation of their capital funds, and by limiting their liability since corporate assets will answer for corporate debts.<sup>26</sup> However, this legal structure should not be abused.

While a separate corporate personality shields corporate officers acting in good faith and within their scope of authority from personal liability, law and jurisprudence<sup>27</sup> enumerate exceptions<sup>28</sup> to this rule, such as “gross negligence or bad faith [by directors] in directing the affairs of the corporation”<sup>29</sup> when established by clear and convincing evidence.<sup>30</sup> This court has also disregarded the separate personality of corporations by applying the doctrine of piercing the corporate veil in the following instances:

[T]he doctrine of piercing the corporate veil applies only in three (3) basic instances, namely: a) when the separate and distinct corporate personality defeats public convenience, as when the corporate fiction is used as a vehicle for the evasion of an existing obligation; b) in fraud cases, or when the corporate entity is used to justify a wrong, protect a fraud, or defend a crime; or c) is used in alter ego cases, i.e. where a corporation is essentially a farce, since it is a mere alter ego or business conduit or a person, or where the corporation is so organized and controlled and its affairs so

<sup>24</sup> See Paddy Ireland, *Limited liability, shareholder rights and the problem of corporate irresponsibility*, Cambridge Journal of Economics 837, 838 (2010) <<http://cje.oxfordjournals.org/content/34/5/837.full.pdf+html>> (visited July 9, 2015).

<sup>25</sup> See *Pioneer v. Morning Star*, G.R. No. 198436, July 8, 2015 [Per J. Leonen, Second Division].

<sup>26</sup> See *Pioneer v. Morning Star*, G.R. No. 198436, July 8, 2015 [Per J. Leonen, Second Division].

<sup>27</sup> See *Edsa Shangri-La Hotel and Resort, Inc., et al. v. BF Corporation*, 578 Phil. 588, 607 (2008) [Per J. Velasco, Jr., Second Division], *Aratea v. Suico*, 547 Phil. 407, 415–416 (2007) [Per J. Garcia, First Division]; *Solidbank Corporation v. Mindanao Ferroalloy Corporation*, 502 Phil. 651, 665 (2005) [Per J. Panganiban, Third Division], *MAM Realty Development Corp. v. National Labor Relations Commission*, 314 Phil. 838, 844–845 (1995) [Per J. Vitug, Third Division], citing *Tramat Mercantile, Inc. v. Court of Appeals*, G.R. No. 111008, November 7, 1994, 238 SCRA 14, 19 [Per J. Vitug, Third Division].

<sup>28</sup> *Solidbank Corporation v. Mindanao Ferroalloy Corporation*, 502 Phil. 651, 665 (2005) [Per J. Panganiban, Third Division], quoting *Tramat Mercantile, Inc. v. Court of Appeals*, G.R. No. 111008, November 7, 1994, 238 SCRA 14, 19 [Per J. Vitug, Third Division]. See also *Aratea v. Suico*, 547 Phil. 407, 415–416 (2007) [Per J. Garcia, First Division], quoting *MAM Realty Development Corp. v. National Labor Relations Commission*, 314 Phil. 838, 844–845 (1995) [Per J. Vitug, Third Division]:

Personal liability of a corporate director, trustee or officer along (although not necessarily) with the corporation may so validly attach, as a rule, only when —

- ‘1. He assents (a) to a patently unlawful act of the corporation, or (b) for bad faith or gross negligence in directing its affairs, or (c) for conflict of interest, resulting in damages to the corporation, its stockholders or other persons;
- ‘2. He consents to the issuance of watered stocks or who, having knowledge thereof, does not forthwith file with the corporate secretary his written objection thereto;
- ‘3. He agrees to hold himself personally and solidarily liable with the corporation; or
- ‘4. He is made, by a specific provision of law, to personally answer for his corporate action.’

<sup>29</sup> CORP. CODE, sec. 31.

<sup>30</sup> *Francisco v. Mallen, Jr.*, 645 Phil. 369, 376 (2010) [Per J. Carpio, Second Division], quoting *Carag v. National Labor Relations Commission*, 548 Phil. 581, 602 (2007) [Per J. Carpio, En Banc], emphasis supplied.

conducted as to make it merely an instrumentality, agency, conduit or adjunct of another corporation.<sup>31</sup> (Emphasis and citations omitted)

The lower courts pierced the veil of corporate fiction against Rogelio Sangil after finding that he had control of MADCI before the execution of the Memorandum of Agreement with petitioners, and he used MADCI as an alter ego to sell golf and country club shares without authority from the Securities and Exchange Commission.<sup>32</sup> He also failed to redeem shares sold to third parties like respondent James Yu as agreed upon in the Memorandum of Agreement, despite his receipt of money for this purpose, and he invoked MADCI's separate personality to evade this existing obligation.<sup>33</sup> These acts, in abuse of the corporate legal fiction, resulted in the injury of investors and creditors such as respondent James Yu.

The third exception laid down in *Edward J. Nell Company v. Pacific Farms, Inc.*<sup>34</sup> falls under this framework of providing protection for corporate creditors and consequently encouraging investments in support of economic development.

The ponencia discussed the factual findings supporting the conclusion that seller corporation MADCI can no longer exist as a development company for the golf course, while petitioner purchaser corporation to whom it transferred substantially all of its assets will continue its operations.<sup>35</sup>

The Court of Appeals found that the sale of MADCI's entire asset of 120 hectares of land in Pampanga rendered it incapable of continuing its golf and country club business plan.<sup>36</sup> On the other hand, petitioner purchaser corporation's President and Chief Executive Officer testified that "[petitioner corporation] bought the share[s] of stock of MADCI because it had some interest in the project involving the development of a golf course [and] [t]he petitioners then found that MADCI had landholdings in Pampanga which it would be able to develop into a golf course."<sup>37</sup>

Since the third exception applies, petitioners Yats International Ltd., Y-1 Leisure Philippines, Inc., and Y-1 Clubs and Resorts, Inc. are liable to respondent James Yu.

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<sup>31</sup> *WPM International Trading, Inc. v. Labayen*, G.R. No. 182770, September 17, 2014, 735 SCRA 297, 307–308 [Per J. Brion, Second Division].

<sup>32</sup> *Rollo*, pp. 56 and 72.

<sup>33</sup> *Id.* at 54 and 56.

<sup>34</sup> 122 Phil. 825 (1965) [Per J. Concepcion, En Banc].

<sup>35</sup> Ponencia, pp. 16–18.

<sup>36</sup> *Id.* at 17; *Rollo*, p. 52.

<sup>37</sup> Ponencia, pp. 4 and 18.

ACCORDINGLY, I vote to DENY the Petition.



MARVIC M.V.F. LEONEN  
Associate Justice