Republic of the Philippines
Supreme Court
Manila

FIRST DIVISION

JENNIFER M. ENANO-BOTE, VIRGILIO A. BOTE, JAIME M. MATIBAG, WILFREDO L. PIMENTEL, TERESITA M. ENANO, Petitioners,	**G.R. No. 223572**
- versus -	Present: PERALTA, *C.J.*, *Chairperson*, CAGUIOA, CARANDANG, ZALAMEDA, and GAERLAN, *JJ.*
JOSE CH. ALVAREZ, CENTENNIAL AIR, INC. and SUBIC BAY METROPOLITAN AUTHORITY, Respondents.	Promulgated: NOV 10 2020

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DECISION

CAGUIOA, *J.*:

Before the Court is a Petition for Review on Certiorari[1] (Petition) under Rule 45 of the Rules of Court (Rules) assailing the Decision[2] dated September 21, 2015 and Resolution[3] dated March 3, 2016 of the Court of Appeals[4] (CA) in CA-G.R. CV. No. 103619. The CA Decision affirmed the Decision[5] dated April 8, 2014 of the Regional Trial Court of Olongapo City, Branch 72 (RTC) in Civil Case No. 190-0-2004 while the CA Resolution denied petitioners' motion for reconsideration.

The Facts

The CA Decision narrates the antecedents as follows:

> On February 3, 1999, plaintiff-appellee Subic Bay Metropolitan Authority (SBMA for brevity) entered into a Lease Agreement with defendant/third-party plaintiff Centennial Air, Inc. (CAIR for brevity),

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1 *Rollo*, pp. 3-21, excluding Annexes.
2 Id. at 27-52. Penned by Associate Justice Remedios A. Salazar-Fernando, with Associate Justices Priscilla J. Baltazar-Padilla (a retired Member of the Court) and Socorro B. Inting concurring.
3 Id. at 23-25.
4 Second Division.
5 Records, Vol. 2, pp. 1199-1226. Penned by Presiding Judge Richard A. Paradeza.

represented by defendant Roberto Lozada (Lozada for brevity), for the lease of Building 8324 (subject property for brevity) located at Subic Bay International Airport (SBIA), Subic Bay Freeport Zone (SBFZ), for a period of five (5) years commencing on February 1, 1999 until midnight of January 31, 2004.

Under the pertinent provisions of the lease, the parties agreed that the monthly rental for the use and occupation of the subject property shall be payable as follows:

> "[x x x] **Section 1. Rental Payment** – The LESSEE shall pay the LESSOR the amount of Two United States Dollars and fifty cents (US$2.50) per square meter per month or Four Thousand Seven Hundred Fifty Seven United States Dollars and Fifty cents (US$4,757.50) per month or its equivalent in the Philippine Peso currency at the prevailing exchange rate at the time of payment. [x x x]"

In addition to the payment of rental, [CAIR] was also required to remit a monthly amount for the use of the facilities in relation to its operations. Concomitantly, in case of default in the fulfillment of these obligations, an additional rent charged against [CAIR] equivalent to twenty-four percent (24%) of any overdue amount was imposed. [SBMA] was also authorized to seek judicial relief for damages incurred by reason of such default as well as recovery of all amounts and penalties due under the lease contract including court costs, attorney's fees and expenses.

For the duration of the lease, [CAIR] became delinquent and was constantly remiss in the payment of its obligations. As a result, [SBMA], through its Accounting Department, sent a letter dated November 9, 1999 to [CAIR] demanding the latter to settle its outstanding obligation which, as of October 31, 1999, amounted to [₱119,324.51]. In an attempt to settle its account, [CAIR] proposed a payment scheme for its overdue debts which, as of December 31, 2002, reached [₱168,405.84]. Under this payment scheme, [CAIR] vowed to: (1) pay an initial payment of [US$33,682.00]; (2) submit [18] post dated checks to cover payment of its balance of [US$134,723.84] payable in monthly installments of [US$7,484.66]; and pay current rental starting January 2003. While the initial payment of US$33,682.00 was received, [CAIR] never delivered the 18 post dated checks to [SBMA]. Thus, on February 7, 2003, another letter was sent to [CAIR], asking the same to comply with its proposed payment scheme by submitting the 18 post dated checks for the settlement of its outstanding balance of US$134,723.84 and pay the rent for March 2003. Despite repeated demands, [CAIR] still failed to comply. On January 14, 2004, a Final Demand Letter was sent to [CAIR], requiring the latter to pay its outstanding obligation within five (5) days from receipt thereof. In the same letter, the Lease Agreement between [SBMA] and [CAIR] was terminated, and the latter was ordered to vacate the premises.

Due to the continuous refusal of [CAIR] to settle its debts, [SBMA] was compelled to file a Complaint against the former and its stockholders asking for the payment of [(1)] its outstanding obligation in the total amount of US$163,341.89 plus legal interest; (2) exemplary damages in the amount of [₱]100,000.00[;] and (3) [a]ttorney's fees in the amount of [₱]20,000.00.

Subsequently, [summonses] were served on defendants-appellants Jennifer Enano-Bote [(Jennifer for brevity)], Virgilio A. Bote [(Virgilio for brevity)], Amelita G. Simon, Teresita M. Enano, Jaime M. Matibag,[6] Wilfredo Pimentel, Vicente T. Suazo (hereinafter collectively referred to as [Enano-Bote, *et al.*] for brevity), [Lozada] and [CAIR].

On September 3, 2004, [Enano-Bote, *et al.*] filed their Answer denying any liability to [SBMA]. [They] argued that they were no longer stockholders of the corporation at the time the Lease Agreement was executed between [CAIR] and [SBMA] on February 3, 1999. Allegedly, on December 1, 1998, they entered into a Deed of Assignment of Subscription Rights ([DASR)] for brevity) with third-party defendant-appellee Jose Ch. Alvarez (Alvarez for brevity), whereby they assigned, transferred, and conveyed their aggregate subscription of [400,000] shares, representing [100%] of the outstanding capital stock of [CAIR], in favor of [Alvarez]. Pursuant to the [DASR], [Alvarez] was obliged to transfer and assign 76,000 and 4,000 of fully paid and non-assessable shares of the corporation to [Jennifer] and [Virgilio]. Furthermore, [Alvarez] assumed to pay the unpaid balance of their subscriptions in the amount of [₱30,000,000.00]. In effect, only [Jennifer] and [Virgilio] remained as nominal stockholders of the corporation while the rest of them were totally divested of their corporate shares. Since they ceased to be stockholders of the corporation, they were no longer parties to the Lease Agreement, thus they cannot be held liable for any breach thereof.

On September 27, 2004, [Lozada] filed his Answer with Counterclaim alleging that: [SBMA] has no cause of action against [Enano-Bote, *et al.*] because its cause of action was barred by the Statute of Limitations; the obligation set forth in the complaint had been paid, waived, abandoned or otherwise extinguished; and that there was novation, compensation, confusion or remission of debt which extinguished the obligation. By way of compulsory counterclaim, he prayed for the payment of attorney's fees and expenses of litigation in the amount of [₱]50,000.00, as well as exemplary damages in the amount of [₱]200,000.00 in view of the filing of the unfounded and unmeritorious claim against them.

On February 4, 2005, [CAIR] was declared in default for failure to file an answer. However, such order was lifted on June 15, 2006, and [CAIR] was allowed to adopt "*en toto*" the answer filed by [Lozada].

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[After the preliminary and pre-trial conferences], trial ensued.

[SBMA] presented Editha Lim-Marzal[, the Division Chief of the Accounting Department, Account Receivables Division of SBMA,[7]] and Kenneth Lemuel G. Rementilla[, the Manager of the Locator's Registration and Licensing Department of SBMA,[8]] as its witnesses.

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After [SBMA] rested its case, [CAIR] filed a Demurrer to Evidence, which the [RTC] subsequently denied for lack of merit.

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6 Appears as "Jaime M. Mabitag" in some parts of the records.

7 *Rollo*, p. 34.

8 Id. at 35.

Meanwhile, defendants-appellants [Jennifer], [Virgilio], Jaime M. Matibag, Wilfredo L. Pimentel and Teresita M. Enano ([petitioners for brevity]), with leave of court, filed a Third[-]Party Complaint against [Alvarez]. In their complaint, they admitted that they were the incorporators of [CAIR] when it was incorporated on December 29, 1997. On December 1, 1998, they executed [the DASR] in favor of [Alvarez] covering their entire shares of stock in [CAIR]. Among the conditions of this transfer was [Alvarez's] undertaking to relieve each of them from the payment of their remaining unpaid subscriptions to the corporation. Moreover, in consideration of the assignment, [Alvarez] also agreed to transfer and assign 76,000 and 4,000 fully paid and non-assessable shares to [Jennifer and Virgilio]. Thus, with the exception of [Jennifer and Virgilio], who remained as nominal stockholders of the corporation, the rest of them were totally divested of their corporate shares and were thereafter relieved from paying their unpaid subscriptions as a consequence of the assignment. When the Lease Agreement was executed between [SBMA] and [CAIR] on February 1, 1999, [petitioners] were no longer the majority stockholders of the latter. At that time, it was [Alvarez] who stood as the President and the authorized representative of [CAIR]. As such, he alone should be held liable for the payment of their unpaid subscription which would cover the unpaid rentals of the corporation.

On June 25, 2008, [s]ummons was issued upon [Alvarez]. On July 18, 2008, the latter filed his Third-Party Answer with Counterclaim, reiterating the same defenses raised in the answer filed by [Lozada] in the main case.

[The preliminary and pre-trial conferences for the third-party complaint ensued.]

In the interim, [petitioners] filed a Request for Admission addressed to [Alvarez], asking, among others, for the latter to admit the genuineness of the [DASR] dated December 1, 1998, Minutes of the Special Meeting of the Board of Directors of [CAIR] held in December 1998, and the Lease Agreement dated February 3, 1999. On September 24, 2009, [Alvarez] filed his Answer to Request for Admission and denied all the allegations set forth in said request. On even date, [SBMA] commented [thereon], declaring the same to be inappropriate for being a repetition of the claims stated in [petitioners'] previous pleadings. In resolving this pending incident, the [RTC] in its September 22, 2010 Order, echoed the comment of [SBMA], holding that a response to the request for admission is no longer required since the allegations therein were mere reiteration of the statements in the third-party complaint. The same has been effectively denied in the third-party answer filed by [Alvarez].

Significantly, at the continuation of the trial, only [Jennifer] was presented as a witness x x x.

[CAIR] did not present any evidence. On the other hand, [Alvarez] was given several opportunities to present his evidence but he still failed to do so, thus he was deemed to have waived his right.

On April 8, 2014, the [RTC] issued [its] Decision. [The dispositive portion of which, states:

> **WHEREFORE**, in light of the foregoing, judgment is hereby rendered **ORDERING:**

1. Defendant corporation Centennial Air, Inc. and individual defendants Jennifer M. Enano-Bote, Virgilio A. Bote, Jaime M. Matibag, Wilfredo L. Pimentel, Teresita M. Enano, Vicente Suazo and Amelita G. Simon jointly and severally to pay plaintiff SBMA the total amount of US$ 163,341.89, plus legal interest;

2. Third-party defendant Jose Ch. Alvarez to refund/reimburse to individual defendants Jennifer M. Enano-Bote, Virgilio A. Bote, Jaime M. Matibag, Wilfredo L. Pimentel, Teresita M. Enano, Vicente Suazo and Amelita G. Simon the total amount of US$ 163,341.89, plus legal interests, to be paid by the latter to the plaintiff SBMA;

3. Third-party defendant Jose Ch. Alvarez to pay third-party plaintiff Jennifer M. Enano-Bote the amount of three hundred thousand (P300,000.00) pesos by way of moral damages and the amount of two hundred thousand (P200,000.00) pesos as attorney's fees; and

4. The case as against defendant Roberto Lozada is dismissed for lack of merit.

SO ORDERED.[9]]

[Petitioners then appealed to the CA.][10]

Ruling of the CA

The CA in its Decision[11] dated September 21, 2015 denied the appeal of petitioners. The dispositive portion thereof states:

> **WHEREFORE**, premises considered, the appeal is **DENIED**. The Decision dated April 8, 2014 of the Regional Trial Court, Branch 72, in Civil Case No. 190-0-2004 is hereby **AFFIRMED**.
>
> **SO ORDERED.**[12]

Petitioners filed a motion for reconsideration[13] with the CA, which the CA denied in its Resolution[14] dated March 3, 2016.

Hence the present Petition. SBMA filed its Comment[15] dated November 24, 2016. Petitioners filed their Reply[16] dated May 26, 2017.

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9 Records, Vol. 2, p. 1226.
10 *Rollo*, pp. 29-43.
11 Supra note 2.
12 Id. at 51.
13 CA *rollo*, pp. 108-124.
14 Supra note 3.
15 *Rollo*, pp. 87-96.
16 Id. at 112-125.

Alvarez and CAIR filed a belated Comment[17] dated March 26, 2019. Petitioners filed their Reply (to the Comment dated 26 March 2019)[18] dated October 7, 2019.

The Issues

The Petition raises two main issues: (1) whether the CA committed an error of law in applying the trust fund doctrine to make petitioners personally and solidarily liable with CAIR for the unpaid rentals claimed by SBMA against CAIR because of their supposedly unpaid subscriptions in CAIR's capital stock; and (2) whether under the Third-Party Complaint, Alvarez should be made liable to independently and separately pay Jennifer and Virgilio moral damages in the amount of ₱300,000.00 and ₱200,000.00 as attorney's fees, aside from cost of suit.

The Court's Ruling

The Petition is partly meritorious.

Anent the first issue, the CA affirmed the RTC's invocation of *Halley v. Printwell, Inc.*[19] (*Halley*) to justify the application of the trust fund doctrine in this wise:

> Consistently, the [RTC] is convinced that [petitioners] may be held liable up to the extent of their unpaid subscription for the payment of [CAIR's] outstanding obligation to [SBMA]. The rationale [for] the [RTC's] rulings find support in the case of [*Halley*], which held that:
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> > "[x x x] The trust fund doctrine, first enunciated in the American case of Wood v. Dummer, was adopted in our jurisdiction in Philippine Trust Co. v. Rivera, where this Court declared that:
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> > It is established doctrine 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. (Velasco vs. Poizat, 37 Phil., 802) . . .
> >
> > We clarify that the trust fund doctrine is not limited to reaching the stockholder's unpaid subscriptions. The scope

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17 Id. at 157-169. While the Comment was supposedly for respondents Alvarez, CAIR and SBMA, SBMA had already filed its Comment and paragraph 4 of the Comment alleges that Gargantiel Ilagan and Atanante Law Firm, the law firm which filed the Comment, earlier filed on March 20, 2019 a Notice of Appearance as collaborating counsel of Alvarez and CAIR.

18 Id. at 208-212.

19 G.R. No. 157549, May 30, 2011, 649 SCRA 116. Rendered by the Third Division; penned by Associate Justice Lucas P. Bersamin and concurred in by Associate Justices Conchita Carpio Morales, Arturo D. Brion, Martin S. Villarama, Jr. and Ma. Lourdes P. A. Sereno.

> of the doctrine when the corporation is insolvent encompasses not only the capital stock, but also other property and assets generally regarded in equity as a trust fund for the payment of corporate debts. All assets and property belonging to the corporation held in trust for the benefit of creditors that were distributed or in the possession of the stockholders, regardless of full payment of their subscriptions, may be reached by the creditor in satisfaction of its claim.
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> Also, under the trust fund doctrine, a corporation has no legal capacity to release an original subscriber to its capital stock from the obligation of paying for his shares, in whole or in part, without a valuable consideration, or fraudulently, to the prejudice of creditors. **The creditor is allowed to maintain an action upon any unpaid subscriptions and thereby steps into the shoes of the corporation for the satisfaction of its debt. To make out a prima facie case in a suit against stockholders of an insolvent corporation to compel them to contribute to the payment of its debts by making good unpaid balances upon their subscriptions, it is only necessary to establish that the stockholders have not in good faith paid the par value of the stocks of the corporation.** [x x x]" (*emphasis ours*)[20]

Petitioners argue that *Halley* is inapplicable and takes the position that the facts of *Halley* are "not substantially on **'all fours'** with the present action."[21] They claim that the corporate personality of Business Media Philippines, Inc. (the corporation subject of *Halley*) was disregarded and the stockholders were held personally liable because it was shown that the said stockholders were found and proved to be in charge of its operation at the time the unpaid obligation was transacted and incurred which greatly benefitted the corporation, and that Rizalino Vineza had assigned his "fully paid up" shares to a certain Gerardo Jacinto in 1989 at the time when the directors and stockholders of the corporation had resolved to dissolve the corporation during its annual meeting.[22] They further claim that there was no evidence whatsoever presented during the trial nor self-evident on the records of this case to show that petitioners were in charge of the operation of CAIR and they acted in bad faith or fraudulently when the lease was transacted with SBMA. Having sold, ceded and assigned their entire subscription rights to the 400,000 shares in CAIR representing 100% of its entire outstanding capital stock to Alvarez who as assignee agreed to assume the payment of the unpaid balance of the price of the subscription rights in the total amount of ₱30,000,000.00 and Alvarez being then in charge as President of CAIR and its major stockholder as well as the signatory to the Lease Agreement, petitioners conclude that when *Halley* is invoked correctly, Alvarez should be solely responsible and liable for the unpaid rentals of CAIR to SBMA.[23]

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20 *Rollo*, pp. 46-48.
21 Id. at 6-7.
22 Id. at 7-8.
23 Id. at 8.

Regarding petitioners' assignment of their subscription rights to Alvarez through the DASR, the CA stated that for this to become a viable defense, it was incumbent upon petitioners to show that a valid transfer/assignment of shares, binding against third persons, took place under Section 63 of the Corporation Code, which provides:

> SECTION 63. *Certificate of stock and Transfer of Shares.* – The capital stock of stock corporation shall be divided into shares for which certificates signed by the president or vice-president, countersigned by the secretary or assistant secretary, and sealed with the seal of the corporation shall be issued in accordance with the by-laws. Shares of stock so issued are personal property and may be transferred by delivery of the certificate or certificates indorsed by the owner or his attorney-in-fact or other person legally authorized to make the transfer. No transfer, however, shall be valid, except as between the parties, until the transfer is recorded in the books of the corporation so as to show the names of the parties to the transaction, the date of the transfer, the number of the certificate or certificates and the number of shares transferred.
>
> No shares of stock against which the corporation holds any unpaid claim shall be transferable in the books of the corporation. (35)[24]

Citing *The Rural Bank of Lipa City, Inc. v. Court of Appeals*,[25] the CA noted that there must be strict compliance with the mode of transfer prescribed by law before a valid transfer of stock takes place wherein the following requirements are complied with: (1) there must be delivery of the stock certificate; (2) the certificate must be endorsed by the owner or his attorney-in-fact or other persons legally authorized to make the transfer; and (3) to be valid against third persons, the transfer must be recorded in the books of the corporation.[26] Based on these parameters, the CA stated that petitioners failed to hurdle their burden as the record is bereft of any proof to show compliance with the requirements for a valid transfer of shares; thus, without a valid transfer of shares, petitioners are still deemed to be stockholders of CAIR at the time the lease was enforced.[27] The CA further stated that the unrecorded transfer/assignment of shares between petitioners

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[24] See id. at 44. The counterpart provision of the Revised Corporation Code (Republic Act No. 11232), which became effective on February 23, 2019, is Section 62, which states:

> SEC. 62. *Certificate of Stock and Transfer of Shares.* - The capital stock of corporations shall be divided into shares for which certificates signed by the president or vice president, countersigned by the secretary or assistant secretary, and sealed with the seal of the corporation shall be issued in accordance with the bylaws. Shares of stock so issued are personal property and may be transferred by delivery of the certificate or certificates indorsed by the owner, his attorney-in-fact, or any other person legally authorized to make the transfer. No transfer, however, shall be valid, except as between the parties, until the transfer is recorded in the books of the corporation showing the names of the parties to the transaction, the date of the transfer, the number of the certificate or certificates, and the number of shares transferred. The Commission may require corporations whose securities are traded in trading markets and which can reasonably demonstrate their capability to do so to issue their securities or shares of stocks in uncertificated or scripless form in accordance with the rules of the Commission.
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> No shares of stock against which the corporation holds any unpaid claim shall be transferable in the books of the corporation.

[25] G.R. No. 124535, September 28, 2001, 366 SCRA 188.

[26] *Rollo*, pp. 44-45.

[27] Id. at 45.

and Alvarez is not binding on SBMA, and the latter can proceed against petitioners, who in its eyes remained as stockholders, against their unpaid subscriptions for the satisfaction of CAIR's rental arrears pursuant to the trust fund doctrine.[28]

Petitioners counter by insisting that under the DASR, which Alvarez failed to deny under oath its genuineness and due execution in his Third-Party Answer with Counterclaim, Alvarez is deemed to have admitted that petitioners had already assigned, transferred and conveyed to him their entire subscription rights representing 100% of the outstanding capital stock of CAIR with the exception of Jennifer and Virgilio who remained stockholders with fully paid and non-assessable shares numbering 76,000 and 4,000, respectively.[29] With the assignment, petitioners claim that they are no longer stockholders of CAIR with unpaid subscription and should not be made primarily and principally liable to SBMA, and that instead Alvarez should be solely be responsible for the unpaid rentals because he is the majority stockholder and the active President in charge of CAIR at the time he signed the lease contract.[30]

Petitioners further argue that as inactive stockholders with fully paid shares, Jennifer and Virgilio cannot be liable for the debts of CAIR.[31] Given the separate personality of CAIR, they posit that the piercing of the corporate veil is unwarranted without any allegation in the complaint and proof that individual petitioners consented or connived to commit patently unlawful acts of the corporation or that any of them was guilty of gross negligence or bad faith.[32] In fact, they claim that, effective December 1, 1998, they ceased to be directors of CAIR and had no participation in its operation, with Jennifer being replaced by Bienvenido S. Santos as Treasurer based on the minutes of the election of the corporate officers held in December 1998.[33]

Moreover, petitioners claim that the unpaid stock subscriptions are receivables of the corporation, which can only become due and owing upon a subscription call by the corporation's Board of Directors or when it undergoes bankruptcy or its assets are being levied under an execution or attachment, and none of them obtains in this case.[34]

Lastly, petitioners claim that Alvarez has admitted liability to them when he did not present contradictory evidence to the evidence presented by them despite the RTC giving him several chances and a final opportunity to

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28 Id. at 45-46.
29 Id. at 9-10.
30 Id. at 10.
31 Id.
32 Id. at 11-12.
33 Id. at 12-13.
34 Id. at 13-14.

present evidence, with prior notice to his counsel of record, on October 16, 2012.[35]

To have a historical perspective of the development of the common law trust fund doctrine, theory or principle, the following excerpt from Edwin S. Hunt's article[36] on the subject is insightful:

> It was formerly supposed that the relations between a corporation and its creditors were the same as those which existed between an individual debtor and his creditor. For example, in the year 1826, in the case of *Catlin v. The Eagle Bank* (6 Conn. 233), Chief Justice Hosmer said:
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> > "Where no legal lien has been obtained, it is a reasonable supposition that the relation between creditor and debtor must in all cases infer the same consequences; and that where the same mischief exists, there is the same law. The cases of an individual and of a corporation, in the matter under discussion, it appears to me are not merely analogous but identical; and I discern no reason for the slightest difference between them."
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> Since that time, however, the view has gradually grown up that the common law rights of a creditor over his debtor's property did not adequately protect the creditor of a corporation. In order to give the latter more extensive rights, it was thought that those rights must be based upon a theory different from that which ordinarily applies between debtor and creditor.
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> This new doctrine was for the first time announced in the year 1824 by Judge Story in the well-known case of *Wood v. Dummer* (3 Mason 309). In that case, the stockholders of a bank without paying its debts, had divided among themselves all the property of the corporation. Manifestly, a great injustice had been done to the creditors and on some theory or other they must be allowed to recover their claims from the persons who had so received the property of the corporation. Apparently, Judge Story thought that none of the principles of law applicable to the ordinary relation of debtor and creditor were adequate to the situation. The stockholders did not owe the debt and how, therefore, could the creditor compel them to pay? If, however, the property of the company be regarded as a fund held by the corporation in trust for its creditors, then the difficulty was overcome, for trust property could be followed into the hands of persons who have notice of the trust. As Judge Story said:
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> > "If I am right in this position, the principle difficulty in the cause is overcome. If the capital stock is a trust fund, then it may be followed into the hands of any persons having notice of the trust attaching to it."
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> As this new theory was so convenient to the solution of this case, Judge Story proceeded to show that the property of a corporation was a fund held in trust by it for its creditors. He says:

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35 Id. at 14-15.

36 Edwin S. Hunt, "The Trust Fund Theory and Some Substitutes For It," The Yale Law Journal, vol. 12, no. 2, 1902, pp. 63-81, available at <https://www.jstor.org/stable/782112>.

> "It appears to me very clear upon general principles as well as the Legislative intention, that the capital stock is to be deemed a pledge or trust fund for payment of debts contracted by the bank. The public as well as the Legislature have always supposed this to be a fund appropriated for such a purpose. The individual stockholders are not liable for the debts of the bank in their private capacities. The charter relieves them from personal responsibility and substitutes the capital stock in its stead. Credit is universally given to this fund by the public as the only means of repayment. * * * The stockholders have no rights until all the other creditors are satisfied. They have the full benefit of all the profits made by the establishment, and cannot take any portion of the fund until all the other claims on it are extinguished."

There would perhaps be little reason to object to calling the property of a corporation a trust fund for the benefit of its creditors, if all that the phrase meant was, that a corporation must pay its debts before dividing its assets among its stockholders.

But the trouble is that the "trust fund theory" thus originated has not been confined to the case to which Judge Story first applied it. That could not be expected. x x x

x x x x

A trust implies a trustee holding a legal title and cestui que trusts who have the beneficial interest. A court of equity will compel a trustee to hold and manage the property for the sole benefit of a cestui, to whom alone, in its eyes, the property belongs. The trustee can make no profit out of the property. His sole reward is his commission. All the property and all the profits belong to the cestui que trust.

Manifestly, the property of a corporation is held by it in trust in no such sense. A corporation has the beneficial or equitable as well as the legal title. It is in business to make money for itself and its stockholders and not for its creditors; while a trustee can only make money for his cestui que trust.

But it may be said that it is not claimed that the property of a going, solvent corporation is a trust fund for its creditors; it is only when the corporation becomes insolvent and ceases to do business that the assets become a trust fund. Many cases may be found where it is so stated. For example, in the case of *Appleton v. Turnbull* (84 Me. 72), the court said:

> "It is too firmly established at the present day to be questioned, that the capital stock of a corporation is a trust fund for the payment of its debts * * * during the existence of the life of the corporation, it is a trust to be managed for the benefit of its stockholders, but in the event of a dissolution or of insolvency, it becomes a trust fund for the benefit of its creditors."

x x x x

> x x x The trust fund theory has been, perhaps, most often applied to the case where a creditor of an insolvent corporation seeks to compel a stockholder to pay a balance claimed to be due on stock for which the par value has never been paid to the corporation.[37]

The trust fund doctrine or theory has been, perhaps, most often applied to the case where a creditor of an insolvent corporation seeks to compel a stockholder to pay a balance claimed to be due on stock for which the par value has never been paid to the corporation.[38] On this matter of the creditors running after shareholders for their unpaid subscriptions, it has been said:

> *Sawyer v. Hoag*[39] established that the stockholders of an insolvent corporation were liable to its creditors to the extent of the amount unpaid on stock subscriptions. Justice Miller based liability squarely on the trust-fund doctrine, saying that the doctrine applied to the capital stock of a corporation "especially its unpaid subscriptions." This holding carved a significant exception out of the general rule that stockholders of a corporation are insulated from liability for its debts.
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> As long as a corporation remains solvent the subscriber's only liability runs to the corporation. Once the corporation has matured the contract liability of the shareholder, it can, of course, assign that debt like no other. But except by way of assignment, the *creditor* of a *solvent* corporation, being in no sense a party to the subscription contract, is unable to reach an unpaid subscription. Practically speaking, however, as long as the corporation is solvent a corporate creditor will not need to pursue any remedy beyond a direct action against the corporation taken to judgment; hence any absence of privity between creditor and shareholder is not at this time a serious problem. But when the corporation becomes insolvent judgments at law are relatively worthless. At this juncture the trust-fund doctrine entered the picture to protect the creditor.[40]

In the Philippine setting, the following cases are illustrative of the application of the trust fund doctrine where the debtor is insolvent.

In the 1923 case of *Philippine Trust Company v. Rivera*[41] (*Philippine Trust Co.*), the Court allowed Philippine Trust Company, as assignee in insolvency of *La Cooperativa Naval Filipina,* to collect the balance of ₱22,500.00 that was due upon the subscription of Marciano Rivera, the defendant therein, to the capital stock of said insolvent corporation, *viz.*:

> It appears in evidence that in 1918 the *Cooperativa Naval Filipina* was duly incorporated under the laws of the Philippine Islands, with a capital of ₱100,000, divided into one thousand shares of a par value of ₱100 each. Among the incorporators of this company was numbered the

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37 Id. at 63-72.
38 Id. at 72.
39 17 Wall. 610, 21 L. Ed. 731 (1873).
40 James R. Ellis & Charles L. Sayre, "Trust-Fund Doctrine Revisited, Part II," 24 Wash. L. Rev. & St. B. J. 134-135 (1949), available at <https://digitalcommons.law.uw.edu/wlr/vol24/iss2/4>.
41 44 Phil. 469 (1923).

> defendant Marciano Rivera, who subscribed for 450 shares representing a value of ₱45,000, the remainder of the stock being taken by other persons. The articles of incorporation were duly registered in the Bureau of Commerce and Industry on October 30 of the same year.
>
> In the course of time the company became insolvent and went into the hands of the Philippine Trust Company, as assignee in bankruptcy; and by it this action was instituted to recover one-half of the stock subscription of the defendant, which admittedly has never been paid.
>
> The reason given for the failure of the defendant to pay the entire subscription is, that not long after the *Cooperativa Naval Filipina* had been incorporated, a meeting of its stockholders occurred, at which a resolution was adopted to the effect that the capital should be reduced by 50 per centum and the subscribers released from the obligation to pay any unpaid balance of their subscription in excess of 50 per centum of the same. As a result of this resolution it seems to have been supposed that the subscriptions of the various shareholders had been cancelled to the extent stated; and fully paid certificates were issued to each shareholder for one-half of his subscription. It does not appear that the formalities prescribed in section 17 of the Corporation Law (Act No. 1459), as amended, relative to the reduction of capital stock in corporations were observed, and in particular it does not appear that any certificate was at any time filed in the Bureau of Commerce and Industry, showing such reduction.
>
> His Honor, the trial judge, therefore held that the resolution relied upon by the defendant was without effect and that the defendant was still liable for the unpaid balance of his subscription. In this we think his Honor was clearly right.
>
> It is established doctrine 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. (Velasco *vs.* Poizat, 37 Phil., 802.) A corporation has no power to release an original subscriber to its capital stock from the obligation of paying for his shares, without a valuable consideration for such release; and as against creditors a reduction of the capital stock can take place only in the manner and under the conditions prescribed by the statute or the charter or the articles of incorporation. Moreover, strict compliance with the statutory regulations is necessary (14 C. J., 498, 620).
>
> In the case before us the resolution releasing the shareholders from their obligation to pay 50 per centum of their respective subscriptions was an attempted withdrawal of so much capital from the fund upon which the company's creditors were entitled ultimately to rely and, having been effected without compliance with the statutory requirements, was wholly ineffectual.[42] (Underscoring supplied)

The 1918 case of *Velasco v. Poizat*[43] cited in *Philippine Trust Co.* also involved recovery of unpaid subscriptions in an insolvent company, *viz.*:

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42 Id. at 469-471.

43 37 Phil 802 (1918).

From the amended complaint filed in this cause upon February 5, 1915, it appears that the plaintiff, as assignee in insolvency of "The Philippine Chemical Product Company" (Ltd.) is seeking to recover of the defendant, Jean M. Poizat, the sum of ₱1,500, upon a subscription made by him to the corporate stock of said company. It appears that the corporation in question was originally organized by several residents of the city of Manila, where the company had its principal place of business, with a capital of ₱50,000, divided into 500 shares. The defendant subscribed for 20 shares of the stock of the company, and paid in upon his subscription the sum of ₱500, the par value of 5 shares. The action was brought to recover the amount subscribed upon the remaining shares.

x x x x

No attempt is made in the Corporation Law to define the precise conditions under which an action may be maintained upon a stock subscription, as such conditions should be determined with reference to the rules governing contract liability in general; and where it appears as in this case that a matured stock subscription is unpaid, none of the provisions contained in sections 38 to 48, inclusive, of Act No. 1459 can be permitted to obstruct or impede the action to recover thereon. By virtue of the first subsection of section 36 of the Insolvency Law (Act No. 1956) the assignee of the insolvent corporation succeeds to all the corporate rights of action vested in the corporation prior to its insolvency; and the assignee therefore has the same freedom with respect to suing upon a stock subscription as the directors themselves would have had under section 49 above cited.

But there is another reason why the present plaintiff must prevail in this case, even supposing that the failure of the directors to comply with the requirements of the provisions of sections 38 to 48, inclusive, of Act No. 1459 might have been an obstacle to a recovery by the corporation itself. That reason is this: When insolvency supervenes upon a corporation and the court assumes jurisdiction to wind it up, all unpaid stock subscriptions become payable on demand, and are at once recoverable in an action instituted by the assignee or receiver appointed by the court. This rule apparently had its origin in a recognition of the principle that a court of equity, having jurisdiction of the insolvency proceedings, could, if necessary, make the call itself, in its capacity as successor to the powers exercised by the board of directors of the defunct company. Later a further rule gained recognition to the effect that the receiver or assignee, in an action instituted by proper authority, could himself proceed to collect the subscription without the necessity of any prior call whether. This conclusion is well supported by reference to the following authorities:

". . . a court of equity may enforce payment of stock subscriptions, although there have been no calls for them by the company." (Hatch *vs.* Dana, 101 U.S., 205.)

"It is again insisted that plaintiffs cannot recover because the suit was not preceded by a call or assessment against the defendant as a subscriber, and that until this is done no right of action accrues. In a suit by a solvent going corporation to collect a subscription, and in certain suits provided by statute this would be true; but it is now quite well settled that when the corporation becomes insolvent, with proceedings instituted by creditors to wind up and distribute its assets, no call or assessment is necessary before the institution of suits to collect unpaid balances on

> subscription." (Ross-Meehan Shoe F. Co. *vs.* Southern Malleable Iron Co., 72 Fed., 957, 960; *see also* Henry *vs.* Vermillion etc. R. R. Co., 17 Ohio, 187, and Thompson on Corporations, 2d ed., vol. 3, sec. 2697.)
>
> It evidently cannot be permitted that a subscriber should escape from his lawful obligation by reason of the failure of the officers of the corporation to perform their duty in making a call; and when the original mode of making the call becomes impracticable, the obligation must be treated as due upon demand. If the corporation were still an active entity, and this action should be dismissed for irregularity in the making of the call, other steps could be taken by the board to cure the defect and another action could be brought; but where the company is being wound up, no such procedure would be practicable. **The better doctrine is that when insolvency supervenes all unpaid subscriptions become at once due and enforceable.**[44] (Emphasis supplied)

In *Philippine National Bank v. Bitulok Sawmill, Inc., et al.*,[45] the Court allowed Philippine National Bank, as creditor, to substitute the receiver of Philippine Lumber Distributing Agency in the actions for the recovery from defendant lumber producers the balance of their stock subscriptions and ordered the payment by the latter of their unpaid subscriptions, applying the trust fund doctrine, *viz.*:

> In Philippine Trust Co. *v.* Rivera, citing their leading case of Velasco *v.* Poizat, this Court held: "It is established doctrine 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 debt.... A corporation has no power to release an original subscriber to its capital stock from the obligation of paying for his shares, without a valuable consideration for such release; and as against creditors a reduction of the capital stock can take place only in the manner and under the conditions prescribed by the statute or the charter or the articles of incorporation. Moreover, strict compliance with the statutory regulations is necessary...." The Poizat doctrine found acceptance in latter cases. One of the latest cases, Lingayen Gulf Electric Power *v.* Baltazar, speaks to this effect: "In the case of Velasco *v.* Poizat, the corporation involved was insolvent, in which case all unpaid stock subscriptions become payable on demand and are immediately recoverable in an action instituted by the assignee."[46]

In *Steinberg v. Velasco*,[47] the trust fund doctrine was impliedly applied in a situation wherein the debtor corporation was not only insolvent, but its directors also acted in fraud of creditors when they authorized the purchases of the corporation's capital stock from the stockholders and even purchased and distributed dividends to the stockholders, leaving the creditors unpaid, *viz.*:

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44 Id. at 803-808.
45 132 Phil. 758 (1968).
46 Id. at 763-764. Citations omitted.
47 52 Phil. 953 (1929).

It is very apparent that on June 24, 1922, the board of directors acted on the assumption that, because it appeared from the books of the corporation that it had accounts receivable of the face value of ₱19,126.02, therefore it had a surplus over and above its debts and liabilities. But as stated there is no stipulation as to the actual cash value of those accounts, and it does appear from the stipulation that on February 28, 1924, ₱12,512.47 of those accounts had but little, if any, value, and it must be conceded that, in the purchase of its own stock to the amount of ₱3,300 and in declaring the dividends to the amount of P3,000, the real assets of the corporation were diminished ₱6,300. It also appears from paragraph 4 of the stipulation that the corporation had a "surplus profit" of ₱3,314.72 only. It is further stipulated that the dividends should "be made in installments so as not to affect financial condition of the corporation." In other words, that the corporation did not then have an actual *bona fide* surplus from which the dividends could be paid, and that the payment of them in full at that time would "affect the financial condition of the corporation."

It is, indeed, peculiar that the action of the board in purchasing the stock from the corporation and in declaring the dividends on the stock was all done at the same meeting of the board of directors, and it appears in those minutes that both Ganzon and Mendaros were formerly directors and resigned before the board approved the purchase and declared the dividends, and that out of the whole 330 shares purchased, Ganzon sold 100 and Mendaros 200, or a total of 300 shares out of the 330, which were purchased by the corporation, and for which it paid ₱3,300. In other words, that the directors were permitted to resign so that they could sell their stock to the corporation. As stated, the authorized capital stock was P20,000 divided into 2,000 shares of the par value of ₱10 each, of which only ₱10,030 was subscribed and paid. Deducting the ₱3,300 paid for the purchase of the stock, there would be left P7,000 of paid up stock, from which deduct ₱3,000 paid in dividends, there would be left ₱4,000 only. In this situation and upon this state of facts, it is very apparent that the directors did not act in good faith or that they were grossly ignorant of their duties.

Upon each of those points, the rule is well stated in Ruling Case Law, vol. 7, p. 473, section 454, where it is said:

"*General Duty to Exercise Reasonable Care.* — The directors of a corporation are bound to care for its property and manage its affairs in good faith, and for a violation of these duties resulting in waste of its assets or injury to the property they are liable to account the same as other trustees. And there can be no doubt that if they do acts clearly beyond their power, whereby loss ensues to the corporation, or dispose of its property or pay away its money without authority, they will be required to make good the loss out of their private estates. This is the rule where the disposition made of money or property of the corporation is one either not within the lawful power of the corporation, or, if within the power of the corporation, is not within the power or authority of the particular officer or officers."

And section 458 which says:

"*Want of Knowledge, Skill, or Competency.* — It has been said that directors are not liable for losses resulting to the corporation from want of knowledge on their part; or for mistakes of judgment, provided they were

> honest, and provided they are fairly within the scope of the powers and discretion confided to the managing body. But the acceptance of the office of a director of a corporation implies a competent knowledge of the duties assumed, and directors cannot excuse imprudence on the ground of their ignorance or inexperience; and if they commit an error of judgment through mere recklessness or want of ordinary prudence or skill, they may be held liable for the consequences. Like a mandatory, to whom he has been likened, a director is bound not only to exercise proper care and diligence, but ordinary skill and judgment. As he is bound to exercise ordinary skill and judgment, he cannot set up that he did not possess them."
>
> Creditors of a corporation have the right to assume that so long as there are outstanding debts and liabilities, the board of directors will not use the assets of the corporation to purchase its own stock, and that it will not declare dividends to stockholders when the corporation is insolvent.[48]

From the foregoing disquisition, it is clear that a corporate creditor cannot immediately invoke the trust fund doctrine to proceed against unpaid subscriptions of stockholders of the debtor corporation without alleging and proving the corporation's insolvency or any of the other acceptable grounds where the trust fund doctrine, theory or principle has been applied.[49] The observation that a corporation has the beneficial or equitable as well as the legal title of its capital stock and is in business to make money for itself and its stockholders and not for its creditors is well-taken.[50] As well, the capital stock of a corporation is a trust to be managed during its corporate life for the benefit of stockholders. It is only in the event of its dissolution or insolvency, does the capital stock become a trust fund for the benefit of its creditors.[51]

The Court will now proceed to determine the propriety of the CA's application of *Halley* in this case.

In *Halley*, Business Media Philippines, Inc. (BMPI) made several orders on credit from Printwell, Inc. (Printwell) involving the printing of business magazines, wrappers and subscription cards, in the total amount of ₱291,342.76. The said goods were delivered to and received by BMPI but it failed to pay its overdue account to Printwell as well as the interest thereon, at the rate of 20% *per annum* until fully paid. It was also during this time that defendant stockholders therein, which included Donnina C. Halley (Halley) (petitioner therein), were in charge of the operation of BMPI

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48 Id. at 959-961.

49 In general, the trust fund doctrine or principle has been applied to instances: (1) where the property of a corporation has been divided among its stockholders without paying creditors, (2) where an insolvent corporation has preferred a creditor, and (3) where it is sought to recover unpaid or partially paid subscriptions to capital stock. Edwin S. Hunt, supra note 36, at 69. Also, the trust fund doctrine usually applies in four cases: (a) where the corporation has distributed its capital among the stockholders without providing for the payment of creditors; (b) where it had released the subscribers to the capital stock from their subscriptions; (c) where it has transferred the corporate property in fraud of its creditors; and (d) where the corporation is insolvent. Cesar L. Villanueva, "The Trust Fund Doctrine Under Philippine Corporate Setting," Ateneo Law Journal, Vol. XXXI, 1987, p. 42.

50 See Edwin S. Hunt, id. at 65.

51 Id.

despite the fact that they were not able to pay their unpaid subscriptions to BMPI, and yet greatly benefited from said transactions. On February 8, 1990, Printwell amended the complaint in order to implead as defendants all the original stockholders and incorporators to recover on their unpaid subscriptions. Printwell impleaded the petitioner therein and the other stockholders of BMPI for two reasons, namely: (a) to reach the unpaid subscriptions because it appeared that such subscriptions were the remaining visible assets of BMPI; and (b) to avoid multiplicity of suits. The defendants therein filed a consolidated answer, averring that they all had paid their subscriptions in full; that BMPI had a separate personality from those of its stockholders; that Rizalino C. Viñeza (one of the defendant stockholders) had assigned his fully paid up shares to a certain Gerardo R. Jacinto in 1989; and that the directors and stockholders of BMPI had resolved to dissolve BMPI during the annual meeting held on February 5, 1990.

The issues, which are relevant to this case, that Halley presented to the Court to resolve were: (a) the propriety of piercing of the thin veil of the corporate fiction, and (b) the application of the trust fund doctrine.

On the first issue, Halley argued that she should not be liable because she had no participation in the transaction between BMPI and Printwell; BMPI acted on its own; and she had no hand in persuading BMPI to renege on its obligation to pay.

The Court observing that corporate personality cannot be used to foster injustice ruled against Halley's submission, thus:

> Although a corporation has a personality separate and distinct from those of its stockholders, directors, or officers, such separate and distinct personality is merely a fiction created by law for the sake of convenience and to promote the ends of justice. The corporate personality may be disregarded, and the individuals composing the corporation will be treated as individuals, if the corporate entity is being used as a cloak or cover for fraud or illegality; as a justification for a wrong; as an alter ego, an adjunct, or a business conduit for the sole benefit of the stockholders. As a general rule, a corporation is looked upon as a legal entity, unless and until sufficient reason to the contrary appears. Thus, the courts always presume good faith, and for that reason accord prime importance to the separate personality of the corporation, disregarding the corporate personality only after the wrongdoing is first clearly and convincingly established. It thus behooves the courts to be careful in assessing the milieu where the piercing of the corporate veil shall be done.
>
> Although nowhere in Printwell's amended complaint or in the testimonies Printwell offered can it be read or inferred from that the petitioner was instrumental in persuading BMPI to renege on its obligation to pay; or that she induced Printwell to extend the credit accommodation by misrepresenting the solvency of BMPI to Printwell, her personal liability, together with that of her co-defendants, remained because the CA found her and the other defendant stockholders to be in charge of the

operations of BMPI at the time the unpaid obligation was transacted and incurred, to wit:

> "In the case at bench, it is undisputed that BMPI made several orders on credit from appellee PRINTWELL involving the printing of business magazines, wrappers and subscription cards, in the total amount of ₱291,342.76 x x x which facts were never denied by appellants' stockholders that they owe(d) appellee the amount of ₱291,342.76. The said goods were delivered to and received by BMPI but it failed to pay its overdue account to appellee as well as the interest thereon, at the rate of 20% *per annum* until fully paid. It was also during this time that appellants stockholders were in charge of the operation of BMPI despite the fact that they were not able to pay their unpaid subscriptions to BMPI yet greatly benefited from said transactions. In view of the unpaid subscriptions, BMPI failed to pay appellee of its liability, hence appellee in order to protect its right can collect from the appellants stockholders regarding their unpaid subscriptions. To deny appellee from recovering from appellants would place appellee in a limbo on where to assert their right to collect from BMPI since the stockholders who are appellants herein are availing the defense of corporate fiction to evade payment of its obligations."

It follows, therefore, that whether or not the petitioner persuaded BMPI to renege on its obligations to pay, and whether or not she induced Printwell to transact with BMPI were not good defenses in the suit.[52] (Citations omitted)

Anent the second issue, Halley argued that the trust fund doctrine was inapplicable because she had already fully paid her subscriptions to the capital stock of BMPI. However, the Court affirmed the factual findings of the lower courts that she failed to discharge her burden to prove full payment of her subscriptions. On the trust fund doctrine, the Court stated:

> The *trust fund doctrine* enunciates a –
>
> "x x x rule that the property of a corporation is a trust fund for the payment of creditors, but such property can be called a trust fund 'only by way of analogy or metaphor.' As between the corporation itself and its creditors it is a simple debtor, and as between its creditors and stockholders its assets are in equity a fund for the payment of its debts."

The *trust fund doctrine*, first enunciated in the American case of *Wood v. Dummer*, was adopted in our jurisdiction in *Philippine Trust Co. v. Rivera*, where this Court declared that:

> "It is established doctrine that subscriptions to the capital of a corporation constitute a fund to which creditors

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52 *Halley v. Printwell, Inc.*, supra note 19, at 132-134.

> 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. (*Velasco vs. Poizat*, 37 Phil., 802) x x x"
>
> We clarify that the *trust fund doctrine* is not limited to reaching the stockholder's unpaid subscriptions. The scope of the doctrine when the corporation is insolvent encompasses not only the capital stock, but also other property and assets generally regarded in equity as a trust fund for the payment of corporate debts. All assets and property belonging to the corporation held in trust for the benefit of creditors that were distributed or in the possession of the stockholders, regardless of full payment of their subscriptions, may be reached by the creditor in satisfaction of its claim.
>
> Also, under the *trust fund doctrine*, a corporation has no legal capacity to release an original subscriber to its capital stock from the obligation of paying for his shares, in whole or in part, without a valuable consideration, or fraudulently, to the prejudice of creditors. The creditor is allowed to maintain an action upon any unpaid subscriptions and thereby steps into the shoes of the corporation for the satisfaction of its debt. **To make out a *prima facie* case in a suit against stockholders of an insolvent corporation to compel them to contribute to the payment of its debts by making good unpaid balances upon their subscriptions, it is only necessary to establish that the stockholders have not in good faith paid the par value of the stocks of the corporation.**[53] (Emphasis supplied; citations omitted)

Based on the Court's above pronouncements, *Halley* recognized two instances when the creditor is allowed to maintain an action upon any unpaid subscriptions based on the trust fund doctrine: (1) where the debtor corporation released the subscriber to its capital stock from the obligation of paying for their shares, in whole or in part, without a valuable consideration, or fraudulently, to the prejudice of creditors; and (2) where the debtor corporation is insolvent or has been dissolved without providing for the payment of its creditors.

The crucial fact in *Halley* which justified the application of the trust fund doctrine is that after the filing of the original complaint, the directors and stockholders of BMPI had resolved to dissolve BMPI during the annual meeting held on February 5, 1990. This move to dissolve BMPI triggered the amendment of Printwell's complaint on February 8, 1990 in order to implead as defendants all the original stockholders and incorporators to recover their unpaid subscriptions. The move to dissolve BMPI was viewed by the Court as a clear attempt by the directors and stockholders to escape BMPI's liability to Printwell. And, as it turned out, the subscriptions, while appearing on the books of the corporation as fully paid, were in fact not paid. These circumstances thus justified the Court's piercing of BMPI's corporate veil where the corporate personality may be disregarded if the corporate entity is being used as a cloak or cover for fraud. While good faith is always presumed

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[53] Id. at 134-136.

and prime importance is accorded to the separate personality of the corporation as an alter ego, an adjunct, or a business conduit for the sole benefit of stockholders, the corporate personality can be disregarded only after the wrongdoing is first clearly and convincingly established.[54]

Clearly, the first instance finds no relevance in the present case. It is the second which SBMA, as creditor, may invoke to collect from CAIR's stockholders for their unpaid subscriptions and apply the same to CAIR's unpaid rentals. But, as stressed in *Halley*: "To make out a *prima facie* case in a suit against stockholders of an insolvent corporation to compel them to contribute to the payment of its debts by making good unpaid balances upon their subscriptions, it is only necessary to establish that the stockholders have not in good faith paid the par value of the stocks of the corporation."[55]

Unfortunately, SBMA has not even pleaded either insolvency of CAIR or its dissolution. What is evident in SBMA's complaint is that it is a simple collection suit, to wit:

> 10. Despite the clear language of the Lease Agreement, however, Defendant Corporation has been consistently remiss in paying its lease rentals and airport fees as it failed to pay numerous monthly rentals and airport fees at the specified time each month, despite repeated demands for its compliance.
>
> x x x x
>
> 15. Despite the above demands and notices, Defendant Corporation still failed to heed the same. x x x
>
> x x x x
>
> 19. Despite several demands on Plaintiff's part for Defendant Corporation to fully settle its outstanding accounts, the latter has utterly failed and/or refused to pay the same. x x x
>
> x x x x
>
> 21. Equally important to stress is the fact that the foregoing antecedents would only prove Defendant Corporation's continuous and unfair disregard of its contractual obligations to pay the amounts due the Plaintiff under the Lease Agreement, to Plaintiff's extreme damage and prejudice.
>
> 22. By reason of its continued refusal to settle the above said amounts, Defendants should therefore be adjudged liable to pay the amount of **US$163,641.89** (US$143,269.76 + US$20,372.13), plus legal interest until it has effected full payment of the said amounts.[56]

As to petitioners, the only allegation of the complaint is:

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54 See id. at 132.
55 Id. at 136.
56 Records, Vol. 1, pp. 4-7.

> 4. Defendants [who are individually named with their respective addresses] are impleaded herein being the incorporators/ stockholders of [CAIR], and are liable to the payment of the Defendant Corporation's unpaid obligations, incurred damages and other amounts to be adjudged by this Honorable Court, to the extent of their unpaid subscribed capital stock as follows:
>
> x x x x[57]

Not only were the allegations of SBMA's complaint insufficient to justify the invocation and application of the trust fund doctrine as appreciated in *Halley*, even the evidence adduced by SBMA was solely to prove the uncollected rentals. SBMA presented two witnesses, Editha Lim-Marzal (Editha) and Kenneth Lemuel G. Rementilla (Kenneth). Editha, the Division Chief of the Accounting Department, Account Receivables of SBMA, testified in the main that: as per records, CAIR was consistently remiss in paying its lease rentals and airport fees; demand letters were sent to CAIR, which fell on deaf ears; and according to the Summary of Outstanding Account, the obligation incurred by CAIR amounted to US$212,135.55 or ₱10,171,899.60 as of March 28, 2007.[58] Kenneth, the Manager of the Locator's Registration and Licensing Department of SBMA, testified that: he was familiar with CAIR; it underwent the usual process of registration to become a free port enterprise and complied with all the documentary requirements to prove its existence as a business enterprise, such as its Articles of Incorporation (AOI) duly registered with the Securities and Exchange Commission; he was not notified of any changes or amendments in the AOI with respect to the names of the incorporators; and SBMA and CAIR entered into a Lease Agreement on February 3, 1999 but was pre-terminated on January 14, 2004 due to CAIR's failure to settle its account.[59]

In short, SBMA failed to either allege or prove any of the two grounds recognized in *Halley* when the trust fund doctrine may be applied to compel the stockholders to contribute to the payment of CAIR's debts by compelling them to pay the unpaid balances upon their subscriptions.

The CA indeed misapplied *Halley* in this case. The CA miserably failed to identify the salient facts of the case constituting the specific ground to justify the application of the trust fund doctrine. The CA relied on *Halley* without showing, either in the pleadings or in the evidence, how its ratio could be applied.

Given the failure of SBMA to make a case for the application of the trust fund doctrine against petitioners, the Court will not provide the basis for the former.

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57 Id. at 2.
58 Id. at 33-34.
59 Id. at 35-36.

With the Court's finding that the CA erred in applying the trust fund doctrine to make the stockholders liable to SBMA for their unpaid subscriptions to the extent of CAIR unpaid obligations to SBMA, and without any evidence to controvert the total amount of US$163,341.89, plus legal interest, adjudged by the lower courts in favor of SBMA, only CAIR should be solely liable therefor. The third-party complaint filed by petitioners against Alvarez should also be dismissed with the award of damages in favor of petitioners vacated. With the dismissal of the third-party complaint, the resolution of the second issue is rendered superfluous.

As a final note, the Court quotes Judge Clark in *Barr & Creelman Mill & Plumbing Supply Co. v. Zoller*,[60]

> The well-publicized criticisms of the trust fund doctrine are appreciated in New York, for the Court of Appeals has said recently in Reif v. Equitable Life Assurance Society, 268 N.Y. 269, 276, 197 N.E. 278, 280, 100 A.L.R. 55: "First declared by Justice Story (Wood v. Dummer (1824), Fed.Cas.No. 17,994, 3 Mason 308, 311), this 'trust fund doctrine' has been the subject of much adverse commentary and has often been repudiated as a fiction unsound in principle and vexing in business practice. See 5 Pomeroy's Equity Jurisprudence (4th Ed.) §§ 2319, 2320, 2130, collating the authorities. We do not stop now to canvass the limits of such a theory. It is enough that the facts of the present case so we hold do not call for application of the doctrine." x x x[61]

WHEREFORE, the Petition is partly **GRANTED**. The Decision dated September 21, 2015 and Resolution dated March 3, 2016 of the Court of Appeals in CA-G.R. CV No. 103619 are **REVERSED** and **SET ASIDE**. A new judgment is hereby rendered in Civil Case No. 190-0-2004 before the Regional Trial Court of Olongapo City, Branch 72, **ORDERING** defendant corporation Centennial Air, Inc. solely liable to pay plaintiff Subic Bay Metropolitan Authority the total amount of US$163,341.89, plus legal interest at 6% *per annum* from January 14, 2004[62] until fully paid, and **DISMISSING** the case against defendant Roberto Lozada and the Third-Party Complaint for lack of merit.

SO ORDERED.

ALFREDO BENJAMIN S. CAGUIOA
Associate Justice

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60 109 F.2d 924 (2d Cir. 1940).
61 Id. at 927.
62 Date of final demand letter, Annex "I" of the Complaint. Records, Vol. 1, p. 53.

WE CONCUR:

DIOSDADO M. PERALTA
Chief Justice
Chairperson

ROSMARI D. CARANDANG
Associate Justice

RODIL V. ZALAMEDA
Associate Justice

SAMUEL H. GAERLAN
Associate Justice

CERTIFICATION

Pursuant to Section 13, Article VIII of the Constitution, I certify that the conclusions in the above Decision had been reached in consultation before the case was assigned to the writer of the opinion of the Court's Division.

DIOSDADO M. PERALTA
Chief Justice