

CATALINA R. REYES, PETITIONER, VS. HON. BIENVENIDO A. TAN, AS JUDGE OF THE COURT OF FIRST INSTANCE OF MANILA, BRANCH XIII, AND FRANCISCA R. JUSTINIANI, RESPONDENTS.*G.R. No. 16982. September 30, 1961*

Ponente: LABRADOR, J.

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This is a petition for certiorari to review and set aside an order of the Court of First Instance of Manila, Hon. Bienvenido A. Tan, presiding, in Civil Case No. 42375, entitled "Francisca R. Justiniani vs. Wadhupal Dalamal, et al.", appointing a receiver of the corporation Roxas-Kalaw Textile Mills, Inc. In said action, plaintiff Justiniani asks the court to order the directors of the corporation, jointly and severally, to repair the damage caused to the corporation, of which all the plaintiff and defendants are members. The action was filed about January of 1960 and the order for the appointment of the receiver issued on February 15, 1960, while the designation of the receiver was made in an order of the court dated April 30, 1960.

In the complaint in said Civil Case No. 42375, it is alleged that the corporation, Roxas-Kalaw Textile Mills, Inc., was organized on June 5, 1954 by defendants Cesar K. Roxas, Adelia K. Roxas, Benjamin M. Roxas, Jose Ma. Barcelona and Morris Wilson, for and on behalf of the following primary principals with the following shareholdings: Adelia K. Roxas, 1200 Class A shares; I, Sherman, 900 Class A shares; Robert W. Born, 504 Class A shares and Morris Wilson, 450 Class A shares; that the plaintiff holds both Class A and Class B shares and the number and value thereof are as follows: Class A-50 shares, Class B-1,250 shares; that on May 8, 1957, the Board of Directors approved a resolution designating one Dayaram as co-manager with the specific understanding that he was to act as defendant Wadhupal Dalama's designee, Morris Wilson was likewise designated as co-manager with responsibilities for the management of the factory only, that an office in New York was opened for the purpose of supervising purchases, which purchases must have the unanimous agreement of Cesar K. Roxas, New York resident member of the board of directors, Robert Born and Wadhupal Dalamal or their respective representatives; that several purchases aggregating \$289,678.86 were made in New York for raw materials such as greige cloth, rayon and grey goods for the textile mill and shipped to the Philippines, which shipment were found out to consist not of raw materials but already finished products, such as, West Point khaki, rayon suiting materials dyed in the piece, finished rayon tafetta in cubes, cotton eyelets, etc., for which reasons the Central Bank of the Philippines stopped all dollar allocations for raw materials for the corporation which necessarily led to the paralization of the operation of the textile mill and its business; that the supplier of the aforesaid finished goods was the United Commercial Company of New York in which defendant Dalamal had interests and the letter of credit for said goods were guaranteed by the Indian Commercial Company and the Indian Traders in which firms defendant Dalamal likewise held interests; that the resale of the finished goods was the business of the Indian Commercial Company of Manila, which company could not obtain dollar allocations for importations of finished goods under the Central Bank regulations; that plaintiff and some members of the board of directors urged defendants to proceed against Dalamal, exposing his offense to the Central Bank, and to initiate suit against

Dalamal for his fraud against the corporation; that defendants refused to proceed against Dalamal and instead continued to deal with the Indian Commercial Company to the damage and prejudice of the corporation. The prayer asks for the appointment of a receiver and a judgment making defendants jointly and severally liable for the damages.

After a denial of a motion to dismiss and the filing of an answer alleging that the complaint states no cause of action, the motion for the appointment of a receiver was set for hearing and subsequently the court entered the order for the appointment of a receiver. The court found and held:

"The second ground of the defendant's motion to dismiss and/or deny the petition is the alleged want of a cause of action of the plaintiff's complaint. Philippine jurisprudence is complete with authorities upholding the principle that this ground for dismissal must appear in the face of the complaint itself; and that to determine the sufficiency of the cause of action, only the facts alleged in the complaint and no other, should be considered; in fine, the test of sufficiency of cause of action is whether or not, admitting the facts alleged in the complaint, the Court could render a valid judgment upon the same in accordance with the prayer of the petition (e. g., *Paminsan vs. Costales*, 28 Phil. 587, 589). The complaint in the instant case abounds with arguments establishing and supporting plaintiff's cause of action for and in behalf of the Roxas-Kalaw Textile Mills, Inc. against all the defendants (Sec. e. g. paragraphs 4, 5, 6 and 7 of the Complaint). Taking these paragraphs of the complaint in context, it is clear that the plaintiff has sufficiently averred facts constituting a cause or basis for a derivative suit for injuries to the corporation, as by negligence, mismanagement or fraud of its directors, are normally dealt with as wrong to the whole group of share holders in their corporate capacity, to be redressed in a suit by or on behalf of the corporation."

"Evident from the defendants' motion to dismiss and/or to deny the petition for receivership is their complete failure to come up with a valid and substantial defense against or denial of the complaint's allegations of mismanagement, if not the actual commission of ultra vires and illegal acts. Invariably the props of defendants' motion consist of the unconvincing countercharges of the plaintiffs non-observance of the technicalities of our procedural law and disregard of technical and evidently futile intracorporate remedies to redress the violations charged against the defendants. It is clear that the controlling majority did nothing for two years to protect the interests of the corporation, (see pars. 5-7, complaint.)

"The defendants themselves having admitted in open court during the oral discussion of their motion to dismiss and the plaintiff's motion for receivership that the majority stockholders will under any condition entertain any suggestion of the minority shareholders, the appointment of an independent third party in the management of the corporation becomes imperative for the survival of the company." (Order dated Feb. 15, 1960).

On April 30, 1960, the court issued another order which reads as follows:

"After this incident wherein it was clearly shown that the minority stockholders, represented by the plaintiff, have no recourse whatsoever before the majority stockholders of the company, and after it has been shown that the majority has violated the law by importing into the Philippines finished goods instead of raw materials as stipulated in their license, and since these acts are prejudicial to the company because it might result in the cancellation of their license, the Court is of the opinion and so holds that the appointment of a receiver is absolutely necessary for the protection not only of the rights of the minority but also those of the majority stockholders of the company."

In the first assignment of error, petitioner claims that respondent Justiniani neither alleged nor proved the existence of an emergency requiring the immediate appointment of a receiver of the Roxas-Kalaw Textile Mill, Inc.; that the alleged fraudulent transaction took place more than two years before the application for receivership, and so was the refusal of the directors to sue or prosecute Dalamal. This contention is not well founded. At the hearing of the petition for the appointment of a receiver held on January 30, 1960, various records of shipments of

finished textile goods on dollar allocations for raw materials were exhibited. Publicity had also been given to the importations of textiles by the corporation, in place of cotton raw materials. The record shows the list of the various documents proving the purchase of letters of credit for textiles. These textiles were denied importation and had to be re-exported. The fact of the importation of finished textiles on dollar allocations for raw materials in violation of Central Bank regulations was, therefore, conclusively shown.

It is also not denied by petitioner that the allocation of dollars to the corporation for the importation of raw materials was suspended. In the eyes of the court below, as well as in our own, the importation of textiles instead of raw materials, as well as the failure of the Board of Directors to take action against those directly responsible for the misuse of dollar allocations constitute fraud, or consent thereto on the part of the directors. Therefore, a breach of trust was committed which justified the derivative suit by a minority stockholder on behalf of the corporation.

"It is well settled in this jurisdiction that where corporate directors are guilty of a breach of trust—not of mere error of judgment or abuse of discretion—and intracorporate remedy is futile or useless, a stockholder may institute a suit in behalf of himself and ether stockholders and for the benefit of the corporation, to bring about a redress of the wrong inflicted directly upon the corporation and indirectly upon the stockholders. An illustration of a suit of this kind is found in the case of Pascual vs. Del Saz Orozco (19 Phil., 82), decided by this court as early as 1911. In that case, the Banco Español-Filipino suffered heavy losses due to fraudulent connivance between a depositor and an employee of the bank, which losses, it was contended, could have been avoided if the president and directors had been more vigilant in the administration of the affairs of the bank. The stockholders constituting the minority brought a suit in behalf of the bank against the directors to recover damages, and this over the objection of the majority of the stockholders and the directors. This court held that the suit could properly be maintained." (Angeles vs. Santos 64 Phil., 697).

The claim that respondent Justiniani did not take steps to remedy the illegal importation for a period of two years is also without merit. During that period of time respondent had the right to assume and expect that the directors would remedy the anomalous situation of the corporation brought about by their own wrong doing. Only after such period of time had elapsed could respondent conclude that the directors were remiss in their duty to protect the corporation property and business.

Counsel for petitioner claims that respondent Justiniani was treasurer of the corporation for sometime and had control of funds and this notwithstanding, she had not taken the steps to remedy the situation. In answer we state that the fraud consisted in importing finished textile instead of raw cotton for the textile mill; the fraud, therefore, was committed by the manager of the business and was consented to by the directors, evidently beyond reach of respondent.

The directors permitted the fraudulent transaction to go unpunished and nothing appears to have been done to remove the erring purchasing managers. In a way the appointment of a receiver may have been thought of by the court below so that the dollar allocation for raw material may be revived and the textile mill placed on an operating basis. It is possible that if a receiver in which the Central Bank may have confidence is appointed, the dollar allocation for raw material may be restored. Claim is made that if a receiver is appointed, the Philippine National Bank to which the corporation owes considerable sums of money might be led to foreclose the mortgage. Precisely the appointment of a receiver in whom the bank may have had confidence might rehabilitate the business and bring a restoration of the dollar allocation much needed for raw material and an improvement in the business and assets of the corporation, thus insuring the collection of the bank's loan.

Considering the above circumstances we are led to agree with the judge below that the appointment of a receiver was not only expedient but also necessary to restore the faith and confidence of the Central Bank authorities in the

administration of the affairs of the corporation, thus ultimately leading to a restoration of the dollar allocation so essential to the operation of the textile mills. The first assignment of error is, therefore, overruled.

In the second assignment of error, petitioner claims that the management has been changed and the new management has not been afforded a chance to show what it can do. This ground of the petition was not mentioned or raised as a ground of defense or objection to the appointment of a receiver in the court below. It is only raised for the first time before Us in the petition for certiorari. The principle has long ago been enunciated by Us that an appellate court may not consider any ground of objection that was not raised in the court below. (*Tan Machan vs. Trinidad*, 3 Phil. 684; *Ramiro vs. Graño*, 54 Phil. 744; *Vda. de Villaruel, et al. vs. Manila Motor Co., Inc., et al.*, 104 Phil., 926; 56 Off. Gaz. (11) 3184; *Collector of Internal Revenue vs. Estate of F. P. Buan, et al.*, G. R. Nos. L-11438-39, and L-11542-46, July 31, 1958; *S. V. S. Pictures, Inc., et al. vs. The Court of Appeals, et al.*, 106 Phil., 897; *Vda. de Caina vs. Hon. Reyes, et al.*, 108 Phil., 513; 58 Off. Gaz., (2) 4745.

The supposed new management alleged as a ground for the reversal of the order of the court below appointing a receiver, is not in itself a ground of objection to the appointment of a receiver. The parties found to be guilty of the fraud, as a cause of which receivership proceedings were instituted, were the Board of Directors, which took no action to stop the anomalies being perpetrated by the management. But it appears that the management must have acted directly under orders of the Board of Directors. The appointment of a new management, therefore, would not remedy the anomalous situation in which the corporation is found, because such situation was not due to the management alone but principally because of direction of the Board of Directors.

The second ground for the petition is, therefore, also without merit.

Wherefore, the court finds that the court below did not commit an abuse of discretion in appointing a receiver for the corporation and the petition to set aside the order for the appointment of a receiver should be, as it is hereby, dismissed. With costs against the petitioner.

Bengzon, C. J., Padilla, Reyes, J. B. L., Paredes, and De Leon, JJ., concur.

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