

THE GOVERNMENT OF THE PHILIPPINE ISLANDS (ON RELATION OF THE ATTORNEY-GENERAL), PLAINTIFF, VS. EL HOGAR FILIPINO, DEFENDANT.*G.R. No. 26649. July 13, 1927*

Ponente: STREET, J.

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This is a quo warranto proceeding instituted originally in this court by the Government of the Philippine Islands on the relation of the Attorney-General against the building and loan association known as El Hogar Filipino, for the purpose of depriving it of its corporate franchise, excluding it from all corporate rights and privileges, and effecting a final dissolution of said corporation. The complaint enumerates seventeen distinct causes of action, to all of which the defendant has answered upon the merits, first admitting the averments of the first paragraph in the statement of the first cause of action, wherein it is alleged that the defendant was organized in the year 1911 as a building and loan association under the laws of the Philippine Islands, and that, since its organization, the corporation has been doing business in the Philippine Islands, with its principal office in the City of Manila. Other facts alleged in the various causes of action in the complaint are either denied in the answer or controverted in legal effect by other facts.

After issue had been thus joined upon the merits, the attorneys entered into an elaborate agreement as to the facts, thereby removing from the field of dispute such matters of fact as are necessary to the solution of the controversy. It follows that we are here confronted only with the legal questions arising upon the agreed statement.

On March 1, 1906, the Philippine Commission enacted what is known as the Corporation Law (Act No. 1459) effective upon April 1 of the same year. Sections 171 to 190, inclusive, of this Act are devoted to the subject of building and loan associations, defining their objects and making various provisions governing their organization and administration, and providing for the supervision to be exercised over them. These provisions appear to be adopted from American statutes governing building and loan associations and they of course reflect the ideals and principles found in American law relative to such associations. The respondent, El Hogar Filipino, was apparently the first corporation organized in the Philippine Islands under the provisions cited, and the association has been favored with extraordinary success. The articles of incorporation bear the date of December 28, 1910, at which time capital stock in the association had been subscribed to the amount of P150,000, of which the sum of P10,620 had been paid in. Under the law as it then stood, the capital of the association was not permitted to exceed P3,000,000, but by Act No. 2092, passed December 23, 1911, the statute was so amended as to permit the capitalization of building and loan associations to the amount of ten millions. Soon thereafter the association took advantage of this enactment by amending its articles so as to provide that the capital should be in an amount not exceeding the then lawful limit. From the time of its first organization the number of shareholders has constantly increased, with the result that on December 31, 1925, the association had 5,826 shareholders holding 125,750 shares, with a total paid-up value of P8,703,602.25. During the period of its existence prior to the date last above-mentioned the association paid to withdrawing stockholders the amount of P7,618,257.72; and in the same

period it distributed in the form of dividends among its stockholders the sum of P7,621,565.81.

First cause of action.—The first cause of action is based upon the alleged illegal holding by the respondent of the title to real property for a period in excess of five years after the property had been bought in by the respondent at one of its own foreclosure sales. The provision of law relevant to the matter is found in section 75 of Act of Congress of July 1, 1902 (repeated in subsection 5 of section 13 of the Corporation Law). In both of these provisions it is in substance declared that while corporations may loan funds upon real estate security and purchase real estate when necessary for the collection of loans, they shall dispose of real estate so obtained within five years after receiving the title.

In this connection it appears that in the year 1920 El Hogar Filipino was the holder of a recorded mortgage upon a tract of land in the municipality of San Clemente, Province of Tarlac, as security for a loan of P24,000 to the shareholders of El Hogar Filipino who were the owners of said property. The borrowers having defaulted in their payments, El Hogar Filipino foreclosed the mortgage and purchased the land at the foreclosure sale for the net amount of the indebtedness, namely, the sum of P23,744.18. The auction sale of the mortgaged property took place November 18, 1920, and the deed conveying the property to El Hogar Filipino was executed and delivered December 22, 1920. On December 27, 1920, the deed conveying the property to El Hogar Filipino was sent to the register of deeds of the Province of Tarlac, with the request that the certificate of title then standing in the name of the former owners be cancelled and that a new certificate of title be issued in the name of El Hogar Filipino. Said deed was received in the office of the register of deeds of Tarlac on December 28, 1920, together with the old certificate of title, and thereupon the register made upon the said deed the following annotation:

"The foregoing document was received in this office at 4.10 p. m., December 28, 1920, according to entry 1898, page 50 of Book One of the Day Book and registered on the back of certificate of title No. 2211 and its duplicate, folio 193 of Book A-10 of the register of original certificate. Tarlac, Tarlac, January 12, 1921. (Sgd.) SILVINO LOPEZ DE JESUS, Register of Deeds."

For months no reply was received by El Hogar Filipino from the register of deeds of Tarlac, and letters were written to him by El Hogar Filipino on the subject in March and April, 1921, requesting action. No answer having been received to these letters, a complaint was made by El Hogar Filipino to the Chief of the General Land Registration Office; and on May 7, 1921, the certificate of title to the San Clemente land was received by El Hogar Filipino from the register of deeds of Tarlac.

On March 10, 1921, the board of directors of El Hogar Filipino adopted a resolution authorizing Vicente Bengzon, an agent of the corporation, to endeavor to find a buyer for the San Clemente land. On July 27, 1921, El Hogar Filipino authorized one Jose Laguardia to endeavor to find a purchaser for the San Clemente land for the sum of P23,000, undertaking to pay the said Laguardia a commission of 5 per centum of the selling price for his services, but no offers to purchase were obtained through this agent or through the agent Bengzon. In July, 1923, plans of the San Clemente land were sent to Mr. Luis Gomez, Mr. J. Gonzalez and Mr. Alfonso de Castelvi, as prospective purchasers, but no offers were received from them. In January, 1926, the agents not having succeeded in finding a buyer, the San Clemente land was advertised for sale by El Hogar Filipino in *El Debate*, *La Vanguardia* and *Taliba*, three newspapers of general circulation in the Philippine Islands published in the City of Manila. On March 16, 1926, the first offer for the purchase of the San Clemente land was received by El Hogar Filipino. This offer was made to it in writing by one Alcantara, who offered to buy it for the sum of P4,000, Philippine currency, payable P500 in cash, and the remainder within thirty days. Alcantara's offer having been reported by the manager of El Hogar Filipino to its board of directors, it was decided, by a resolution adopted at a meeting of the board held on March 25, 1926, to accept the offer, and this acceptance was communicated to the prospective buyer. Alcantara was given successive extensions of the time, the last of which expired April 30,

1926, within which to make the payment agreed upon; and upon his failure to do so El Hogar Filipino treated the contract with him as rescinded, and efforts were made at once to find another buyer. Finally the land was sold to Doña Felipa Alberto for P6,000 by a public instrument executed before a notary public at Manila, P. I., on July 30, 1926.

Upon consideration of the facts above set forth it is evident that the strict letter of the law was violated by the respondent; but it is equally obvious that its conduct has not been characterized by obduracy or pertinacity in contempt of the law. Moreover, several facts connected with the incident tend to mitigate the offense. The Attorney-General points out that the respondent acquired title on December 22, 1920, when the deed was executed and delivered, by which the property was conveyed to it as purchaser at its foreclosure sale, and this title remained in it until July 30, 1926, when the property was finally sold to Felipa Alberto. The interval between these two conveyances is thus more than five years; and it is contended that, as a consequence, the respondent has become amenable to dissolution. For the respondent it is contended that the five year period did not begin to run against the respondent until May 7, 1921, when the register of deeds of Tarlac delivered the new certificate of title to the respondent pursuant to the deed by which the property was acquired. As an equitable consideration affecting the case this contention, though not decisive, is in our opinion more than respectable. It has been held by this court that a purchaser of land registered under the Torrens system cannot acquire the status of an innocent purchaser for value unless his vendor is able to place in his hands an owner's duplicate showing the title of such land to be in the vendor (*Director of Lands vs. Addison*, 49 Phil., 19; *Rodriguez vs. Llorente*, G. R. No. 26615[1]). It results that prior to May 7, 1921, El Hogar Filipino was not really in a position to pass an indefeasible title to any purchaser. In this connection it will be noted that section 75 of the Act of Congress of July 1, 1902, and the similar provision in section 13 of the Corporation Law, allow the corporation "five years after receiving the title," within which to dispose of the property. A fair interpretation of these provisions would seem to indicate that the date of the receiving of the title in this case was the date when the respondent received the owner's certificate, or May 7, 1921, for it was only after that date that the respondent had an unequivocal and unquestionable power to pass a complete title. The failure of the respondent to receive the certificate sooner was not due in any wise to its fault, but to unexplained delay on the part of the register of deeds. For this delay the respondent cannot be held accountable.

Again, it is urged for the respondent that the period between March 25, 1926, and April 30, 1926, should not be counted as part of the five-year period. This was the period during which the respondent was under obligation to sell the property to Alcantara, prior to the rescission of the contract by reason of Alcantara's failure to make the stipulated first payment. Upon this point the contention of the respondent is, in our opinion, well founded. The acceptance by it of Alcantara's offer obligated the respondent to Alcantara; and if it had not been for the default of Alcantara, the effective sale of the property would have resulted. The respondent was not at all chargeable with the collapse of these negotiations; and hence in any equitable application of the law this period should be deducted from the five-year period within which the respondent ought to have made the sale. Another circumstance explanatory of the respondent's delay in selling the property is found in the fact that it purchased the property for the full amount of the indebtedness due to it from the former owner, which was nearly P24,000. It was subsequently found that the property was not salable for anything like that amount and in the end it had to be sold for P6,000, notwithstanding energetic efforts on the part of the respondent to find a purchaser upon better terms.

The question then arises whether the failure of the respondent to get rid of the San Clemente property within five years after it first acquired the deed thereto, even supposing the five-year period to be properly counted from that date, is such a violation of law as should work a forfeiture of its franchise and require a judgment to be entered for its dissolution in this action of quo warranto. Upon this point we do not hesitate to say that in our opinion the

corporation has not been shown to have offended against the law in a manner that should entail a forfeiture of its charter. Certainly no court with any discretion to use in the matter would visit upon the respondent and its thousands of shareholders the extreme penalty of the law as a consequence of the delinquency here shown to have been committed.

The law applicable to the case is in our opinion found in section 212 of the Code of Civil Procedure, as applied by this court in *Government of the Philippine Islands vs. Philippine Sugar Estates Development Co.* (38 Phil., 15). This section (212), in prescribing the judgment to be rendered against a corporation in an action of quo warranto, among other things says:

"* * * When it is found and adjudged that a corporation has offended in any matter or manner which does not by law work as a surrender or forfeiture, or has misused a franchise or exercised a power not conferred by law, but not of such a character as to work a surrender or forfeiture of its franchise, judgment shall be rendered that it be ousted from the continuance of such offense or the exercise of such power."

This provision clearly shows that the court has a discretion with respect to the infliction of capital punishment upon corporations and that there are certain misdemeanors and misusers of franchises which should not be recognized as requiring their dissolution. In *Government of the Philippine Islands vs. Philippine Sugar Estates Development Co.* (38 Phil., 15), it was found that the offending corporation had been largely (though indirectly) engaged in the buying and holding of real property for speculative purposes in contravention of its charter and contrary to the express provisions of law. Moreover, in that case the offending corporation, was found to be still interested in the properties so purchased for speculative purposes at the time the action was brought. Nevertheless, instead of making an absolute and unconditional order for the dissolution of the corporation, the judgment of ouster was made conditional upon the failure of the corporation to discontinue its unlawful conduct within six months after final decision. In the case before us the respondent appears to have rid itself of the San Clemente property many months prior to the institution of this action. It is evident from this that the dissolution of the respondent would not be an appropriate remedy in this case. We do not of course undertake to say that a corporation might not be dissolved for offenses of this nature perpetrated in the past, especially if its conduct had exhibited a willful obduracy and contempt of law. We content ourselves with holding that upon the facts here before us the penalty of dissolution would be excessively severe and fraught with consequences altogether disproportionate to the offense committed.

The evident purpose behind the law restricting the rights of corporations with respect to the tenure of land was to prevent the revival of the entail (mayorazgo) or other similar institution by which land could be fettered and its alienation hampered over long periods of time. In the case before us the respondent corporation has in good faith disposed of the piece of property which appears to have been in its hands at the expiration of the period fixed by law, and a fair explanation is given of its failure to dispose of it sooner. Under these circumstances the destruction of the corporation would bring irreparable loss upon the thousands of innocent shareholders of the corporation without any corresponding benefit to the public. The discretion permitted to this court in the application of the remedy of quo warranto forbids so radical a use of the remedy.

But the case for the plaintiff supposes that the discretion of this court in matters like that now before us has been expressly taken away by the third section of Act No. 2792, and that the dissolution of the corporation is obligatory upon the court upon a mere finding that the respondent has violated the provisions of the Corporation Law in any respect. This makes it necessary to examine the Act last above-mentioned with some care. Upon referring thereto, we find that it consists of three sections under the following style:

"No. 2792.—An Act to amend certain sections of the Corporation Law, Act Numbered Fourteen hundred and fifty-nine, providing for the publication of the assets and liabilities of corporations registering in the Bureau of

Commerce and Industry, determining the liability of the officers of corporations with regard to the issuance of stock or bonds, establishing penalties yfor certain things, and for other purposes."

The first two sections contain amendments to the Corporation Law with respect to matters with which we are not here concerned. The third section contains a new enactment to be inserted as section 190(A) in the corporation Law immediately following section 190. This new section reads as follows:

"SEC. 190. (A). Penalties.—The violation of any of the provisions of this Act and its amendments not otherwise penalized therein, shall be punished by a fine of not more than one thousand pesos, or by imprisonment for not more than five years, or both, in the discretion of the court. If the violation is committed by a corporation, the same shall, upon such violation being proved, be dissolved by quo warranto proceedings instituted by the Attorney-General or by any provincial fiscal, by order of said Attorney-General: Provided, That nothing in this section, provided shall be construed to repeal the other causes for the dissolution of corporations prescribed by existing law, and the remedy provided for in this section shall be considered as additional to the remedies already existing."

The contention for the plaintiff is to the effect that the second sentence in this enactment has entirely abrogated the discretion of this court with respect to the application of the remedy of quo warranto, as expressed in section 212 of the Code of Civil Procedure, and that it is now mandatory upon us to dissolve any corporation whenever we find that it has committed any violation of the Corporation Law, however trivial. In our opinion this radical view of the meaning of the enactment is untenable. When the statute says, "If the violation is committed by a corporation, the same shall, upon such violation being proved, be dissolved by quo warranto proceedings * * *," the intention was to indicate that the remedy against the corporation shall be by action of quo warranto. There was no intention to define the principles governing said remedy, and it must be understood that in applying the remedy the court is still controlled by the principles established in immemorial jurisprudence. The interpretation placed upon this language in the brief of the Attorney-General would be dangerous in the extreme, since it would actually place the life of all corporate investments in the country within the absolute power of a single Government official. No corporate enterprise of any moment can be conducted perpetually without some trivial misdemeanor against corporate law being committed by some one or other of its numerous employees. As illustrations of the preposterous effects of the provision, in the sense contended for by the Attorney-General, the attorneys for the respondent have called attention to the fact that under section 52 of the Corporation Law, a business corporation is required to keep a stock book and a transfer book in which the names of stockholders shall be kept in alphabetical order. Again, under section 94, railroad corporations are required to cause all employees working on passenger trains or at a station for passengers to wear a badge on his cap or hat which will indicate his office. Can it be supposed that the Legislature intended to penalize the violation of such provisions as these by dissolution of the corporation involved? Evidently such could not have been the intention; and the only way to avoid the consequence suggested is to hold, as we now hold, that the provision now under consideration has not impaired the discretion of this court in applying the writ of quo warranto.

Another way to put the same conclusion is to say that the expression "shall be dissolved by quo warranto proceedings" means in effect, "may be dissolved by quo warranto proceedings in the discretion of the court." The proposition that the word "shall" may be construed as "may," when addressed by the Legislature to the courts, is well supported in jurisprudence. In the case of *Becker vs. Lebanon and M. St. Ry. Co.*, (188 Pa., 484), the Supreme Court of Pennsylvania had under consideration a statute providing as follows:

"It shall be the duty of the court * * * t o examine, inquire and ascertain whether such corporation does in fact possess the right or franchise to do the act from which such alleged injury to private rights or to the rights and franchises of other corporations results; and if such rights or franchises have not been conferred upon such corporations, such courts, if exercising equitable power, shall, by injunction, at suit of the private parties or

other corporations, restrain such injurious acts."

In an action based on this statute the plaintiff claimed injunctive relief as a matter of right. But this was denied, the court saying:

"Notwithstanding, therefore, the use of the imperative 'shall,' the injunction is not to be granted unless a proper case for injunction be made out, in accordance with the principles and practice of equity. The word 'shall' when used by the legislature to a court, is usually a grant of authority and means 'may,' and even if it be intended to be mandatory it must be subject to the necessary limitation that a proper case has been made out for the exercise of the power."

Other authorities amply sustain this view (*People vs. Nusebaum*, 66 N. Y. Supp., 129, 133; *West Wisconsin R. Co. vs. Foley*, 94 U. S., 100, 103; 24 Law. Ed., 71; *Clancy vs. McElroy*, 30 Wash., 567; 70 Pac, 1095; *State vs. West*, 3 Ohio State, 509, 511; *In re Lent*, 40 N. Y. Supp., 570, 572; 16 Misc. Rep., 606; *Ludlow vs. Ludlow's Executors*, 4 N. J. Law [1 Southard], 387, 394; *Whipple vs. Eddy*, 161 111., 114; 43 N. E., 789, 790; *Borkheim vs. Fireman's Fund Ins. Co.*, 38 Cal., 505, 506; *Beasley vs. People*, 89 Ill., 571, 575; *Donnelly vs. Smith*, 128 Iowa, 257; 103 N. W., 776).

But section 3 of Act No. 2792 is challenged by the respondent on the ground that the subject-matter of this section is not expressed in the title of the Act, with the result that the section is invalid. This criticism is in our opinion well founded. Section 3 of our organic law (Jones Bill) declares, among other things, that "No bill which may be enacted into law shall embrace more than one subject, and that subject shall be expressed in the title of the bill." Any law or part of a law passed by the Philippine Legislature since this provision went into effect and offending against its requirement is necessarily void.

Upon examining the entire Act (No. 2792), we find that it is directed to three ends which are successively dealt with in the first three sections of the Act. But it will be noted that these three matters all relate to the Corporation Law; and it is at once apparent that they might properly have been embodied in a single Act if a title of sufficient unity and generality had been prefixed thereto. Furthermore, it is obvious, even upon casual inspection, that the subject-matter of each of the first two sections is expressed and defined with sufficient precision in the title. With respect to the subject-matter of section 3 the only words in the title which can be taken to refer to the subjectmatter of said section are these, "An Act * * * establishing penalties for certain things, and for other purposes." These words undoubtedly have sufficient generality to cover the subject-matter of section 3 of the Act. But this is not enough. The Jones Law requires that the subject-matter of the bill "shall be expressed in the title of the bill."

When reference is had to the expression "establishing penalties for certain things," it is obvious that these words express nothing. The constitutional provision was undoubtedly adopted in order that the public might be informed as to what the Legislature is about while bills are in process of passage. The expression "establishing penalties for certain things" would give no definite information to anybody as to the project of legislation intended under this expression. An examination of the decided cases shows that courts have always been indulgent of the practices of the Legislature with respect to the form and generality of title, for if extreme refinements were indulged by the courts, the work of legislation would be unnecessarily hampered. But, as has been observed by the California court, there must be some reasonable limit to the generality of titles that will be allowed. The measure of legality is whether the title is sufficient to give notice of the general subject of the proposed legislation to the persons and interests likely to be affected.

In *Lewis vs. Dunne* (134 Cal., 291), the court had before it a statute entitled "An Act to revise the Code of Civil Procedure of the State of California, by amending certain sections, repealing others, and adding certain new

sections." This title was held to embrace more than one subject, which were not sufficiently expressed in the title. In "discussing the question the court said:

"* * * It is apparent that the language of the title of the act in question, in and of itself, expresses no subject whatever. No one could tell from the title alone what subject of legislation was dealt with in the body of the act; such subject, so far as the title of the act informs us, might have been entirely different from anything to be found in the act itself. * * *

"We cannot agree with the contention of some of respondent's counsel—apparently to some extent countenanced by a few authorities—that the provision of the constitution in question can be entirely avoided by the simple device of putting into the title of an act words which denote a subject 'broad' enough to cover everything. Under that view, the title, 'An act concerning the laws of the state,' would be good, and the convention and people who framed and adopted the constitution would be convicted of the folly of elaborately constructing a grave constitutional limitation of legislative power upon a most important subject, which the legislature could at once circumvent by a mere verbal trick. The word 'subject' is used in the constitution in its ordinary sense; and when it says that an act shall embrace but 'one subject,' it necessarily implies—what everybody knows—that there are numerous subjects of legislation, and declares that only one of these subjects shall be embraced in any one act. All subjects cannot be conjured into one subject by the mere magic of a word in a title. * * *"

In *Rader vs. Township of Union* (39 N. J. L., 509, 515), the Supreme Court of New Jersey made the following observation:

"* * * It is true, that it may be difficult to indicate, by a formula, how specialized the title of a statute must be; but it is not difficult to conclude that it must mean something in the way of being a notice of what is doing. Unless it does this, it can answer no useful end. It is not enough that it embraces the legislative purpose—it must express it; and where the language is too general, it will accomplish the former, but not the latter. Thus, a law entitled 'An act for a certain purpose,' would embrace any subject, but would express none, and, consequently, it would not stand the constitutional test."

The doctrine properly applicable in matters of this kind is, we think, fairly summed up in a current repository of jurisprudence in the following language:

"* * * While it may be difficult to formulate a rule by which to determine the extent to which the title of a bill must specialize its object, it may be safely assumed that the title must not only embrace the subject of proposed legislation, but also express it clearly and fully enough to give notice of the legislative purpose." (25 R. C. L., p. 853.)

In dealing with the problem now before us the words "and for other purposes" found at the end of the caption of Act No. 2792, must be laid completely out of consideration. They express nothing, and amount to nothing as a compliance with the constitutional requirement to which attention has been directed. This expression ("for other purposes") is frequently found in the title of acts adopted by the Philippine Legislature; and its presence in our laws is due to the adoption by our Legislature of the style used in Congressional legislation. But it must be remembered that the legislation of Congress is subject to no constitutional restriction with respect to the title of bills. Consequently, in Congressional legislation the words "and for other purposes" at least serve the purpose of admonishing the public that the bill whose heading contains these words contains legislation upon other subjects than that expressed in the title. Now, so long as the Philippine Legislature was subject to no restriction with respect to the title of bills intended for enactment into general laws, the expression "for other purposes" could be appropriately used in titles, not precisely for the purpose of conveying information as to the matter legislated upon, but for the purpose of admonishing the public that any bill containing such words in the title might contain other subjects than that expressed in the definitive part of the title. But, when Congress adopted the Jones Law,

the restriction with which we are now dealing became effective here and the words "for other purposes" could no longer be appropriately used in the title of legislative bills. Nevertheless, the custom of using these words has still been followed, although they can no longer serve to cover matter not germane" to the bill in the title of which they are used. But the futility of adding these words to the style of any act is now obvious (Cooley, Const. Lims., 8th ed., p. 302).

In the brief for the plaintiff it is intimated that the constitutional restriction which we have been discussing is more or less of a dead letter in this jurisdiction; and it seems to be taken for granted that no court would ever presume to hold a legislative act or part of a legislative act invalid for non-compliance with the requirement. This is a mistake; and no utterance of this court can be cited as giving currency to any such notion. On the contrary the discussion contained in *Central Capiz vs. Ramirez* (40 Phil., 883), shows that when a case arises where a violation of the restriction is apparent, the court has no alternative but to declare the legislation affected thereby to be invalid.

Second cause of action.—The second cause of action is based upon a charge that the respondent is owning and holding a business lot, with the structure thereon, in the financial district of the City of Manila in excess of its reasonable requirements and in contravention of subsection 5 of section 13 of the Corporation Law. The facts on which this charge is based appear to be these:

On August 28, 1913, the respondent purchased 1,413 square meters of land at the corner of Juan Luna Street and the Muelle de la Industria, in the City of Manila, immediately adjacent to the building then occupied by the Hongkong and Shanghai Banking Corporation. At the time the respondent acquired this lot there stood upon it a building, then nearly fifty years old, which was occupied in part by the offices of an importing firm and in part by warehouses of the same firm. The material used in the construction was Guadalupe stone and hewn timber, and the building contained none of the facilities usually found in a modern office building.

In pursuance of a design which had been formed prior to the purchase of the property, the directors of the El Hogar Filipino caused the old building to be demolished; and they erected thereon a modern reinforced concrete office building. As at first constructed the new building was three stories high in the main, but in 1920, in order to obtain greater advantage from the use of the land, an additional story was added to the building, making a structure of four stories except in one corner where an additional story was placed, making it five stories high over an area of 117.52 square meters. It is admitted in the plaintiff's brief that this "noble and imposing structure"—to use the words of the Attorney-General—"has greatly improved the aspect of the banking and commercial district of Manila and has greatly contributed to the movement and campaign for the Manila Beautiful." It is also admitted that the completed building is reasonably proportionate in value and revenue producing capacity to the value of the land upon which it stands. The total outlay of the respondent for the land and the improvements thereon was P690,000 and at this valuation the property is carried on the books of the company, while the assessed valuation of the land and improvements is at P786,478.

Since the new building was completed the respondent has used about 324 square meters of floor space for its own offices and has rented the remainder of the office space in said building, consisting of about 3,175 square meters, to other persons and entities. In the second cause of action of the complaint it is supposed that the acquisition of this lot, the construction of the new office building thereon, and the subsequent renting of the same in great part to third persons, are ultra vires acts on the part of the corporation, and that the proper penalty to be enforced against it in this action is that of dissolution.

With this contention we are unable to agree. Under subsection 5 of section 13 of the Corporation Law, every corporation has the power to purchase, hold and lease such real property as the transaction of the lawful business

of the corporation may reasonably and necessarily require. When this property was acquired in 1916, the business of El Hogar Filipino had developed to such an extent, and its prospects for the future were such as to justify its directors in acquiring a lot in the financial district of the City of Manila and in constructing thereon a suitable building as the site of its offices; and it cannot be fairly said that the area of the lot—1,413 square meters—was in excess of its reasonable requirements. The law expressly declares that corporations may acquire such real estate as is reasonably necessary to enable them to carry out the purposes for which they were created; and we are of the opinion that the owning of a business lot upon which to construct and maintain its offices is reasonably necessary to a building and loan association such as the respondent was at the time this property was acquired. A different ruling on this point would compel important enterprises to conduct their business exclusively in leased offices—a result which could serve no useful end but would retard industrial growth and be inimical to the best interests of society.

We are furthermore of the opinion that, inasmuch as the lot referred to was lawfully acquired by the respondent, it is entitled to the full beneficial use thereof. No legitimate principle can be discovered which would deny to one owner the right to enjoy his (or its) property to the same extent that is conceded to any other owner; and an intention to discriminate between owners in this respect is not lightly to be imputed to the Legislature. The point here involved has been the subject of consideration in many decisions of American courts under statutes even more restrictive than that which prevails in this jurisdiction; and the conclusion has uniformly been that a corporation whose business may properly be conducted in a populous center may acquire an appropriate lot and construct thereon an edifice with facilities in excess of its own immediate requirements.

Thus in *People vs. Pullman's Palace-Car Co.* (175 Ill., 125; 64 L. R. A., 366), it appeared that the respondent corporation owned and controlled a large ten-story business block in the City of Chicago, worth \$2,000,000, and that it occupied only about one-fourth thereof for its own purposes, leasing the remainder to others at heavy rentals. The corporate' charter merely permitted the holding of such real estate by the respondent as might be necessary for the successful prosecution of its business. An attempt was made to obtain the dissolution of the corporation in a quo warranto proceeding similar to that now before us, but the remedy was denied.

In *Rector vs. Hartford Deposit Co.* (190 Ill., 380; 60 N. E., 528), a question was raised as to the power of the Deposit Company to erect and own a fourteen-story building—containing eight storerooms, one hundred suites of offices, and one safety deposit vault, under a statute authorizing the corporation to possess so much real estate "as shall be necessary for the transaction of their business." The court said:

"That the appellee company possessed ample power to acquire real property and construct a building thereon for the purpose of transacting therein the legitimate business of the corporation is beyond the range of debate. Nor is the contrary contented, but the insistence is that, under the guise of erecting a building for corporate purposes, the appellee company purposely constructed a much larger building than its business required, containing many rooms intended to be rented to others for offices and business purposes,—among them, the basement rooms contracted to be leased to the appellant,—and that in so doing it designedly exceeded its corporate powers. The position of appellant, therefore, is that the appellee corporation has flagrantly abused its general power to acquire real estate and construct a building thereon * * * It was within the general scope of the express powers of the appellee corporation to own and possess a building necessary for its proper corporate purposes. In planning and constructing such a building, as was said in *People vs. Pullman's Palace Car Co.*, supra, the corporation should not necessarily be restricted to a building containing the precise number of rooms its then business might require, and no more, but that the future probable growth and volume of its business might be considered and anticipated, and a larger building, and one containing more rooms than the present volume of business required be erected, and the rooms not needed might be rented by the corporation,—provided, of course, such course should be taken in good faith, and not as a mere evasion of the public law and the policy of the state relative to the ownership of real estate by corporations. In such state of case the question

is whether the corporation has abused or excessively and unjustifiably used the power and authority granted it by the state to construct buildings and own real estate necessary for, its corporate purposes."

In *Home Savings Building Association vs. Driver* (129 Ky., 754), one of the questions before the court was precisely the same as that now before us. Upon this point the Supreme Court of Kentucky said:

"The third question is, has the association the right to erect, remodel, or own a building of more than sufficient capacity to accommodate its own business and to rent out the excess? There is nothing in the Constitution, charter of the association, or statutes placing any limitation upon the character of a building which a corporation may erect as a home in which to conduct its business. A corporation conducting a business of the character of that in which appellant is engaged naturally expects its business to grow and expand from time to time, and, in building a home; it would be exercising but a short-sighted judgment if it did not make provision for the future by building a home large enough to take care of its expanding business, and hence, even if it should build a house larger and roomier than its present needs or interests require, it would be acting clearly within the exercise of its corporate right and power. The limitation which the statute imposes is that it shall not own more real estate than is necessary for the proper conduct of its business, but it does not attempt to place any restriction or limitation upon the right of the corporation or association as to the character of building it shall erect on said real estate; and, while the Constitution and the statutes provide that no corporation shall engage in any business other than that expressly authorized by its charter, we are of opinion that, in renting out the unoccupied and unused portions of the building so erected, the association could not be said to be engaged in any other business than that authorized by its charter. The renting of the unused portions of the building is a mere incident in the conduct of its real business. We would not say that a building association might embark in the business of building houses and renting or leasing them, but there is quite a difference in building or renting a house in which to conduct its own business and leasing the unused portion thereof for the time being, or until such time as they may be needed by the association, and in building houses for the purpose of renting or leasing them. The one might properly be said to be the proper exercise of a power incident to the conduct of its legitimate business, whereas the other would be a clear violation of that provision of the statute which denies to any corporation the right to conduct any business other than that authorized by its charter. To hold otherwise would be to charge most of the banking institutions, trust companies and other corporations, such as title guaranty companies, etc., doing business in the state, and especially in the large cities, with violating the law; for it is well known that there are few of such institutions that do not, at times, rent out or lease the unneeded portions of the building occupied by them as homes. We do not think that in so doing they are violating any provisions of the law, but that the renting out of the unused or unoccupied portions of their buildings is but an incident in the conduct of their business."

In *Wingert vs. First National Bank of Hagerstown, Md.* (175 Fed., 739, 741), a stockholder sought to enjoin the bank from building a six-story building on a lot then owned by the bank in the commercial district of Hagerstown of which only the first story was to be used by the bank, the remaining stories to be rented out for offices and places of business, on the theory that such action was ultra vires and in violation of the provisions of the national banking act confining such corporations, to the holding, only, of such real estate "as shall be necessary for its immediate accommodation in the transaction of its business."

The injunction was denied, the court adopting the opinion of the lower court in which the following was said:

"The other ground urged by the complainant is that the proposed action is violative of the restriction which permits a national bank to hold only such real estate as shall be necessary for its immediate accommodation in the transaction of its business, and that, therefore, the erection of a building which will contain offices not necessary for the business of the bank is not permitted by the law, although that method of improving the lot may be the most beneficial use that can be made of it. It is matter of common knowledge that the actual practice of national banks is to the contrary. Where ground is valuable, it may probably be truly said that the majority of national bank buildings are built with accommodations in excess of the needs of the bank for the purpose of lessening the bank's expense by renting out the unused portion. If that were not allowable, many

smaller banks in cities would be driven to become tenants as the great cost of the lot would be prohibitive of using it exclusively for the banking accommodation of a single bank. As indicative of the interpretation of the law commonly received and acted upon, reference may be made to the reply of the Comptroller of the Currency to the inquiry by the bank in this case asking whether the law forbids the bank constructing such a building as was contemplated.

" The reply was as follows: "Your letter of the 9th instant received, stating that the directors contemplate making improvements in the bank building and inquiring if there is anything in the national banking laws prohibiting the construction of a building which will contain floors for offices to be rented out by the bank as well as the banking room. Your attention is called to the case of *Brown vs. Schleier*, 118 Fed., 981 [55 C. C. A., 475], in which the court held that: 'If the land which a national bank purchases or leases for the accommodation of its business is very valuable it may exercise the same rights that belong to other landowners of improving it in a way that will yield the largest income, lessen its own rent, and render that part of its funds which are invested in realty most productive.' " This seems to be the common sense interpretation of the act of Congress and is the one which prevails.' "

It would seem to be unnecessary to extend the opinion by lengthy citations upon the point under consideration, but *Brown vs. Schleier* (118 Fed., 981), may be cited as being in harmony with the foregoing authorities. In dealing with the powers of a national bank the court, in this case, said:

"When an occasion arises for an investment in real property for either of the purposes specified in the statute, the national bank act permits banking associations to act as any prudent person would act in making an investment in real estate, and to exercise the same measure of judgment and discretion. The act ought not to be construed in such a way as to compel a national bank, when it acquires real property for a legitimate purpose, to deal with it otherwise than a prudent landowner would ordinarily deal with such property."

In the brief of the Attorney-General reliance is placed almost entirely upon two Illinois cases, namely, *Africani Home Purchase and Loan Association vs. Carroll* (267 Ill., 380), and *First Methodist Episcopal Church of Chicago vs. Dixon* (178 Ill., 260), In our opinion these cases are either distinguishable from that now before us, or they reflect a view of the law which is incorrect. At any rate the weight of judicial opinion is so overwhelmingly in favor of sustaining the validity of the acts alleged in the second cause of action to have been done by the respondent in excess of its powers that we refrain from commenting at any length upon said cases. The ground stated in the second cause of action is in our opinion without merit.

Third cause of action.—Under the third cause of action the respondent is charged with engaging in activities foreign to the purposes for which the corporation was created and not reasonably necessary to its legitimate ends. The specifications under this cause of action relate to three different sorts of activities. The first consists of the administration of the offices in the El Hogar building not used by the respondent itself and the renting of such offices to the public. As stated in the discussion connected with the second cause of action, the respondent uses only about ten per cent of the office space in the El Hogar building for its own purposes, and it leases the remainder to strangers. In the years 1924 and 1925 the respondent received as rent for the leased portions of the building the sums of P75,395.06 and P58,259.27, respectively. The activities here criticised clearly fall within the legitimate powers of the respondent, as shown in what we have said above relative to the second cause of action. This matter will therefore no longer detain us. If the respondent had the power to acquire the lot, construct the edifice and hold it beneficially, as there decided, the beneficial administration by it of such parts of the building as are let to others must necessarily be lawful.

The second specification under the third cause of action has reference to the administration and management of properties belonging to delinquent shareholders of the association. In this connection it appears that in case of delinquency on the part of its shareholders in the payment of interest, premiums, and dues, the association has

been accustomed (pursuant to clause 8 of its standard mortgage) to take over and manage the mortgaged property for the purpose of applying the income to the obligations of the debtor party. For these services the respondent charges a commission at the rate of 2 1/2 per centum on sums collected. The case for the Government supposes that the only remedy which the respondent has in case of default on the part of its shareholders is to proceed to enforce collection of the whole loan in the manner contemplated in section 185 of the Corporation Law. It will be noted, however, that, according to said section, the association may treat the whole indebtedness as due, "at the option of the board of directors," and this remedy is not made exclusive. We see no reason to doubt the validity of the clause giving the association the right to take over the property which constitutes the security for the delinquent debt and to manage it with a view to the satisfaction of the obligations due to the association. Such course is certainly more favorable to the debtor than the immediate enforcement of the entire obligation, and the validity of the clause allowing this course to be taken appears to us to be not open to doubt. The second specification under this cause of action is therefore without merit, as was true of the first.

The third specification under this cause of action relates to certain activities which are described in the following paragraphs contained in the agreed statement of facts:

"El Hogar Filipino has undertaken the management of some parcels of improved real estate situated in Manila not under mortgage to it, but owned by shareholders, and has held itself out by advertisement as prepared to do so. The number of properties so managed during the years to 1925, inclusive, was as follows:

1921 eight properties

1922 six properties

1923 ten properties

1924 fourteen properties

1925 fourteen properties

This service is limited to shareholders; but some of the persons whose properties are so managed for them became shareholders only to enable them to take advantage thereof.

"The services rendered in the management of such improved real estate by El Hogar Filipino consist in the renting of the same, the payment of real estate taxes and insurance for the account of the owner, causing the necessary repairs for upkeep, to be made, and collecting rents due from tenants. For the services so rendered in the management of such properties El Hogar Filipino receives compensation in the form of commissions upon the gross receipts from such properties at rates varying from two and one-half per centum to five per centum of the sums so collected, according to the location of the property and the effort involved in its management.

"The work of managing real estate belonging to non-borrowing shareholders administered by El Hogar Filipino is carried on by the same members of the staff who attend to the details of the management of properties administered by the manager of El Hogar Filipino under the provisions of paragraph 8 of the standard mortgage form, and of properties bought in on foreclosure of mortgage."

The practice described in the passage above quoted from the agreed facts is in our opinion unauthorized by law. Such was the view taken by the bank examiner of the Treasury Bureau in his report to the Insular Treasurer on December 21, 1925, wherein the practice in question was criticised. The administration of property in the manner described is more befitting to the business of a real estate agent or trust company than to the business of a building and loan association. The practice to which this criticism is directed relates of course solely to the management and administration of properties which are not mortgaged to the association. The circumstance that the owner of the property may have been required to subscribe to one or more shares of the association with a view to qualifying him to receive this service is of no significance. It is a general rule of law that corporations possess only such express powers as are actually conferred and such implied powers as are reasonably necessary to the

exercise of the express powers. The management and administration of the property of the shareholders of the corporation is not expressly authorized by law, and we are unable to see that, upon any fair construction of the law, these activities are necessary to the exercise of any of the granted powers. The corporation, upon the point now under criticism, has clearly extended itself beyond the legitimate range of its powers. But it does not result that the dissolution of the corporation is in order, and it will merely be enjoined from further activities of this sort.

Fourth cause of action.—It appears that among the by-laws of the association there is an article (No. 10) which reads as follows:

"The board of directors of the association, by the vote of an absolute majority of its members, is empowered to cancel shares and to return to the owner thereof the balance resulting from the liquidation thereof whenever, by reason of their conduct, or for any other motive, the continuation as members of the owners of such shares is not desirable."

This by-law is of course a patent nullity, since it is in direct conflict with the latter part of section 187 of the Corporation Law, which expressly declares that the board of directors shall not have the power to force the surrender and withdrawal of miniaturized stock except in case of liquidation of the corporation or of forfeiture of the stock for delinquency. It is agreed that this provision of the by-laws has never been enforced, and in fact no attempt has ever been made by the board of directors to make use of the power therein conferred. In November, 1923, the Acting Insular Treasurer addressed a letter to El Hogar Filipino, calling attention to article 10 of its by-laws and expressing the view that said article was invalid. It was therefore suggested that the article in question should be eliminated from the by-laws. At the next meeting of the board of directors the matter was called to their attention and it was resolved to recommend to the shareholders that in their next annual meeting the article in question be abrogated. It appears, however, that no annual meeting of the shareholders called since that date has been attended by a sufficient number of shareholders to constitute a quorum, with the result that the provision referred to has not been eliminated from the by-laws, and it still stands among the by-laws of the association, notwithstanding its patent conflict with the law.

It is supposed, in the fourth cause of action, that the existence of this article among the by-laws of the association is a misdemeanor on the part of the respondent which justifies its dissolution. In this view we are unable to concur. The obnoxious by-law, as it stands, is a mere nullity, and could not be enforced even if the directors were to attempt to do so. There is no provision of law making it a misdemeanor to incorporate an invalid provision in the by-laws of a corporation; and if there were such, the hazards incident to corporate effort would certainly be largely increased. There is no merit in this cause of action.

Fifth cause of action.—In section 31 of the Corporation Law it is declared that, "at all elections of directors there must be present, either in person or by representative authorized to act by written proxy, the owners of the majority of the subscribed capital stock entitled to vote, * * *." Conformably with this requirement it is declared in article 61 of the by-laws of El Hogar Filipino that, "the attendance in person or by proxy of shareholders owning one-half, plus one of the shareholders shall be necessary to constitute a quorum for the election of directors. At the general annual meetings of the El Hogar Filipino held in the years 1911 and 1912, there was a quorum of shares present or represented at the meetings and directors were duly elected accordingly. As the corporation has grown, however, it has been found increasingly difficult to get together a quorum of the shareholders, or their proxies, at the annual meetings; and with the exception of the annual meeting held in 1917, when a new directorate was elected, the meetings have failed for lack of quorum. It has been foreseen by the officials in charge of the respondent that this condition of affairs would lead to emr barrassment, and a special effort was made by the management to induce a sufficient number of shareholders to attend the annual meeting for February, 1923. In addition to the publication of notices in the newspapers, as required by the by-laws, a letter

of notification was sent to every shareholder at his last known address, together with a blank form of proxy to be used in the event the shareholder could not personally attend the meeting. Notwithstanding these special efforts the meeting was attended only by shareholders, in person and by proxy, representing 3,889 shares, out of a total of 106,491 shares then outstanding and entitled to vote.

Owing to the failure of a quorum at most of the general meetings since the respondent has been in existence, it has been the practice of the directors to fill vacancies in the directorate by choosing suitable persons from among the stockholders. This custom finds its sanction in article 71 of the by-laws, which reads as follows:

"Art. 71. The directors shall elect from among the shareholders members to fill the vacancies that may occur in the board of directors until the election at the general meeting."

The persons thus chosen to fill vacancies in the directorate have it is admitted, uniformly been experienced and successful business and professional men of means, enjoying earned incomes of from P12,000 to P50,000 per annum, with an annual average of P30,000 in addition to such income as they derive from their properties. Moreover, it appears that several of the individuals constituting the original directorate and persons chosen to supply vacancies therein belong to prominent Filipino families, and that they are more or less related to each other by blood or marriage. In addition to this it appears that it has been the policy of the directorate to keep thereon some member or another of a single prominent American law firm in the city.

It is supposed in the statement of the fifth cause of action in the complaint that the failure of the corporation to hold annual meetings and the filling of vacancies in the directorate in the manner described constitute misdemeanors on the part of the respondent which justify the resumption of the franchise by the Government and dissolution of the corporation; and in this connection it is charged that the board of directors of the respondent has become a permanent and self-perpetuating body composed of wealthy, men instead of wage earners and persons of moderate means. We are unable to see the slightest merit in the charge. No fault can be imputed to the corporation on account of the failure of the shareholders to attend the annual meetings; and their non-attendance at such meeting to be interpreted in part as expressing their satisfaction at the way in which things have been conducted. Upon failure of a quorum at any annual meeting the directorate naturally holds over and continues to function until another directorate is chosen and qualified. Unless the law or the charter of a corporation expressly provides that an office shall become vacant at the expiration of the term of office for which the officer was elected, the general rule is to allow the officer to hold over until his successor is duly qualified. Mere failure of a corporation to elect officers does not terminate the terms of existing officers nor dissolve the corporation (*Quitman Oil Company vs. Peacock*, 14 Ga. App., 550; *Jenkins vs. Baxter*, 160 Pa. State, 199; *New York B. & E. Ry. Co. vs. Motil*, 81 Conn., 466; *Hatch vs. Lucky Bill Mining Company*, 71 Pac, 865; *Youree vs. Home Town Mutual Ins. Company*, 180 Missouri, 153; *Cassell vs. Lexington, H. & P. Turnpike Road Co.*, 10 Ky. L. R., 486). The doctrine above stated finds expression in article 66 of the by-laws of the respondent which declares in so many words that directors shall hold office "for the term of one year or until their successors shall have been elected and taken possession of their offices."

It results that the practice of the directorate of filling the vacancies by the action of the directors themselves is valid. Nor can any exception be taken to the personality of the individuals chosen by the directors to fill vacancies in the body. Certainly it is no fair criticism to say that they have chosen competent businessmen of financial responsibility instead of electing poor persons to so responsible a position. The possession of means does not disqualify a man for filling positions of responsibility in corporate affairs.

Sixth cause of action.—Under the sixth cause of action it is alleged that the directors of El Hogar Filipino, instead of serving without pay, or receiving nominal pay or a fixed salary,—as the complaint supposes would be proper,—have been receiving large compensation, varying in amount from time to time, out of the profits of the respondent.

The facts relating to this cause of action in substance these:

Under section 92 of the by-laws of El Hogar Filipino 5 per centum of the net profit shown by the annual balance sheet is distributed to the directors in proportion to their attendance at meetings of the board. The compensation paid to the directors from time to time since the organization was organized in 1910 to the end of the year 1925, together with the number of meetings of the board held each year, is exhibited in the following table:

Year

Compensation paid directors as a whole

Number of meetings held

Rate per meeting as a whole

1911.....
1912.....
1913.....
1914.....
1915.....
1916.....
1917.....
1918.....
1919.....
1920.....
1921.....
1922.....
1923.....
1924.....
1925.....

P4,167.96

10,511.87

15,479.29

19,164.72

24,032.85

27,539.50

31,327.00

32,858.35

36,318.78

63,517.01

36,815.33

43,133.73

39,773.61

38,651.92

35,719.27

25

29

27

27

25

28

26

20

21

28

25

25

27

26

26

P166.71

362.47

573.30

709.80

961.31

983.55

1,204.88

1,642.91

1,729.46

2,268.46

1,472.61

1,725.34

1,473.09

1,486.61

1,373.81

It will be noted that the compensation above indicated as accruing to the directorate as a whole has been divided among the members, actually present at the different meetings. As a result this practice, and the liberal measure of compensation adopted, we find that, the attendance of the membership at the board meetings has been extraordinarily good. Thus, during the years 1920 to 1925, inclusive, when the board was composed of nine members, the attendance has regularly been eight at each meeting with the exception of two years when the average attendance was seven. It is insisted in the brief for the Attorney-General that the payment of the compensation indicated is excessive and prejudicial to the interests of the shareholders at large. For the respondent, attention is directed to the fact that the liberal policy adopted by the association with respect to the compensation of the directors has had highly beneficial results, not only in securing a constant attendance on the part of the membership, but in obtaining their intelligent attention to the affairs of the association. Certainly, in this connection, the following words from the report of the Government examiners for 1918 to the Insular Treasurer contain matter worthy of consideration:

"The management of the association is entrusted to men of recognized ability in financial affairs and it is believed that they have long foreseen all possible future contingencies and that under such men the interests of the stockholders are duly protected. The steps taken by the directorate to curtail the influx of unnecessary capital into the Association's coffers, as mentioned above, reveals how the men at the helm of the Association

are always on the lookout to grasp the situation and to apply the necessary remedy as the circumstances may require. The accounts and documents were found in the same excellent condition as in the previous examination."

In so far as this court is concerned the question here before us is not one concerning the propriety and wisdom of the measure of compensation adopted by the respondent but rather the question of the validity of the measure. Upon this point there can, it seems to us¹, be no difference of intelligent opinion. The Corporation Law does not undertake to prescribe the rate of compensation for the directors of corporations. The power to fix the compensation they shall receive, if any, is left to the corporation, to be determined in its by-laws (Act No. 1459, sec. 21). Pursuant to this authority the compensation for the directors of El Hogar Filipino has been fixed in section 92 of its by-laws, as already stated. The justice and propriety of this provision was a proper matter for the shareholders when the by-laws were framed; and the circumstance that, with the growth of the corporation, the amount paid as compensation to the directors has increased beyond what would probably be necessary to secure adequate service from them is a matter that cannot be corrected in this action; nor can it properly be made a basis for depriving the respondent of its franchise, or even for enjoining it from compliance with the provisions of its own by-laws. If a mistake has been made, or the rule adopted in the by-laws has been found to work harmful results, the remedy is in the hands of the stockholders who have power at any lawful meeting to change the rule. The remedy, if any seems to lie rather in publicity and competition, rather than in a court proceeding. The sixth cause of action is in our opinion without merit.

Seventh cause of action.—It appears that the promoter and organizer of El Hogar Filipino was Mr. Antonio Melian, and in the early stages of the organization of the association the board of directors authorized the association to make a contract with him with regard to the services to be rendered by him and the compensation to be paid to him therefor. Pursuant to this authority the president of the corporation, on January 11, 1911, entered into a written agreement with Mr. Melian, which is reproduced in the agreed statement of facts and of which the important clauses are these:

"1. The corporation 'El Hogar Filipino Sociedad Mutua de Construccion y Prestamos' and on its behalf its president, Don Antonio R. Roxas, hereby confers on Don Antonio Melian the office of manager of said association for the period of one year from the date of this contract.

"2. Don Antonio Melian accepts said office and undertakes to render the services thereto corresponding for the period of one year, as prescribed by the by-laws of the corporation, without salary.

"3. Don Antonio Melian furthermore undertakes to pay, for his own account, all the expenses incurred in the organization of the corporation.

"4. Don Antonio Melian further undertakes to lend to the corporation, without interest, the sum of six thousand pesos (P6,000), Philippine currency, for the purpose of meeting the expense of rent, office supplies, etcetera, until such time as the association has sufficient funds of its own with which to return this loan: Provided, nevertheless, That the maximum period thereof shall not exceed three (3) years.

"5. Don Antonio Melian undertakes that the capital of the association shall amount to the sum of four hundred thousand pesos (P400,000), Philippine currency, par value, during the first year of its duration.

"6. In compensation of the studies made and services rendered by Don Antonio Melian for its organization, the expenses incurred by him to that end, and in further consideration of the said loan of six thousand pesos (P6,000), and of the services to be rendered by him as manager, and of the obligation assumed by him that the nominal value of the capital of the association shall reach the sum of four hundred thousand pesos (P400,000) during the first year of its duration, the corporation 'El Hogar Filipino Sociedad Mutua de Construccion y Prestamos' hereby grants him five per centum (5%) of the net profits to be earned by it in each year during the

period fixed for the duration of the association by its articles of incorporation; Provided, That this participation in the profits shall be transmitted to the heirs of Señor Melian in the event of his death; And provided further, That the performance of all the obligations assumed by Senor Melian in favor of the association, in accordance with this contract, shall and does constitute a condition precedent to the acquisition by Senor, Melian of the right to the said participation in the profits of the association, unless the non-performance of such obligations shall be due to a fortuitous event or force majeure."

In conformity with this agreement there was inserted in section 92 of the by-laws of the association a provision recognizing the rights of Mr. Melian, as founder, to 5 per centum of the net profits shown by the annual balance sheet, payment of the same to be made to him or his heirs during the life of the association. It is declared in said article that this portion of the earnings of the association is conceded to him in compensation for the studies, work and contributions made by him for the organization of El Hogar Filipino, and the performance on his part of the contract of January 11, 1911, above quoted. During the whole life of the association, thus far, it has complied with the obligations assumed by it in the contract above-mentioned; and during the years 1911 to 1925, inclusive, it paid to him as founder's royalty the sum of P459,011.19, in addition to compensation received from the association by him in remuneration of services to the association in various official capacities.

As a seventh cause of action it is alleged in the complaint that this royalty of the founder is "unconscionable, excessive and out of all proportion to the services rendered, besides being contrary to and incompatible with the spirit and purpose of building and loan associations." It is not alleged that the making of this contract was beyond the powers of the association (*ultra vires*); nor is it alleged that it is vitiated by fraud of any kind in its procurement; Nevertheless, it is pretended that in making and observing said contract the respondent committed an offense requiring its dissolution, or, as is otherwise suggested, that the association should be enjoined from preforming the agreement.

It is our opinion that this contention is entirely without merit. Stated in its true simplicity, the primary question here is whether the making of a (possibly) indiscreet contract is a capital offense in a corporation,—a question which answers itself. No possible doubt exists as to the power of a corporation to contract for services rendered and to "be rendered by a promoter in connection with organizing and maintaining the corporation. It is true that contracts with promoters must be characterized by good faith; but could it be said with certainty, in the light of facts existing at the time this contract was made, that the compensation therein provided was excessive? If the amount of the compensation now appears to be a subject of legitimate criticism, this must be due to the extraordinary development of the association in recent years.

If the Melian contract had been clearly *ultra vires*—which is not charged and is certainly untrue—its continued performance might conceivably be enjoined in such a proceeding as this; but if the defect from which it suffers is mere matter for an action of nullity, an injunction cannot be obtained in this action because Melian is not a party. It is rudimentary in law that an action to annul a contract cannot be maintained without joining both the contracting parties as defendants. Moreover, the proper party to bring such an action is either the corporation itself, or some shareholder who has an interest to protect.

The mere fact that the compensation paid under this contract is in excess of what, in the full light of history, may be considered appropriate is not a proper consideration for this court, and supplies no ground for interfering with its performance. In the case of *El Hogar Filipino vs. Rafferty* (37 Phil., 995), which was before this court nearly ten years ago, this court held that the El Hogar Filipino is a mutual benefit society and that the existence of this contract with Mr. Melian did not affect the association's legal character. The inference is that the contract under consideration was then considered binding, and it occurred to no one that it was invalid. It would be a radical step indeed for a court to attempt to substitute its judgment for the judgment of the contracting parties and to hold, as

we are invited to hold under this cause of action, that the making of such a contract as this removes the respondent association from the pale of the law. The majority of the court is of the opinion that our traditional respect for the sanctity of the contract obligation should prevail over the radical and innovating tendencies which find acceptance with some and which, if given full rein, would go far to sink legitimate enterprise in the Islands into the pit of populism and bolshevism. The seventh count is not sustainable.

Eighth cause of action.—Under the fourth cause of action we had a case where the alleged ground for the revocation of the respondent's charter was based upon the presence in the by-laws of article 10 that was found to be inconsistent with the express provisions of law. Under the eighth cause of action the alleged ground for putting an end to the corporate life of the respondent is found in the presence of other articles in the by-laws, namely, articles 70 and 76, which are alleged to be unlawful but which, as will presently be seen, are entirely valid. Article 70 of the by-laws in effect requires that persons elected to the board of directors must be holders of shares of the paid up value of P5,000, which shall be held as security for their action; but it is added that said security may be put up in the behalf of any director by some other holder of shares in the amount stated. Article 76 of the by-laws declares that the directors waive their right as shareholders to receive loans from the association.

It is asserted, under the eighth cause of action, that article 70 is objectionable in that, under the requirement for security, a poor member, or wage-earner, cannot serve as director, irrespective of other qualifications, and that as a matter of fact only men of means actually sit on the board. Article 76 is criticized on the ground that the provision requiring directors to renounce their right to loans unreasonably limits their rights and privileges as members. There is nothing of value in either of these suggestions. Section 21 of the Corporation Law expressly gives the power to the corporation to provide in its by-laws for the qualifications of directors; and the requirement of security from them for the proper discharge of the duties of their office, in the manner prescribed in article 70, is highly prudent and in conformity with good practice. Article 76, prohibiting directors from making loans to themselves, is of course designed to prevent the possibility of the looting of the corporation by unscrupulous directors. A more discreet provision to insert in the by-laws of a building and loan association would be hard to imagine. Clearly, the eighth cause of action cannot be sustained.

Ninth cause of action.—The specification under this head is in effect that the respondent has abused its franchise in issuing "special" shares. The issuance of these shares is alleged to be illegal and inconsistent with the plan and purposes of building and loan associations; and in particular, it is alleged that they are, in the main, held by well-to-do people purely for purposes of investment and not by wage-earners for accumulating their modest savings for the building of homes.

In the articles of incorporation we find the special shares described as follows:

" 'Special' shares shall be issued upon the payment of 80 per cent of their par value in cash, or in monthly dues of P10. The 20 per cent remaining of the par value of such shares shall be completed by the accumulation thereto of their proportionate part of the profits of the corporation. At the end of each quarter the holders of special shares shall be entitled to receive in cash such part of the net profits of the corporation corresponding to the amount on such date paid in by the holders of special shares, on account thereof, as shall be determined by the directors, and at the end of each year the full amount of the net profits available for distribution corresponding to the special shares. The directors shall apply such part as they deem advisable to the amortization of the subscription to capital with respect to shares not fully paid up, and the remainder of the profits, if any, corresponding to such shares, shall be delivered to the holders thereof in accordance with the provisions of the by-laws."

The ground for supposing the issuance of the "special" shares to be unlawful is that special shares are not mentioned in the Corporation Law as one of the forms of security which may be issued by the association. In the

agreed statement of facts it is said that special shares are issued upon two plans. By the first, the subscriber pays to the association, upon subscribing, P160 in cash, on account of each share. By the second, the shareholder, upon subscribing, pays in cash P10 for each share taken, and undertakes to pay P10 a month, as dues, until the total so paid in amounts to P160 per share. On December 31, 1925, there were outstanding 20,844 special shares of a total paid value (including accumulations) of P3,680,162.51. The practice of El Hogar Filipino, since 1915, has been to accumulate to each special, share, at the end of the year, one-tenth of the dividend declared and to pay the remainder of the dividend in cash to the holders of shares. Since the same year dividends have been declared on the special and common shares at the rate of 10 per centum per annum. When the amount paid in upon any special share plus the accumulated dividends accruing to it, amounts to the par value of the share (P200), such share matures and ceases to participate further in the earnings. The amount of the par value of the share (P200) is then returned to the shareholder and the share cancelled. Holders of special and ordinary shares participate ratably in the dividends declared and distributed, the part pertaining to each share being computed on the basis of the capital paid in, plus the accumulated dividends pertaining to each share at the end of the year. The total number of shares of El Hogar Filipino outstanding on December 31, 1925, was 125,750, owned by 5,826 shareholders, and divided into classes as follows:

Preferred shares	1,503
Special shares.....	20,884
Ordinary shares	103,363

The matter of the propriety of the issuance of special shares by El Hogar Filipino has been before this court in two earlier cases, in both of which the question has received the fullest consideration from this court. In *El Hogar Filipino vs. Rafferty* (37 Phil., 995), it was insisted that the issuance of such shares constituted a departure on the part of the association from the principle of mutuality; and it was claimed by the Collector of Internal Revenue that this rendered the association liable for the income tax to which other corporate entities are subject. It was held that this contention was untenable and that El Hogar Filipino was a legitimate building and loan association notwithstanding the issuance of said shares. In *Severino vs. El Hogar Filipino* (G. R. No. 24926),^[1] and the related cases of *Gervasio Mirafiores* and *Gil Lopez* against the same entity, it was asserted by the plaintiffs that the emission of special shares deprived the herein respondent of the privileges and immunities of a building and loan association and that as a consequence the loans that had been made to the plaintiffs in those cases were usurious. Upon an elaborate review of the authorities, the court, though divided, adhered to the principle announced in the earlier case and held that the issuance of the special shares did not affect the respondent's character as a building and loan association nor make its loans usurious. In view of the lengthy discussion contained in the decisions above-mentioned, it would appear to be an act of supererogation on our part to go over the same ground again. The discussion will therefore not be repeated, and what is now to be said should be considered supplemental thereto.

Upon examination of the nature of the special shares in the light of American usage, it will be found that said shares are precisely the same kind of shares that, in some American jurisdictions, are generally known as advance-payment shares; and if close attention be paid to the language used in the last sentence Of section 178 of the Corporation Law, it will be found that special shares were evidently created for the purpose of meeting the conditions caused by the prepayment of dues that is there permitted. The language of this provision is as follows: "Payments of dues or interest may be made in advance, but the corporation shall not allow interest on such advance payments at a greater rate than six per centum per annum nor for a longer period than one year." In one sort of special shares the dues are prepaid to the extent of P160 per share; in the other sort prepayment is made in the amount of P10 per share, and the subscribers assume the obligation to, pay P10 monthly until P160 shall have been paid.

It will not escape notice that the provision quoted says that interest shall; not be allowed on advance payments at a greater rate than 6 per centum per annum nor for a longer period than one year. The word "interest" as there used must be taken in its true sense of compensation for the use of money loaned, and it must not be confused with the dues upon which it is contemplated that the interest may be paid. Now, in the absence of any showing to the contrary, we infer that no interest is ever paid by the association in any amount for the advance payments made on these shares; and the reason is to be found in the fact that the participation of the special shares in the earnings of the corporation, in accordance with section 188 of the Corporation Law, sufficiently compensates the shareholder for the advance payments made by him; and no other incentive is necessary to induce investors to purchase the stock.

It will be observed that the final 20 per centum of the par value of each special share is not paid for by the shareholder with funds out of the pocket. The amount is satisfied by applying a portion of the shareholder's participation in the annual earnings. But as the right of every shareholder to such participation in the earnings is undeniable, the portion thus annually applied is as much the property of the shareholder as if it were in fact taken out of his pocket. It follows that the emission of the special shares does not involve any violation of the principle that the shares must be sold at par.

From what has been said it will be seen that there is express authority, even in the very letter of the law, for the emission of advance-payment or "special" shares, and the argument that these shares are invalid is seen to be baseless. In addition to this it is satisfactorily demonstrated in *Severino vs. El Hogar Filipino*, supra, that even assuming that the statute has not expressly authorized such shares, yet the association has implied authority to issue them. The complaint consequently fails also as regards the ground stated in the ninth cause of action.

Tenth cause of action.—Under this head of the complaint it is alleged that the defendant is pursuing a policy of depreciating, at the rate of 10 per centum per annum, the value of the real properties acquired by it at its sales; and it is alleged that this rate is excessive. From the agreed statement it appears that since its organization in 1910 *El Hogar Filipino*, prior to the end of the year 1925, had made 1,373 loans to its shareholders secured by first mortgages on real estate as well as by the pledge of the shares of the borrowers. In the same period the association has purchased at foreclosure sales the real estate constituting the security for 54 of the aforesaid loans. In making these purchases the association has always bid the full amount due to it from the debtor, after deducting the withdrawal value of the shares pledged as collateral, with the result that in no case has the shareholder been called upon to pay a deficiency judgment on foreclosure.

El Hogar Filipino places real estate so purchased in its inventory at actual cost, as determined by the amount bid on foreclosure sale; and thereafter until sold the book value of such real estate is depreciated at the rate fixed by the directors in accordance with their judgment as to each parcel, the annual average depreciation having varied from nothing to a maximum of 14.138 per cent. The book value of such real estate is not followed in making sales thereof, but sales are made for the best prices obtainable, whether greater or less than the book value.

It is alleged in the complaint that depreciation is charged by the association at the rate of 10 per centum per annum. The agreed statement of facts on this point, shows that the annual average varies from nothing to a maximum of something over 14 per centum. We are thus left in the dark as to the precise depreciation allowed from year to year. It is not claimed for the Government that the association is without power to allow some depreciation; and it is quite clear that the board of directors possesses a discretion in this matter. There is no positive provision of law prohibiting the association from writing off a reasonable amount for depreciation on its assets for the purpose of determining its real profits; and article 74 of its by-laws expressly authorizes the board of directors to determine each year the amount to be written down upon the expenses of installation and the property of the corporation. There can be no question that the power to adopt such a by-law is embraced within the power

to make by-laws for the administration of the corporate affairs of the association and for the management of its business, as well as the care, control and disposition of its property (Act No. 1459, sec. 13 [7]). But the Attorney-General questions the exercise of the discretion confided to the board; and it is insisted that the excessive depreciation of the property of the association is objectionable in several respects, but mainly because it tends to increase unduly the reserves of the association, thereby frustrating the right of the shareholders to participate annually and equally in the earnings of the association.

This count of the complaint proceeds, in our opinion, upon an erroneous notion as to what a court may do in determining the internal policy of a business corporation. If the criticism contained in the brief of the Attorney-General upon the practice of the respondent association with respect to depreciation be well founded, the Legislature should supply the remedy by defining the extent to which depreciation may be allowed by building and loan associations. Certainly this court cannot undertake to control the discretion of the board of directors of the association about an administrative matter as to which they have legitimate power of action. The tenth cause of action 4s therefore not well founded.

Eleventh and twelfth causes of action.—The same comment is appropriate with respect to the eleventh and twelfth causes of action, which are treated together in the briefs, and will be here combined. The specification in the eleventh cause of action is that the respondent maintains excessive reserve funds, and in the twelfth cause of action that the board of directors has settled upon the unlawful policy of paying a straight annual dividend of 10 per centum, regardless of losses suffered and profits made by the corporation and in contravention of the requirements of section 188 of the Corporation Law. The facts relating to these two counts in the complaint, as set forth in the stipulation, are these:

In article 92 of the by-laws of El Hogar Filipino it is provided that 5 per centum of the net profits earned each year, as shown by the annual balance sheet shall be carried to a reserve fund. The fund so created is called the General Reserve. Article 93 of the by-laws authorizes the directors to carry funds to a Special Reserve, whenever in their judgment it is advisable to do so, provided that the annual dividend in the year in which funds are carried to special reserve exceeds 8 per centum. It appears to have been the policy of the board of directors for several years past to place in the special reserve any balance in the profit and loss account after the satisfaction of preferential charges and the payment of a dividend of 10 per centum to all special and ordinary shares (with accumulated dividends) . As things stood in 1926 the General Reserve contained an amount equivalent to about 5 per centum of the paid-in value of shares. This fund has never been drawn upon for the purpose of maintaining the regular annual dividend; but recourse has been had to the Special Reserve on three different occasions to make good the amount necessary to pay dividends. It appears that in the last five years the reserves have declined from something over 9 per cent to something over 7.

It is insisted in the brief of the Attorney-General that the maintenance of reserve funds is unnecessary in the case of building and loan associations, and at any rate the keeping of reserves is inconsistent with section 188 of the Corporation Law. Moreover, it is said that the practice of the association in declaring regularly a 10 per cent dividend is in effect a guaranty by the association of a fixed dividend which is contrary to the intention of the statute.

Upon careful consideration of the questions involved we find no reason to doubt the right of the respondent to maintain these reserves. It is true that the Corporation Law does not expressly grant this power, but we think it is to be implied. It is a fact of common observation that all commercial enterprises encounter periods when earnings fall below the average, and the prudent manager makes provision for such contingencies. To regard all surplus as profit is to neglect one of the primary canons of good business practice. Building and loan associations, though among the most solid of financial institutions, are nevertheless subject to vicissitudes. Fluctuations in the dividend

rate are highly detrimental to any fiscal institutions, while uniformity in the payments of dividends, continued over long periods, supplies the surest foundation of public confidence.

The question now under consideration is not new in jurisprudence, for the American courts have been called upon more than once to consider the legality of the maintenance of reserves by institutions of this or similar character.

In *Greeff vs. Equitable Life Assurance Society* (160 N. Y., 19; 73 Am. St. Rep., 659), the court had under consideration a charter provision of a life insurance company, organized on the mutual plan, in its relation to the power of the company to provide reserves. There the statute provided that "the officers of the company, within sixty days from the expiration of the first five years, from December 31, 1859, and within the first sixty days of every subsequent period of five years, shall cause a balance to be struck of the affairs of the company, which shall exhibit its assets and liabilities, both present and contingent and also the net surplus, after deducting a sufficient amount to cover all outstanding risks and other obligations. Each policy holder shall be credited with an equitable share of the said surplus."

The court said:

"No prudent person would be inclined to take a policy in a company which had so improvidently conducted its affairs that it only retained a fund barely sufficient to pay its present liabilities, and, therefore, was in a condition where any change by the reduction of interest upon, or depreciation in, the value of its securities, or any increase of mortality, would render it insolvent and subject to be placed in the hands of a receiver. The evident purpose of the provisions of the defendant's charter and policy relating to this subject was to vest in the directors of the corporation a discretion to determine the proportion of its surplus which should be divided each year."

In a friendly suit tried in a circuit court of Wisconsin in 1916, entitled *Bohemian Bldg. and Loan Association vs. Knolt*, the court, in commenting on the nature of these reserves, said:

"The apparent function of this fund is to insure the stockholders against losses. Its purpose is not unlike that of the various forms of insurance now in such common use. * * * This contribution is as legitimate an item of expense as are the premiums paid on any insurance policy." (See *Clarks and Chase, Building and Loan Associations*, footnote, page 344.)

In commenting on the necessity of such funds, *Sundheim* says:

"It is optional with the association whether to maintain such a fund or not, but justice and good business policy seem to require it. The retiring stockholder must be paid the value of his stock in cash and leave for those remaining a large number of securities and perhaps some real estate purchased to protect the association's interest. How much will be realized on these securities, or real estate, no human foresight can tell. Further, the realizing on these securities may entail considerable litigation and expense. There are many other contingencies which might cause a shrinkage in the association's assets, such as defective titles, undisclosed defalcations on the part of an officer, a miscalculation of assets and liabilities, and many other errors and omissions which must always be reckoned with in the conduct of human affairs.

"The contingent fund is merely insurance against possible loss. That losses may occur from time to time seems almost inevitable and it is, therefore, inequitable that the remaining stockholders should be compelled to accept all securities at par, so, to say the least, the maintenance of this fund is justified. The association teaches the duty of providing for the proverbial rainy day. Why should it not provide for the hour of adversity? The reserve fund has protected the maturing or withdrawing member during the period of his membership. In case of loss it has or would have, reimbursed him and, at all times, it has protected him and given strength and standing to the association. Losses may occur, after his membership ceases, that arose from some mistake or mismanagement committed during the period of his membership, and in fairness and equity the remaining members should

have some protection against this." (Sundheim, Law of Building and Loan Associations, sec. 53.)

The Government insists, we think, upon an interpretation of section 188 of the Corporation Law that is altogether too strict and literal. From the fact that the statute provides that profits and losses shall be annually apportioned among the shareholders it is argued that all earnings should be distributed without carrying anything to the reserve. But it will be noted that it is provided in the same section that the profits and losses shall be determined by the board of directors; and this means that they shall exercise the usual discretion of good businessmen in allocating a portion of the annual profits to purposes needful to the welfare of the association. The law contemplates the distribution of earnings and losses after other legitimate obligations have been met.

Our conclusion is that the respondent has the power to maintain the reserves criticized in the eleventh and twelfth counts of the complaint; and at any rate, if it be supposed that the reserves referred to have become excessive, the remedy is in the hands of the Legislature. It is no proper function of the court to arrogate to itself the control of administrative matters which have been confided to the discretion of the board of directors. The causes of action under discussion must be pronounced to be without merit.

Thirteenth cause of action.—The specification under this head is, in effect, that the respondent association has loans which, to the knowledge of the association's officers, were intended to be used by the borrowers for other purposes than the building of homes. In this connection it appears that, though loans have been made by the association exclusively to its shareholders, no attempt has been made by it to control the borrowers with respect to the use made of the borrowed funds, the association being content to see that the security given for the loan in each case is sufficient. On December 31, 1925, the respondent had five hundred forty-four loans outstanding secured by mortgages upon real estate and by the pledge of the borrowers' shares in an amount sufficient at maturity to amortize the loans. With respect to the nature of the real estate upon which these loans were made it appears that three hundred fifty-one loans were secured by mortgages upon city residences, seven by mortgages upon commercial building in cities, and three by mortgages upon unimproved city lots. At the same time one hundred eighty-three of the loans were secured by mortgages upon improved agricultural property consisting of coconut groves, sugar land, and rice land, with a total area of about 7,558 hectares. From information gathered by the association from voluntary statements of borrowers given at the time of application with respect to the use intended to be made of the borrowed funds, it appears that the amount of P693,200 was borrowed to redeem real property from existing mortgages or pactos de retro, P280,800 to buy real estate, P449,100 to erect buildings, P24,000 to improve and repair buildings, P1,480,900 for agricultural purposes, while the amount of P5,763,700 was borrowed for purposes not disclosed.

Upon these facts an elaborate argument has been constructed in behalf of the plaintiff to the effect that in making loans for other purposes than the building of residential houses the association has illegally departed from its charter and made itself amenable to the penalty of dissolution. Aside from being directly opposed to the decision of this court in *Lopez and Javelona vs. El Hogar Filipino and Registrar of Deeds of Occidental Negros* (47 Phil, 249), this contention finds no substantial support in the prevailing decisions made in American courts; and our attention has not been directed to a single case wherein the dissolution of a building and loan association has been decreed in a quo warranto proceeding because the association allowed its borrowers to use the loans for other purposes than the acquisition of homes.

The case principally relied upon for the Government appears to be *Pfeister vs. Wheeling Building Association* (19 W. Va., 676, 716), which involved the question whether a building and loan association could recover the full amount of a note given to it by a member and secured by a mortgage from a stranger. At the time the case arose there was a statute in force in the State of West Virginia expressly forbidding building and loan associations to use or direct their funds for or to any other object or purpose than the buying of lots or houses or in building and

repairing houses, and it was declared that in case the funds should be improperly directed to other objects, the offending association should forfeit all rights and privileges as a corporation. Under the statute so worded the court held that the plaintiff could only recover the amount actually advanced by it with lawful interest and fines, without premium; and judgment was given accordingly. The suggestion in that case that the result would have been the same even in the absence of statute was mere dictum and is not supported by respectable authority.

Reliance is also placed in the plaintiffs brief upon *McCauley vs. Building & Saving Association* (97 Tenn., 421). The statute in force in the State of Tennessee at the time this action arose provided that all loans should be made to the members of the association at open stated meetings and that the money should be lent to the highest bidder. Inconsistently with this provision, there was inserted in the by-laws of the association a provision to the effect that no loan should be made at a greater premium than 30 per cent, nor at a less premium than 29 7/8 per cent. It was held that this by-law made free and open competition impossible and that it in effect established a fixed premium. It was accordingly held, in the case cited, that an association could not recover such part of the loan as had been applied by it to the satisfaction of a premium of 30 per centum.

We have no criticism to make upon the result reached in either of the two decisions cited, but it is apparent that much of the discussion contained in the opinions in those cases does not reflect the doctrine now prevailing in the United States; and much less are those decisions applicable in this jurisdiction. There is no statute here expressly declaring that loans may be made by these associations solely for the purpose of building homes. On the contrary, the building of homes is mentioned in section 171 of the Corporation Law as only one among several ends which building and loan associations are designed to promote. Furthermore, section 181 of the Corporation Law expressly authorizes the board of directors of the association from time to time to fix the premium to be charged.

In the brief of the plaintiff a number of excerpts from textbooks and decisions have been collated in which the idea is developed that the primary design of building and loan associations should be to help poor people to procure homes of their own. This beneficent end is undoubtedly served by these associations, and it is not to be denied that they have been generally fostered with this end in view. But in this jurisdiction at least the lawmaker has taken care not to limit the activities of building and loan associations in an exclusive manner, and the exercise of the broader powers must in the end approve itself to the business community. Judging from the past history of these institutions it can be truly said that they have done more to encourage thrift, economy and saving among the people at large than any other institution of modern times, not excepting even the savings banks. In this connection Mr. Sundheim, in a late treatise upon the subject of the law of building and loan associations, makes the following comment:

"They have grown to such an extent in recent years that they no longer restrict their money to the home buyer, but loan their money to the mere investor or dealer in real estate. They are the holders of large mortgages secured upon farms, factories and other business properties and rows of stores and dwellings. This is not an abuse of their powers or a departure from their main purposes, but only a natural and proper expansion along healthy and legitimate lines." (Sundheim, *Building and Loan Associations*, sec. 7.)

Speaking of the purposes for which loans may be made, the same author adds:

"Loans are made for the purpose of purchasing a homestead, or other real estate, or for any lawful purpose or business, but there is no duty or obligation of the association to inquire for what purpose the loan is obtained, or to require any stipulation from the borrower as to what use he will make of the money, or in any manner to supervise or control its disbursement." (Sundheim, *Building and Loan Associations*, sec. 111.)

In *Lopez and Javelona vs. El Hogar Filipino and Registrar of Deeds of Occidental Negros* (47 Phil., 249), this court had before it the question whether a loan made by the respondent association upon the security of a mortgage upon agricultural land,—where the loan was doubtless used for agricultural purposes,—was usurious or

not; and the case turned upon the point whether, in making sucfi loans, the association had violated the law and departed from its fundamental purposes. The conclusion of the court was that the loan was valid and could be lawfully enforced by a nonjudicial foreclosure in conformity with the terms of the contract between the association and the borrowing member. We now find no reason to depart from the conclusion reached in that case, and it is unnecessary to repeat what was then said. The thirteenth cause of action must therefore be pronounced unfounded.

Fourteenth cause of action.—The specification under this head is that the loans made by the defendant for purposes other than building or acquiring homes have been extended in extremely large amounts and to wealthy persons and large companies. In this connection attention is directed to eight loans made at different times in the last several years to different persons or entities, ranging in amounts from P120,000 to P390,000 and to two large loans made to the Roxas Estate and to the Pacific Warehouse Company in the amounts of P1,122,000 and P2,320,000, respectively. In connection with the larger of the two loans just mentioned it is shown that for about ten months after this loan was made the available funds of El Hogar Filipino were reduced to the point that the association was compelled to take advantage of certain provisions of its by-laws authorizing the postponement of the payment of claims resulting from withdrawals, whereas previously the association had always settled these claims promptly from current funds. At no time was there apparently any delay in the payment of matured shares; but in four or five cases there was as much as ten months delay in the payment of withdrawal applications.

There is little that can be said upon the legal aspects of this cause of action. In so far as it relates to the purposes for which these loans were made, the matter is covered by what was said above with reference to the thirteenth Cause of action; and in so far as it relates to the personality of the borrowers, the question belongs more directly to the discussion under the sixteenth cause of action, which will be found below. The point, then, which remains for consideration here is whether it is a suicidal act on the part of a building and loan association to make loans in large amounts. If the loans which are here the subject of criticism had been made upon inadequate security, especially in case of the largest two, the consequences certainly would have been disastrous to the association in the extreme; but no such fact is alleged; and it is to be assumed that none of the ten borrowers have defaulted in their contracts.

Now, it must be admitted that two of these loans at least are of a very large size, considering the average range of financial transactions in this country; and the making of the largest loan was followed, as we have already seen, with unpleasant consequences to the association in dealing with current claims. Nevertheless the agreed statement of facts shows that all of the loans referred to are only ten out of a total of five hundred forty-four outstanding on December 31, 1925; and the average of all the loans taken together is modest enough. It appears that the chief examiner of banks and corporations of the Philippine Treasury, after his examination of El Hogar Filipino at the end of the year 1925, made a report concerning this association as of January 31, 1926, in which he criticized the Pacific Warehouse Company loan as being so large that it temporarily crippled the lending power of the association for some time. This criticism was apparently justified as proper comment on the activities of the association; but the question for us here to decide is whether the making of this and the other large loans constitutes such a misuser of the franchise as would justify us in depriving the association of its corporate life. This question appears to us to be so simple as almost to answer itself. The law states no limit with respect to the size of the loans to be made by the association. That matter is confided to the discretion of the board of directors; and this court cannot arrogate to itself a control over the discretion of the chosen officials of the company. If it should be thought wise in the future to put a limit upon the amount of loans to be made to a single person or entity, resort should be had to the Legislature; it is not a matter amenable to judicial control. The fourteenth cause of action is therefore obviously without merit.

Fifteenth cause of action.—The criticism here comes back to the supposed misdemeanor of the respondent in maintaining its reserve funds,—a matter already discussed under the eleventh and twelfth causes of action. Under the fifteenth cause of action it is claimed that upon the expiration of the franchise of the association through the effluxion of time, or earlier liquidation of its business, the accumulated reserves and other properties will accrue to the founder, or his heirs, and the then directors of the corporation and to those persons who may at that time to be holders of the ordinary and special shares of the corporation. In this connection we note that article 95 of the by-laws reads as follows:

"ART. 95. The funds obtained by the liquidation of the association shall be applied in the first place to the repayment of shares and the balance, if any, shall be distributed in accordance with the system established for the distribution of annual profits."

It will be noted that the cause of action with which we are now concerned is not directed to any positive misdemeanor supposed to have been committed by the association. It has exclusive relation to what may happen some thirtylive years hence when the franchise expires, supposing of course that the corporation should not be reorganized and continued after that date. There is nothing in article 95 of the by-laws which is, in our opinion, subject to criticism. The real point of criticism is that upon the final liquidation of the corporation years hence there may be in existence, a reserve fund out of all proportion to the requirements that may then fall upon it in the liquidation of the company. It seems to us that this is a matter that may be left to the prevision of the directors or to legislative action if it should be deemed expedient to require the gradual suppression of the reserve funds as the time for dissolution approaches. It is no matter for judicial interference, and much less could the resumption of the franchise on this ground be justified. There is no merit in the fifteenth cause of action.

Sixteenth cause of action.—This part of the complaint assigns as cause of action that various loans now outstanding have been made by the respondent to corporations and partnerships, and that these entities have in some instances subscribed to shares in the respondent for the sole purpose of obtaining such loans. In this connection it appears from the stipulation of facts that of the 5,826 shareholders of El Hogar Filipino, which composed its membership on December 31, 1925, twenty-eight are juridical entities, comprising sixteen corporations and fourteen partnerships; while of the five hundred forty-four loans of the association outstanding on the same date, nine had been made to corporations and five to partnerships. It is also admitted that some of these juridical entities, became shareholders merely for the purpose of qualifying themselves to take loans from the association, and the same is said with respect to many natural persons who have taken shares in the association, Nothing is said in the agreed statement of facts on the point whether the corporations and partnerships that have taken loans from the respondent are qualified by law governing their own organization to enter into these contracts with the respondent.

In section 173 of the Corporation Law it is declared that "any person" may become a stockholder in building and loan associations. The word "person" appears to be here used in its general sense, and there is nothing in the context to indicate that the expression is used in the restricted sense of "natural person." It should therefore be taken to include both natural and artificial persons, as indicated in section 2 of the Administrative Code. We would not say that the word "person," or "persons," is to be taken in this broad sense in every part of the Corporation Law. For instance, it would seem reasonable to say that the incorporators of a corporation ought to be natural persons, although in section 6 it is said that five or more "persons," not exceeding fifteen, may form a private corporation. But the context there, as well as the common sense of the situation, suggests that natural persons are meant. When it is said, however, in section 173, that "any person" may become a stockholder in a building and loan association, no reason is seen why the phrase may not be taken in its proper broad sense of either a natural or artificial person. At any rate the question whether these loans and the attendant subscriptions were properly made involves a consideration of the power of the subscribing corporations and partnerships to own

the stock and take the loans; and it is not alleged in the complaint that they were without power in the premises. Of course the mere motive with which subscriptions are made, whether to qualify the stockholders to take a loan or for some other reason, is of no moment in determining whether the subscribers were competent to make the contracts. The result is that we find nothing in the allegations of the sixteenth cause of action, or in the facts developed in connection therewith, that would justify us in granting the relief.

Seventeenth cause of action.—Vnder the seventeenth cause of action, it is charged that in disposing of real estates purchased by it. in the collection of its loans, the defendant has on various occasions sold some of the said real estate on credit, transferring the title thereto to the purchaser; that the properties sold are then mortgaged to the defendant to secure the payment of the purchase price, said amount being considered as a loan, and carried as such in the books of the defendant, and that several such obligations are still outstanding. It is further charged that the persons and entities to which said properties are sold under the condition charged are not members or shareholders nor are they made members or shareholders of the defendant.

This part of the complaint is based upon a mere technicality of bookkeeping. The central idea involved in the discussion is the provision of the Corporation Law requiring loans to be made to stockholders only and on the security of real estate and shares in the corporation, or of shares alone. It seems to be supposed that, when the respondent sells property acquired at its own foreclosure sales and takes a mortgage to secure the deferred payments, the obligation of the purchaser is a true loan, and hence prohibited. But in requiring the respondent to sell real estate which it acquires in connection with the collection of its loans within five years after receiving title to the same, the law does not prescribe that the property must be sold for cash or that the purchaser shall be a shareholder in the corporation. Such sales can of course be made upon terms and conditions approved by the parties; and when the association takes a mortgage to secure the deferred payments, the obligation of the purchaser cannot be fairly described as arising out of a loan. Nor does the fact that it is carried as a loan on the books of the respondent make it a loan in law. The contention of the Government under this head is untenable.

In conclusion, the respondent is enjoined in the future from administering real property not owned by itself; except as may be permitted to it by contract when a borrowing shareholder defaults in his obligation. In all other respects the complaint is dismissed, without costs. So ordered.

Avanceña, C. J., Johnson, Villamor, and Villa-Real, JJ., concur.

[1] Promulgated March 31, 1926, not reported.

MALCOLM, J., with whom concur OSTRAND and JOHNS, JJ., dissenting:

For the second time in the history of the court—so counsel for plaintiff informs us—we must try a corporation for the violation of a law which carries with it a death warrant—so counsel for defendant intimates. That the corporation at bar is wealthy and powerful should neither prejudice us against it nor cause us to cringe before its might. The court has a duty to perform and should perform it with fairness to the corporation and with justice to the public, whose interests are involved. El Hogar Filipino deserves exactly the same consideration as any other litigant. No more, no less.

The proceeding is one of quo warranto, begun by. the Government of the Philippine Islands under authority of section 190-A of the Corporation Law, and of sections 197-216, 519 of the Code of Civil Procedure. The complaint contains seventeen causes of action. To all of them, the defendant has¹ made answer. The facts have been covered by stipulation. The Government asks for an order of dissolution. Defendant tenaciously resists.

El Hogar Filipino is a corporation organized as a mutual building and loan association under the provisions of the Corporation Law (Act No. 1459). The law last mentioned, it may be recalled, is divided into two parts. Chapter one is entitled "General Provisions as to Corporations." Chapter two is entitled "Special Provisions." In chapter two, in sections 171 to 190, inclusive, are found the special provisions pertaining to building and loan corporations. Section 171 thereof is indicative of the legislative purpose. It provides:

"All corporations whose capital stock is required or is permitted to be paid in by the stockholders in regular, equal, periodical payments and whose purpose is to accumulate the savings of its stockholders, to repay to said stockholders their accumulated savings and profits upon surrender of their stock, to encourage industry, frugality, and. home building among its stockholders, and to loan its funds and funds borrowed for the purpose to stockholders on the security of unencumbered real estate and the pledge of shares of capital stock owned by the stockholders as collateral security, shall be known as building and loan corporation, and the words 'mutual building and loan association' shall form part of the name of every such corporation."

The articles of incorporation of El Hogar Filipino show that the purposes of the corporation are: (1) The accumulation of the savings of its shareholders; (2) the return to said shareholders of their accumulated savings and profits upon the surrender and cancellation of their shares; (3) the encouragement of industry, frugality, and home building among its shareholders; (4) the loan of its funds and funds borrowed for the purpose to its shareholders on the security of unencumbered real estate and the pledge of shares of capital stock of the company owned by its shareholders as collateral security; and (5) the borrowing of money upon the credit of the corporation and the issuance of bonds Or other documents evidencing the existence of such obligations. The capital of the corporation is made not to exceed P10,000,000. At the end of 1925 it had 5,826 shareholders holding 125,750 shares, the total paid up value of which was P8,703,602.25.

El Hogar Filipino having been incorporated under Philippine law as a mutual building and loan association, the primary inquiry should naturally be as to the nature, purposes, and operations of mutual building and loan associations.

In the case of *El Hogar Filipino vs. Rafferty* ([1918], 37 Phil., 995), this court had presented the question of whether El Hogar Filipino, as a building and loan association, was relieved from the necessity of paying an income tax. It was held that it was. Mr. Justice Johnson, speaking for the court, said:

"A building and loan association is an organization created for the purpose of accumulating a fund by the monthly subscription or saving of its members, to assist them in building or purchasing for themselves dwellings or real estate, by loaning to them the requisite money from the funds of the society. To all particular intent it may be said to be to enable a number of associates to have and invest their savings to mutual advantage, so that, from time time, any individual among them may receive, out of the accumulation of the pittances which each contributes periodically, a sum, by way of loan, wherewith to build or pay for a home, and ultimately making it absolutely his own by the payment of such small amounts from time to time. (*Rhodes vs. Missouri Savings & Loan Co.*, 173 Ill, 621; 42 L. R. A., 93.)"

The same opinion quoted from Endlich on Building Associations, section 7, who was termed a leading authority upon such associations, on the subject of the primary designs and general operation of building associations, the following:

"The idea which first gave rise to the institution of building associations, which furnished their ostensible and legitimate *raison d'etre*, and which secured to them their popularity and their, in many respects, exceptionally favored position before the law, is that of enabling persons belonging slowness of the accumulation discourages the effort, to become, by a process of gradual and compulsory savings, either owners of homesteads. The operation of the scheme may be easily understood."

The same opinion quoted from Thornton and Blackledge in their work on Building and Loan Associations, at page 6 the following:

"Societies, known as building, loan fund, and savings association, are now recognized as important factors in the social and economic development of this country. The controlling idea is the massing of the separate earnings of wage-workers, and the savings of persons of small means, in such a manner as to aid them in procuring homes. It is the organization of thrift and self-help; a practical application of the maxim that in 'union there is strength.' The effect of such a movement is to dignify the home; to foster morality, and to make thoughtful, wise, and responsible citizens. It is for such reasons that the law and the courts, where such associations have been properly conducted, have looked upon them with favor. Whether they shall retain the favorable estimation of legislatures and courts will depend in large measure upon the wise forecast and determined purpose of those who control such institutions. Those departures from the original idea, intended to enhance the profits of investors, without in any degree aiding those who are endeavoring to build homes, have been, and in the future probably will be, severely censured by the courts."

In the case of Lopez and Javelona vs. El Hogar Filipino and Registrar of Deeds of Occidental Negros ([1925], 47 Phil., 249), the principal issue had to do with the relation of El Hogar Filipino to the Usury Law permitting it to charge a higher rate of interest than persons or entities, other than similarly organized mutual building and loan associations. Mr. Justice Johns, in a vigorous dissenting opinion, said:

"There must be and is a valid reason for the exception made in the statute which permits building and loan associations to charge and receive 18 per cent per annum as interest, and which limits all other loans made by any other person, firm or corporation to interest at 12 per cent per annum.

"All building and loan associations are founded, and exceptions made in their favor as to the rate of interest, upon the theory that they will enable a person with small means or small income who has a family to support, to build a home in which to live and to improve his property and develop the country. When the exception was made by the Legislature, it was never intended that the El Hogar Filipino or any other corporation, under the guise of a building and loan association, should make a loan upon a sugar plantation of the nature of the one in question.

* * * * *

"It will be noted that the exception made in the statute above quoted is for 'mutual building and loan societies incorporated under the Corporation Act.' The use of the word 'mutual' is significant and important. Under the statute, it is not sufficient that the corporation should be a building and loan association. It must be a mutual building and loan association."

In the same dissent, reference was made to the case of El Hogar Filipino vs. Rafferty, supra, and the remarks of Endlich, and Thornton and Blackledge on the purposes of mutual building and loan associations. Fletcher, Cyclopedia of Corporations, volume 1, page 136, was also quoted from as follows:

"An incorporated building and loan association is a corporation for the purpose of raising, by periodical subscriptions of members, a stock or fund to assist members by advances or loans, generally on mortgage security, in building or purchasing homes. Such corporations are different from corporations formed for pecuniary profit.

"The term (building and loan association) does not generally include corporations unless their purpose is to accumulate funds and lend the same to members to assist them in purchasing or building homes * * *. (Cases cited.) It does not include a corporation * * * for the purpose of purchasing and improving real estate and advancing money on mortgages * * * or a corporation merely for the purpose of loaning money."

In the same dissent, reference was made to what Corpus Juris, volume 9, page 920, contains on the subject of the

object and purpose of building and loan associations, namely:

"As it is sometimes stated in the statutes relating to, and in the charters and constitutions of, building and loan associations, the principal object of a building and loan association is to create a loan fund for the benefit of its borrowing members, the underlying idea being that, by means of the system of small periodical payments provided, people of limited means will be enabled to become the owners of homes, and thrift, economy, and good citizenship will thereby be promoted. By reason of the favorable results attending the operation of these associations, and their beneficent purposes, they have, especially before they attained their present tremendous growth, been favored and granted special privileges by the various legislatures, such as permission to charge high rates of interest and exemption from taxation. * * *" In lieu of asterisk the next succeeding sentence from Corpus Juris could also have been appropriately used: "However, with the growth of these organizations, evils have crept in, the privileges granted have in many instances been abused by unscrupulous officers, and, in recent years, the courts have been compelled to subject their transactions to closer scrutiny."

Speaking of the purposes for which loans can be made by building and loan associations, Rosenthal, in his work on Building, Loan and Savings Associations, third edition, page 108, says:

"In our opinion, the object of building, loan and savings associations is to furnish funds for homes rather than for mercantile or manufacturing improvements. Some of the larger associations have granted loans of this character, and we consider it a dangerous departure from the purposes for which these associations were created."

Thompson on Building Associations, pages 5, 23, 24, 232 and 558, says:

"The building association as now existing is a private corporation designed for the accumulation, by the members, of their money, by periodical payments into its treasury, to be invested from time to time in loans to the members upon real estate for home purposes, * * *. "The building association is a home builder. The member by its system is enabled to acquire a home, and to pay for it he pledges his future savings. * * * It enforces economy, and awakens thoughts of citizenship in its better sense of offering homes. This is the first purpose of these institutions. The language of the Supreme Court of Georgia is timely: 'That they have improved our towns by leading to the erection of a number of new buildings, furnished many families with homes of their own, that could not otherwise have possessed them, given a considerable impulse to mechanical enterprise, and in many other ways promoted the prosperity and welfare of the communities where they exist, is undoubtedly true. But whether they will continue to be entitled to the epithet of the "poor man's exchequer," and whether they will, as they promise to do, enable every man to become his own landlord, will depend entirely upon the manner in which they conduct their business * * *'

"These institutions are well known all over the United States to be depositories of money savings, and investors of those savings in homes for members. The legislature has created them in the interest of good citizenship, to enable the people to save their money and acquire homes and become steady citizens. The ultimate legislative purpose is home-building. If it was merely a depository of savings it would have no strong reason for existence, because the savings banks furnish that; but it goes further, and is designed by law to use those savings in procuring homes for its members. And the courts should promptly curb any disposition to depart from the corporate purposes.

" * * * But a building association is not an ordinary corporation; in fact, it exercises some extraordinary privileges, particularly in not being amenable to the usury laws. It is created for the declared purposes of accumulating money and lending the accumulation to members to build or acquire homes for themselves. The legislature devised this plan of cooperative accumulations for the purpose of assisting each member to become his own landlord. The state has a selfish motive in the promotion of a building association, as through its workings it is planting deeply the roots of citizenship. The drifting, thriftless classes are offered a school of economy, and the earnest and economical classes are given an opportunity. There is, then, the formation of a

steady, energetic and accumulating citizen. The cares of the state are lessened by decreasing poverty, and its prosperity is increased by growing material wealth. We may clearly conceive, then, that the intention of the legislature in the creation of building associations is, first, to encourage savings; second, to secure homes for the savers."

In the case of *Mandlin vs. American Savings and Loan Association* ([1896], 63 Minn., 358), the court said:

"So-called 'building societies,' operated on the plan of the defendant, have so often become the instrument of oppression and extortion as to call down the censure of some eminent courts. The original purpose of building societies, viz., to enable people of small means to build or buy homes, is entirely wanting.

" 'Such a body' says Follet, J., in *Seibel vs. Victoria Building Association* (43 Ohio St., 371, p. 373), 'exists for the equal benefit of all its members, who are presumed to be persons whose earnings are small, and who seek to use weekly savings in procuring suitable homesteads. Every member is presumed to become after sometime a borrower to the extent of his interest. Building associations are not intended to enable money lenders to obtain extraordinary interest, but they are intended to help in securing homes with the aid of small incomes.' (Barry Law of Building Societies, p. 3, sec. 4.)"

In the case of *North American Building Association vs. Sutton* ([1860], 35 Pa., 463), the court said:

"It is well known that the original design of the legislature was to encourage the erection of buildings. The motive for the grant of the franchise was public improvement. But the practical working of the associations formed under the law has not been what was anticipated. Though called 'building societies' they are, in truth, only agencies by which a greater than legal interest is obtained from the necessitous and unwary."

In the case of *Continental National Building and Loan Association vs. Miller* ([1902], 44 Fla., 757), the court said:

"When local in their operations and prudently managed they have served a useful purpose in enabling the man of small means to build his modest homes or to make a safe and profitable investment of his meagre earnings; but when they branch out and forget the original purposes and limitations that have given them this favored position, trouble not infrequently arises."

In the case of *St. Joseph and Kansas Loan and Building Association vs. Thompson* ([1877], 19 Kansas, 321), the court said:

"It was never intended that these corporations, organized as this one was for the purpose of giving to its members through their savings an easy way to discharge incumbrances and to build homes, should loan their funds to others than their own members."

In the case of *Parker vs. Fulton Loan and Building Association* ([1872], 46 Ga., 166), the court said:

"Whether such a contract though legal upon its face, was, in fact, illegal, would depend upon the object of the association. If it were, in truth, a mere device to evade the usury laws, then it would be illegal, if in fact more was taken for the use of money than 7 per cent per annum. But if the organization were in fact and bona fide a plan with the real intent and object of 'accumulating a fund by monthly subscriptions or savings of the members thereof, to assist them in procuring for themselves such real estates as they may deem proper,' then it would not be illegal."

"The practical application of the resources of these institutions (building and loan associations) to the building of homes and aiding their members to change their condition from rent-paying tenants to home-owning citizens has been recognized as a work of vital importance and of the highest helpfulness to the interest of the state and nation." (Rosenthal Cyc. of Building, Loan & Savings Association, p. 73.)

"The aim and purpose of a building association is to aid and encourage its members to learn and practice thrift

by regular systematic saving, and to provide ways and means so that every family may procure home." (Rosenthal Cyc. of Building, Loan & Savings Association, p. 9.)

"The funds of the first associations were applied to aid its members to procure homes. This was in fact the one outstanding feature of the plan and the high purpose for which the association was organized. The wish and desire to own their own home, was, in fact the primary, fundamental inspiration on which the first building association was formed, and has ever continued to be the shining pole star which has guided and directed the progress of these building associations to the present day. The desire to own a home is one of the primary, natural instincts of every real man or woman. An institution organized and operated on a fair and equitable plan which has for its object the gratifying of that desire, is sure to make a strong appeal to all humanity. The constant appeal which building associations have always made to this deep-seated human desire, is the real secret of their great success." (Rosenthal Cyc. of Building, Loan & Savings Association, p. 13.)

"A recent president of the United States League of Local Building and Loan Associations said that 'Our associations are serving just two classes of customers: receiving the savings of thrifty and farseeing people, and loaning these funds to members who wish to buy or build a home. Never was the need for building or owning a home greater than in the past few years, and as you well know, lack of sufficient funds has been one of our problems.'

"Building and Loan Associations started as neighborhood clubs in most parts of the country. Neighbors wished to become home owners and began contributing a certain sum monthly to a treasurer. The aggregate of these monthly payments was soon sufficient to buy or build a home for one of the members. The fund was then loaned to one of them, and as other funds accumulated, others could borrow. The joint purposes of thrift and home ownership are inseparable and are of equal importance. There could be no cooperative building and loan association without both." (Clark and Chase Building and Loan Association, p. 4).

The Commissioner of Internal Revenue of the United States in article 515 of his new regulations, outlines the particular associations entitled to exemption, under the Federal Law as follows:

"In general, a building and loan association entitled to exemption is one organized pursuant to the laws of any state, territory or the District of Columbia, which accumulates funds to be loaned primarily to the shareholders for the purpose of building or acquiring homes. (Rosenthal Cyc. of Building, Loan & Savings Association, p. 94.)"

The authorities could be piled up mountain high. They all disclose that mutual building and loan associations are peculiar and special corporations. They can exercise only such powers as are conferred by the legislative body creating them, either by express terms or by necessary implication. Their basic and essential idea is mutuality. The primary object is to encourage thrift and to assist in home building. "El Hogar Filipino"—or as it is in English "The Filipino Home"—that is the magic thought which attracts small investors. But when pseudo associations branch out and forget the original purposes and limitations that have given them their favored positions, it is incumbent on the judiciary to place them back in their rightful places. We are frank to say that it is these elementary principles, which, in our opinion, the majority have failed to grasp, which have led them into error in the decision of this case.

Why are mutual building and loan associations granted special privileges? Why are mutual building and loan associations exempted from taxation, as disclosed in *El Hogar Filipino vs. Rafferty*, supra? Why are building and loan associations permitted to charge high rates of interest, as disclosed in *Lopez and Javelona vs. El Hogar Filipino*, and *Registrar of Deeds of Occidental Negros*, supra? Why? Need answers be given. If so, it is so that mutual building and loan associations may be made secure in their lawful and beneficent purposes. It is not that mutual building and loan associations may with one hand accept favors rightfully theirs, and with the other hand grasp favors properly belonging to strictly private corporations or loan societies.

El Hogar Filipino has offended against the law of its creation, and has departed from the fundamental purposes of mutual building and loan associations in this:

A. In that it has engaged in business activities entirely foreign to and not reasonably necessary for the purposes for which it was organized, such as the administration of properties and the management of properties not mortgaged;

B. In that it has inserted in article 10 of its by-laws a provision giving the board of directors, by majority vote, the unqualified right to cancel and forfeit shares by merely returning to their owners the amount which may result from the accounting, in violation of the Corporation law;

C. In that its board of directors has become a permanent and self-perpetuating body, since with the exception of the years 1911, 1912, and 1917, there has been no election of directors, and since between 1912 and 1917, and from 1917 until the present, the membership of the board has not been changed, except to fill vacancies which have been filled by the board itself, in violation of the Corporation Law, and of the by-laws of the corporation;

D. In that the directors, instead of serving without pay or for nominal salaries, have been receiving relatively large compensations out of the profits in accordance with article 92 of the by-laws, providing that 5 per cent of the annual profits shall be devoted to the compensation of the directors, according to their attendance at the meetings;

E. In that the corporation has been giving to Antonio Melian, its founder, under, the provisions of article 92 of its by-laws 5 per cent of the yearly net profits, and will continue to do so, for the full fifty-year period of life of the defendant, and under which, Mr. Melian has received a total sum of P615,834;

F. In that articles 70 and 76 of its by-laws are contrary to law, since they only permit the election or appointment to the board of directors of persons owning P5,000 worth of paid up shares, which is made a condition precedent to eligibility to the board of directors;

G. In that it has issued so-called special shares, in violation both of the letter and spirit of the Corporation Law;

H. In that it has maintained out of its profits an unnecessarily large reserve fund, classified into general reserve fund and special reserve-fund, instead of distributing its profits among its members;

I. In that it has made large loans to persons and companies, such as a loan of P2,320,000 to the Pacific Warehouse Company, which so depleted the funds of the corporation that for sometime it was unable to act on applications for small loans and for the retirement of shares;

J. In that under articles 92 and 95 of the by-laws of the corporation, upon the expiration of its period of life or upon earlier liquidation of its business, the accumulated reserves and other properties will be distributed among and will benefit only its directors and its founder, together with a few other persons;

K. In that its membership is in part composed of corporations, companies, and associations, for instance, of sixteen corporations and fourteen partnerships;

L. In that it has disposed of real estate purchased by it in the collection of its loans on credit, thereafter accepting mortgages on the property transferred, in violation of the Corporation Law;

M. And, lastly, in that El Hogar Filipino has failed to carry out and fulfill the main purpose for which it was created, and in consideration of which it has been granted special privileges and exemptions.

The foregoing are not trivial or isolated infractions of the law to be brushed away with a wave of the hand. They constitute grave abuses. They disclose El Hogar Filipino as an octopus whose tentacles have reached out to embrace and stifle vital public interests. The court would be entirely justified in peremptorily decreeing the dissolution of the corporation for misuse of its powers.

Section 190-A of the Corporation Law, inserted by section 3 of Act No. 2792, makes it the imperative duty of the court to dissolve a corporation for any violation which it has committed. It is believed, however, that counsel for the defendant is entirely correct in his argument to the effect that the legislature is without power to diminish the jurisdiction of the court, and to direct a particular judgment in a particular case. Rather would we prefer to follow the precedent in the case of the Government of the Philippine Islands vs. Philippine Sugar Estates Development Company ([1918], 38 Phil., 15), wherein it was ordered that the corporation be dissolved and prohibited from continuing to do business in the Philippine Islands unless it complied with the conditions mentioned in the decision.

In amplification of the above suggestion, it must be said that El Hogar Filipino is the possessor of important property rights which should not be disastrously disturbed. It must also be said that a mutual building and loan association properly conducted is an institution which should be encouraged in the community. The result should, therefore, be to confine El Hogar Filipino to its legitimate purposes and to force it to eliminate its illegitimate purposes. The Government has made out its case, but the defendant should be permitted a reasonable time to fulfill the conditions laid down in this decision.

ROMUALDEZ, J., dissenting:

I believe that the defendant corporation should be compelled to observe the law and to confine itself to its object and purposes as a building and loan association existing under Act No., 1459, and that it should be given a reasonable period within which to do so.

I am of this opinion on the ground that, to my mind, said corporation has deviated from the law and its own object and purposes by adopting articles 10, 70, and 76 of its by-laws in permitting the perpetuation of the same directors, and in making loans to persons who are not stockholders and to wealthy persons or companies in extremely large amounts.

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