

REPUBLIC PLANTERS BANK, PETITIONER, VS. HON. ENRIQUE A. AGANA, SR., AS PRESIDING JUDGE, COURT OF FIRST INSTANCE OF RIZAL, BRANCH XXVIII, PASAY CITY, ROBES-FRANCISCO REALTY & DEV...

G.R. No. 51765. March 03, 1997

Ponente: HERMOSISIMA, JR., J.

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HERMOSISIMA, JR., J.:

This is a petition for certiorari seeking the annulment of the Decision[1] of the then Court of First Instance of Rizal[2] for having been rendered in grave abuse of discretion. Private respondents Robes-Francisco Realty and Development Corporation (hereafter, "the Corporation") and Adalia F. Robes filed in the court a quo, an action for specific performance to compel petitioner to redeem 800 preferred shares of stock with a face value of P8,000.00 and to pay 1% quarterly interest thereon as quarterly dividend owing them under the terms and conditions of the certificates of stock.

The court a quo rendered judgment in favor of private respondents; hence, this instant petition.

Herein parties debate only legal issues, no issues of fact having been raised by them in the court a quo. For ready reference, however, the following narration of pertinent transactions and events is in order:

On September 18, 1961, private respondent Corporation secured a loan from petitioner in the amount of P120,000.00. As part of the proceeds of the loan, preferred shares of stocks were issued to private respondent Corporation, through its officers then, private respondent Adalia F. Robes and one Carlos F. Robes. In other words, instead of giving the legal tender totaling to the full amount of the loan, which is P120,000.00, petitioner lent such amount partially in the form of money and partially in the form of stock certificates numbered 3204 and 3205, each for 400 shares with a par value of P10.00 per share, or for P4,000.00 each, for a total of P8,000.00. Said stock certificates were in the name of private respondent Adalia F. Robes and Carlos F. Robes, who subsequently, however, endorsed his shares in favor of Adalia F. Robes.

Said certificates of stock bear the following terms and conditions:

"The Preferred Stock shall have the following rights, preferences, qualifications and limitations, to wit:

1. Of the right to receive a quarterly dividend of One Per Centum (1%), cumulative and participating.

x x x

2. That such preferred shares may be redeemed, by the system of drawing lots, at any time after two (2) years from the date of issue at the option of the Corporation. x x x."

On January 31, 1979, private respondents proceeded against petitioner and filed a Complaint anchored on private respondents' alleged rights to collect dividends under the preferred shares in question and to have petitioner

redeem the same under the terms and conditions of the stock certificates. Private respondents attached to their complaint, a letter-demand dated January 5, 1979 which, significantly, was not formally offered in evidence.

Petitioner filed a Motion to Dismiss^[3] private respondents' Complaint on the following grounds: (1) that the trial court had no jurisdiction over the subject-matter of the action; (2) that the action was unenforceable under substantive law; and (3) that the action was barred by the statute of limitations and/or laches.

Petitioner's Motion to Dismiss was denied by the trial court in an Order dated March 16, 1979.^[4] Petitioner then filed its Answer on May 2, 1979.^[5] Thereafter, the trial court gave the parties ten (10) days from July 30, 1979 to submit their respective memoranda after the submission of which the case would be deemed submitted for resolution.^[6]

On September 7, 1979, the trial court rendered the herein assailed decision in favor of private respondents. In ordering petitioner to pay private respondents the face value of the stock certificates as redemption price, plus 1% quarterly interest thereon until full payment, the trial court ruled:

"There being no issue of fact raised by either of the parties who filed their respective memoranda delineating their respective contentions, a judgment on the pleadings, conformably with an earlier order of the Court, appears to be in order.

From a further perusal of the pleadings, it appears that the provision of the stock certificates in question to the effect that the plaintiffs shall have the right to receive a quarterly dividend of One Per Centum (1%), cumulative and participating, clearly and unequivocally [sic] indicates that the same are 'interest bearing stocks' which are stocks issued by a corporation under an agreement to pay a certain rate of interest thereon (5 Thompson, Sec. 3439). As such, plaintiffs become entitled to the payment thereof as a matter of right without necessity of a prior declaration of dividend.

On the question of the redemption by the defendant of said preferred shares of stock, the very wordings of the terms and conditions in said stock certificates clearly allows the same.

To allow the herein defendant not to redeem said preferred shares of stock and/or pay the interest due thereon despite the clear import of said provisions by the mere invocation of alleged Central Bank Circulars prohibiting the same is tantamount to an impairment of the obligation of contracts enshrined in no less than the fundamental law itself.

Moreover, the herein defendant is considered in estoppel from taking shelter behind a General Banking Act provision to the effect that it cannot buy its own shares of stocks considering that the very terms and conditions in said stock certificates allowing their redemption are its own handiwork.

As to the claim by the defendant that plaintiffs' cause of action is barred by prescription, suffice it to state that the running of the prescriptive period was considered interrupted by the written extrajudicial demands made by the plaintiffs from the defendant."^[7]

Aggrieved by the decision of the trial court, petitioner elevated the case before us essentially on pure questions of law. Petitioner's statement of the issues that it submits for us to adjudicate upon, is as follows:

"A.

RESPONDENT JUDGE COMMITTED A GRAVE ABUSE OF DISCRETION AMOUNTING TO LACK OR EXCESS OF JURISDICTION IN ORDERING PETITIONER TO PAY RESPONDENT ADALIA F. ROBES THE AMOUNT OF P8,213.69 AS INTERESTS FROM 1961 TO 1979 ON HER PREFERRED SHARES.

B.

RESPONDENT JUDGE COMMITTED A GRAVE ABUSE OF DISCRETION AMOUNTING TO LACK OR EXCESS OF JURISDICTION IN ORDERING PETITIONER TO REDEEM RESPONDENT ADALIA F. ROBES' PREFERRED SHARES FOR P8,000.00

C.

RESPONDENT JUDGE COMMITTED A GRAVE ABUSE OF DISCRETION AMOUNTING TO LACK OR EXCESS OF JURISDICTION IN DISREGARDING THE ORDER OF THE CENTRAL BANK TO PETITIONER TO DESIST FROM REDEEMING ITS PREFERRED SHARES AND FROM PAYING DIVIDENDS THEREON x x x.

D. THE TRIAL COURT ERRED IN NOT HOLDING THAT THE COMPLAINT DOES NOT STATE A CAUSE OF ACTION.

E.

THE TRIAL COURT ERRED IN NOT HOLDING THAT THE CLAIM OF RESPONDENT ADALIA F. ROBES IS BARRED BY PRESCRIPTION OR LACHES."[8]

The petition is meritorious.

Before passing upon the merits of this petition, it may be pertinent to provide an overview on the nature of preferred shares and the redemption thereof, considering that these issues lie at the heart of the dispute.

A preferred share of stock, on one hand, is one which entitles the holder thereof to certain preferences over the holders of common stock. The preferences are designed to induce persons to subscribe for shares of a corporation.[9] Preferred shares take a multiplicity of forms. The most common forms may be classified into two: (1) preferred shares as to assets; and (2) preferred shares as to dividends. The former is a share which gives the holder thereof preference in the distribution of the assets of the corporation in case of liquidation;[10] the latter is a share the holder of which is entitled to receive dividends on said share to the extent agreed upon before any dividends at all are paid to the holders of common stock.[11] There is no guaranty, however, that the share will receive any dividends. Under the old Corporation Law in force at the time the contract between the petitioner and the private respondents was entered into, it was provided that "no corporation shall make or declare any dividend except from the surplus profits arising from its business, or distribute its capital stock or property other than actual profits among its members or stockholders until after the payment of its debts and the termination of its existence by limitation or lawful dissolution." [12] Similarly, the present Corporation Code[13] provides that the board of directors of a stock corporation may declare dividends only out of unrestricted retained earnings.[14] The Code, in Section 43, adopting the change made in accounting terminology, substituted the phrase unrestricted retained earnings," which may be a more precise term, in place of "surplus profits arising from its business" in the former law. Thus, the declaration of dividends is dependent upon the availability of surplus profit or unrestricted retained earnings, as the case may be. Preferences granted to preferred stockholders, moreover, do not give them a lien upon the property of the corporation nor make them creditors of the corporation, the right of the former being always subordinate to the latter. Dividends are thus payable only when there are profits earned by the corporation and as a general rule, even if there are existing profits, the board of directors has the discretion to determine whether or not dividends are to be declared.[15] Shareholders, both common and preferred, are considered risk takers who invest capital in the business and who can look only to what is left after corporate debts and liabilities are fully paid.[16]

Redeemable shares, on the other hand, are shares usually preferred, which by their terms are redeemable at a fixed date, or at the option of either issuing corporation, or the stockholder, or both at a certain redemption price.[17] A redemption by the corporation of its stock is, in a sense, a repurchase of it for cancellation.[18] The present Code

allows redemption of shares even if there are no unrestricted retained earnings on the books of the corporation. This is a new provision which in effect qualifies the general rule that the corporation cannot purchase its own shares except out of current retained earnings.[19] However, while redeemable shares may be redeemed regardless of the existence of unrestricted retained earnings, this is subject to the condition that the corporation has, after such redemption, assets in its books to cover debts and liabilities inclusive of capital stock. Redemption, therefore, may not be made where the corporation is insolvent or if such redemption will cause insolvency or inability of the corporation to meet its debts as they mature.[20]

We come now to the merits of the case. The petitioner argues that it cannot be compelled to redeem the preferred shares issued to the private respondent. We agree. Respondent judge, in ruling that petitioner must redeem the shares in question, stated that:

"On the question of the redemption by the defendant of said preferred shares of stock, the very wordings of the terms and conditions in said stock certificates clearly allows the same." [21]

What respondent Judge failed to recognize was that while the stock certificate does allow redemption, the option to do so was clearly vested in the petitioner bank. The redemption therefore is clearly the type known as "optional". Thus, except as otherwise provided in the stock certificate, the redemption rests entirely with the corporation and the stockholder is without right to either compel or refuse the redemption of its stock.[22] Furthermore, the terms and conditions set forth therein use the word "may". It is a settled doctrine in statutory construction that the word "may" denotes discretion, and cannot be construed as having a mandatory effect. We fail to see how respondent judge can ignore what, in his words, are the "very wordings of the terms and conditions in said stock certificates" and construe what is clearly a mere option to be his legal basis for compelling the petitioner to redeem the shares in question.

The redemption of said shares cannot be allowed. As pointed out by the petitioner, the Central Bank made a finding that said petitioner has been suffering from chronic reserve deficiency,[23] and that such finding resulted in a directive, issued on January 31, 1973 by then Gov. G. S. Licaros of the Central Bank, to the President and Acting Chairman of the Board of the petitioner bank prohibiting the latter from redeeming any preferred share, on the ground that said redemption would reduce the assets of the Bank to the prejudice of its depositors and creditors.[24] Redemption of preferred shares was prohibited for a just and valid reason. The directive issued by the Central Bank Governor was obviously meant to preserve the status quo, and to prevent the financial ruin of a banking institution that would have resulted in adverse repercussions, not only to its depositors and creditors, but also to the banking industry as a whole. The directive, in limiting the exercise of a right granted by law to a corporate entity, may thus be considered as an exercise of police power. The respondent judge insists that the directive constitutes an impairment of the obligation of contracts. It has, however, been settled that the Constitutional guaranty of non-impairment of obligations of contract is limited by the exercise of the police power of the state, the reason being that public welfare is superior to private rights.[25]

The respondent judge also stated that since the stock certificate granted the private respondents the right to receive a quarterly dividend of one Per Centum (1%), cumulative and participating, it "clearly and unequivocally (sic) indicates that the same are 'interest bearing stocks' or stocks issued by a corporation under an agreement to pay a certain rate of interest thereon. As such, plaintiffs (private respondents herein) become entitled to the payment thereof as a matter of right without necessity of a prior declaration of dividend." [26] There is no legal basis for this observation. Both Sec. 16 of the Corporation Law and Sec. 43 of the present Corporation Code prohibit the issuance of any stock dividend without the approval of stockholders, representing not less than two-thirds (2/3) of the outstanding capital stock at a regular or special meeting duly called for the purpose. These provisions underscore the fact that payment of dividends to a stockholder is not a matter of right but a matter of consensus.

Furthermore, "interest bearing stocks", on which the corporation agrees absolutely to pay interest before dividends are paid to common stockholders, is legal only when construed as requiring payment of interest as dividends from net earnings or surplus only.[27] Clearly, the respondent judge, in compelling the petitioner to redeem the shares in question and to pay the corresponding dividends, committed grave abuse of discretion amounting to lack or excess of jurisdiction in ignoring both the terms and conditions specified in the stock certificate, as well as the clear mandate of the law.

Anent the issue of prescription, this Court so holds that the claim of private respondent is already barred by prescription as well as laches. Art. 1144 of the New Civil Code provides that a right of action that is founded upon a written contract prescribes in ten (10) years. The letter-demand made by the private respondents to the petitioner was made only on January 5, 1979, or almost eighteen years after receipt of the written contract in the form of the stock certificate. As noted earlier, this letter-demand, significantly, was not formally offered in evidence, nor were any other evidence of demand presented. Therefore, we conclude that the only time the private respondents saw it fit to assert their rights, if any, to the preferred shares of stock, was after the lapse of almost eighteen years. The same clearly indicates that the right of the private respondents to any relief under the law has already prescribed. Moreover, the claim of the private respondents is also barred by laches. Laches has been defined as the failure or neglect, for an unreasonable length of time, to do that which by exercising due diligence could or should have been done earlier; it is negligence or omission to assert a right within a reasonable time, warranting a presumption that the party entitled to assert it either has abandoned it or declined to assert it.[28]

Considering that the terms and conditions set forth in the stock certificate clearly indicate that redemption of the preferred shares may be made at any time after the lapse of two years from the date of issue, private respondents should have taken it upon themselves, after the lapse of the said period, to inquire from the petitioner the reason why the said shares have not been redeemed. As it is, not only two years had lapsed, as agreed upon, but an additional sixteen years passed before the private respondents saw it fit to demand their right. The petitioner, at the time it issued said preferred shares to the private respondents in 1961, could not have known that it would be suffering from chronic reserve deficiency twelve years later. Had the private respondents been vigilant in asserting their rights, the redemption could have been effected at a time when the petitioner bank was not suffering from any financial crisis.

WHEREFORE, the instant petition, being impressed with merit, is hereby GRANTED. The challenged decision of respondent judge is set aside and the complaint against the petitioner is dismissed.

Costs against the private respondents.

SO ORDERED.

Padilla, (Chairman), Bellosillo, Vitug, and Kapunan, JJ., concur.

[1] Promulgated on September 7, 1979 in Civil Case No. 6965-P, penned by District Judge Enrique A. Agana, Sr.; Rollo, pp. 57-59.

[2] Branch XXVIII, Seventh Judicial District, Pasay City.

[3] Dated February 12, 1979.

[4] Rollo, p. 37.

[5] Rollo, pp. 38-40.

[6] Order dated July 30, 1979; Rollo, p. 43.

- [7] Decision dated September 7, 1979, pp. 2-3; Rollo, pp. 58-59.
- [8] Petition, pp. 10-11; Rollo, pp. 11-12
- [9] DE LEON, The Corporation Code of the Philippines, p. 62 (1989 ed.).
- [10] Id.
- [11] DE LEON, p. 69, citing 2 Fletcher, p. 44
- [12] Act No. 1459, Sec. 16, as amended.
- [13] Effective May 1, 1980.
- [14] The Corporation Code, Sec. 16.
- [15] CAMPOS, THE CORPORATION CODE, p. 9 [1990 ed.].
- [16] DE LEON, p. 69, citing SEC Opinion, February 10, 1969.
- [17] Id., at p. 75.
- [18] Id., at p. 77.
- [19] CAMPOS, p. 33.
- [20] DE LEON, p. 76, citing SEC Opinion of January 23, 1985.
- [21] Decision dated September 7, 1979 in Civil Case No. 6965-P penned by Judge Enrique A. Agana, Sr., pp. 2-3; Rollo, pp. 58-59.
- [22] DE LEON, pp. 76-77, citing Section 8 of the Corporation Code.
- [23] Rollo, p. 12.
- [24] Rollo, p. 8.
- [25] Philippine National Bank v. Remigio, G.R. No. 78508, March 21, 1994.
- [26] Rollo, p. 58.
- [27] DE LEON, p. 62, citing Sec. 43 of the Corporation Code.
- [28] Olizon v. Court of Appeals, et al., G.R. 107075, September 1, 1994

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