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MERCANTILE LAW

I. Letters of Credit

Letter of Credit which is used in non-sale transaction, where it serves to reduce the risk of nonperformance is called—

- a. Irrevocable letter of credit;
- b. Standby letter of credit;
- c. Confirmed letter of credit:
- d. None of the above.

Answer:

b. Standby letter of credit. (BAR 2012)

A. Definition and Nature of Letter of Credit

Is the Uniform Customs and Practice for Documentary Credits of the International Chamber of Commerce applicable to commercial letters of credit issued by a domestic bank even if not expressly mentioned in such letters of credit? What is the basis for your answer? (2015)

Answer:

Yes, the Supreme Court held that the observance of the Uniform Customs and Practice in the Philippines is justified by Article 2 of the Code of Commerce which enunciates that in the absence of any particular provision in the Code of Commerce, commercial transaction shall be governed by usage and customs generally observed (Bank of the Philippine Islands v. De Reny Fabric Industries, Inc. 35 SCRA 253).

ABC Company filed a Petition for Rehabilitation with the Court. An Order was issued by the Court, (1) staying enforcement of all claims, whether money or otherwise against ABC Company, its guarantors and sureties not solidarily liable with the company; and (2) prohibiting ABC Company from making payments of its liabilities, outstanding as of the date of the filing of the petition. XYC Company is a holder of an irrevocable Standby Letter of Credit which was previously procured by ABC Company in favor of XYZ Company to secure performance of certain obligations. In the light of the Order issued by the Court,

- a. Can XYZ Company still be able to draw on their irrevocable Standby Letter of Credit when due? Explain your answer.
- b. Explain the nature of Letters of Credit as a financial devise.

Answer:

a. Yes, as an exception to a Stay or Suspension Order included in a Commencement Order issued pursuant to Section 16(q) of the FRIA, Section 18(c) of the said law provides that a Stay or Suspension Order shall not apply "to the enforcement of claims against sureties and other persons solidarily liable with the debtor, and third party or accommodation mortgagors as well as issuers of letters of credit x x x" Similarly, assuming that it has not been superseded by the FRIA, Section 7(b) of the Supreme Court Rules of Procedure on Corporate Rehabilitation (2008) provides that a stay order shall not cover claims against letters of credit and similar security arrangements issued by a third party to secure the payment of the debtor's obligations. This was the basis of the decision in the case of *Metropolitan Waterworks and Sewerage System v. Hon. Reynaldo B. Daway, et al.*, G.R. No. 160732, June 21, 2004.

NB We also have to add as stated in the same MWSS case the stay order only covers the principal debtor, its guarantors and sureties not liable solidarily with the principal debtor. The liability of the issuing bank is neither of the following. Instead, its liability is direct, primary and solidary

b. A letter of credit is a financial device developed by merchants as a convenient and relatively safe mode of dealing with sale of goods to satisfy the seemingly irreconcilable interest of the seller, who refuses to part with his goods before he is paid, and a buyer, who wants to have control of the goods before paying. To break the impasse, the buyer may be required to contract a bank to issue a letter of credit in favor of the seller so that, by virtue of the letter of credit, the issuing bank can authorize the seller to draw drafts and engage to pay them upon their presentment simultaneously with the tender of documents required by the letter of credit. The buyer and the seller agree on what documents are to be presented for the payment, but ordinarily they are documents of title evidencing or attesting to the shipment of the goods to the buyer. Once the credit is established, the seller ships the goods to the buyer and in the process secures the required shipping documents or documents of title. To get paid, the seller executes a draft and presents it together with the required documents to the issuing bank. The issuing bank redeems the draft and pays cash to the seller if it finds that the documents submitted by the seller conform with what the letter of credit requires. The bank then obtains possession of the documents upon paying the seller. The transaction is completed when the buyer reimburses the issuing bank and acquires the documents entitling him to the goods, while the buyer acquired the said documents and control over the goods only after reimbursing the bank.

However, letters of credit are also used in non-sale settings where they serve to reduce the risk of nonperformance. Generally, letters of credit in non-sale settings have come to be known as standby letters of credit. (BAR 2012)

Letters of Credit are financial devices in commercial transactions which will ensure that the seller of the goods is sure to be paid when he parts with the goods and the buyers of the goods get control of the goods upon payment. Which statement is most accurate?

- a. The use of the Letter of Credit serves to reduce the risk of non-payment of the purchase price in a sale transaction;
- b. The Letters of Credit can only be used exclusively in sales transaction;

- c. The Letters of Credit are issued for the benefit of the seller only;
- d. A, b, and c are all correct.

a) The use of the Letter of Credit serves to reduce the risk of non-payment of the purchase price in a sale transaction. (BAR 2012)

B. Parties to a Letter of Credit

1. Rights and Obligations of Parties

C. Basic Principles of Letter of Credit

1. Doctrine of Independence

PJ Corporation (PJ) obtained a loan from ABC Bank (ABC) in the amount of P10 million for the purchase of 100 pieces of ecodoors. Thereafter, a Letter of Credit was obtained by PJ against such loan. The beneficiary of the Letter of Credit is Scrap Metal Corp. (Scrap Metal) in Beijing, China. Upon arrival of 100 pieces of ecodoors, PJ executed a Trust Receipt in favor of ABC to cover for the value of the ecodoors for its release to PJ. The terms of the Trust Receipt is that any proceeds from the sale of the ecodoors will be delivered to ABC as payment. After the ecodoors were sold, PJ, instead of paying ABC, used the proceeds of the sale to order from Scrap Metal another 100 pieces of ecodoors but using another bank to issue a new Letter of Credit fully covered by such proceeds. PJ refused to pay the proceeds of the sale of the first set of ecodoors to ABC, claiming that the ecodoors that were delivered were defective. It then instructed ABC not to negotiate the Letter of Credit that was issued in favor of Scrap Metal.

- [a] Explain what is a "Letter of Credit" as a financial device and a "Trust Receipt" as a security to the Letter of Credit.
- [b] As counsel of ABC, you are asked for advice on whether or not to grant the instruction of PJ. What will be your advice? (2016 Bar)

SUGGESTED ANSWER

(A) A letter of credit is It is any arrangement, however named or described, whereby the issuing bank acting at the request and on the instructions of a customer (applicant) or on its own behalf, binds itself to: (a) pay to the order of, or accept and pay drafts drawn by a third party (Beneficiary); (b) authorize another bank to pay or to accept and pay such drafts; or (3) authorize another bank to negotiate, against stipulated documents, provided, the terms and conditions of the credit are complied with (Art. 2, Uniform Customs & Practice for Documentary Credits).

Whereas, a Trust receipt is a commercial document whereby the bank releases the goods in the possession of the entrustee but retains ownership thereof while the

entrustee shall sell the goods and apply the proceeds for the full payment of his liability with the bank. It is a security arragement to which a bank acquires ownership of the imported personal property (Garcia vs. CA G.R. No. 119845, July 5, 1996).

ALTERNATIVE ANSWER:

(A) A letter of credit is an instrument issued by a bank that guarantees its client's ability to pay for imported goods or services, by authorizing a person to draw drafts on the bank or its correspondents for the bank's account, under conditions specified in the L/C. (Prudential Bank V. IAC, 216 SCRA 257)

Whereas, a trust receipt is a document which expresses a security transaction where the lender, having no prior title to the goods on which the lien is to be constituted, and not having possession over the same since possession thereof remains in the borrower, lends him money to the borrower on security of the goods which borrower is privileged to sell, clear of the lien, and with an agreement to pay all or part of the sale proceeds to the lender (Metropolitan Bank vs. Go, G.R. No. 155647, November 23, 2007).

(B) No, I will not grant the instruction of PJ. Under the indepence principle, the obligation of the bank to pay the Scrap Metal Corporation is not dependent upon the fulfilment or non-fulfillment of the main contract underlying the letter of credit but conditioned only on its submission of the stipulated documents to ABC Bank.

A standby letter of credit was issued by ABC Bank to secure the obligation of X Company to Y Company. Under the standby letter of credit, if there is failure on the part of X Company to perform its obligation, then Y Company will submit to ABC Bank a certificate of default (in the form prescribed under the standby letter of credit) and ABC Bank will have to pay Y Company the defaulted amount. Subsequently, Y Company submitted to ABC Bank a certificate of default notwithstanding the fact that X Company was not in default. Can ABC Bank refuse to honor the certificate of default? Explain. (2015)

Answer:

No. Under the doctrine of independence in a letter of credit, the obligation of the issuing bank to pay the beneficiary is distinct and independent from the main and originating contract underlying the letter of credit. Such obligation to pay does not depend on the fulfillment or non-fulfillment of the originating contract. It arises upon tender of the stipulated documents under the letter of credit. In the present case, the tender of the certificate of default entitles Y to payment under the standby letter of credit notwithstanding the fact that X Company was not in default. This is without prejudice to the right of X Company to proceed against Y Company under the law on contracts and damages (Insular Bank of Asia and America v. IAC, 167 SCRA 450).

ALTERNATIVE ANSWER:

Under the fraud exception principle, the beneficiary may be enjoined from collecting on the letter of credit in case of fraudulent abuse of credit. The issuance of a certificate of default despite the fact that X Company is not in default constitutes fraudulent abuse of credit (*Transfield Philippines v. Luzon Hydro Corporation, 443 SCRA 307*).

AAA Carmakers opened an irrevocable Letter of Credit with BBB Banking Corporation with CCC Cars Corporation as beneficiary. The irrevocable Letter of Credit was opened to pay for the importation of 10 units of Mercedes Benz S class. Upon arrival of the cars, AAA Carmakers found out that the cars were all not in running condition and some parts were missing. As a consequence, AAA Carmakers instructed BBB Banking Corporation not to allow drawdown on the Letter of Credit. Is this legally possible?

- a. No, because under the "Independence Principle" conditions for the drawdown on the Letters of Credit are based only on documents, like shipping documents, and not with the condition of the goods subject of the importation.
- b. Yes, because the acceptance by the importer of the goods subject of importation is material for the drawdown of the Letter of Credit.
- c. Yes, because under the "Independence Principle", the seller of or the beneficiary is always assured of prompt payment if there is no breach in the contract between the seller and the buyer.
- d. No, because what was opened was an irrevocable letter of credit and not a confirmed letter of credit.

Answer:

a) No, because under the "Independence Principle" conditions for the drawdown on the Letters of Credit are based only on documents, like shipping documents, and not with the condition of the goods subject of the importation. (BAR 2012)

Muebles Classico, Inc. (MC), a Manila-based furniture shop, purchased hardwood lumber from Surigao Timber, Inc. (STI), a Mindanao-based logging company. MC was to pay STI the amount of P5 M for 50 tons of lumber. To pay STI, MC opened a letter of credit with Banco de Plata (BDP). BDP duly informed STI of the opening of a letter of credit in its favor.

In the meantime, MC—which had been undergoing financial reverses—filed a petition for corporate rehabilitation. The rehabilitation court issued a Stay Order to stay the enforcement of all claims against MC.

After shipping the lumber, STI went to DBP, presented the shipping documents, and demanded payment of the letter of credit opened in its favor. MC, on the other hand, informed the bank of the Stay Order and instructed it to deny payment to STI because of the Stay Order.

BDP com	es to you for	advice. Your	r best advice is to	
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- a. Grant STI's claim. Under the "Independence Principle," the bank deals only with the document and not the underlying circumstances; hence, the presentation of the letter of credit is sufficient;
- Deny STI's claim. The Stay Order covers all claims against the debtor and binds all its creditors. The letter of credit is a claim against the debtor that is covered by the Stay Order;
- c. Grant STI's claim. The letter of credit is not a claim against the debtor under rehabilitation, but against the bank which has assumed a solidary obligation;
- d. Deny STI's claim. If the bank disregards the Stay order, it may be subject to contempt by the rehabilitation court. STI should file its claim with the rehabilitation court;
- e. File an action for interpleader to resolve the parties' competing claims.

c) Grant STI's claim. The letter of credit is not a claim against the debtor under rehabilitation, but against the bank which has assumed a solidary obligation. (BAR 2013)

2. Fraud Exception Principle

The Supreme Court has held that fraud is an exception to the "independence principle" governing letters of credit. Explain this principle and give an example of how fraud can be an exception.

Answer:

The "independence principle" posits that the obligations of the parties to a letter of credit are independent of the obligations of the parties to the underlying transaction. Thus, the beneficiary of the letter of credit, which is able to comply with the documentary requirements under the letter of credit, must be paid by the issuing or confirming bank, notwithstanding the existence of a dispute between the parties to the underlying transaction, say a contract of sale of goods where the buyer is not satisfied with the quality of the goods delivered by the seller. The Supreme Court in

Transfield Philippines, Inc. v. Luzon Hydro Corporation, 443 SCRA 307 (2004) for the first time declared that fraud is an exception to the independence principle. For instance, if the beneficiary fraudulently presents to the issuing or confirming bank documents that contain material facts that, to his knowledge, are untrue, then payment under the letter of credit may be prevented through court injunction. (BAR 2010)

3. Doctrine of Strict Compliance

At the instance of CCC Corporation, AAA Bank issued an irrevocable Letter of Credit in favor of BBB Corporation. The terms of the irrevocable Letter of Credit state that the beneficiary must present certain documents including a copy of the Bill of Lading of the importation for the bank to release the funds. BBB

Corporation could not find the original copy of the Bill of Lading so it instead presented to the bank a Xerox copy of the Bill of lading. Would you advise the bank to allow the drawndown on the Letter of Credit?

- a. No, because the rule of strict compliance in commercial transactions involving letters of credit, requiring documents set as conditions for the release of the fund has to be strictly complied with or else funds will not be released;
- b. Yes, because an irrevocable letter of credit means that the issuing bank undertakes to release the fund anytime when claimed by the beneficiary, regardless of the kind of document presented;
- c. Yes, because the issuing bank can always justify to CCC Corporation that Xerox copies are considered as faithful reproduction of the original copies;
- d. Yes, because the issuing bank has no discretion to determine whether the documents presented by the beneficiary are sufficient or not.

Answer:

a. No, because the rule of strict compliance in commercial transactions involving letters of credit, requiring documents set as conditions for the release of the fund has to be strictly complied with or else funds will not be released. (BAR 2012)

II. Trust Receipts Law

a. Definition/Concept of a Trust Receipt Transaction

Delano Cruz is in default in the payment of his existing loan from BDP Bank. To extend and restructure this loan, Delano agreed to execute a trust receipt in the bank's favor covering the iron pellets Delano imported from China one year earlier. Delano subsequently succeeded in selling the iron pellets to a smelting plant, but the proceeds went to the payment of the separation benefits of his employees who were laid off as he reduced his operations.

When the extended loan period expired without any significant payment from Delano (not even to the extent of the proceeds of the sale of the iron pellets), BDP Bank consulted you to on how to proceed against Delano. The bank is contemplating the filing of estafa pursuant to the provisions of PD 115 (Trust Receipts Law) to force Delano to turn in at least the proceeds of the sale of the iron pellets.

Would you, as bank counsel and as officer of the court, advise the bank to proceed with its contemplated action?

Answer:

I will not advise BDP Bank to file a criminal case for estafa against Delano. Delano received the iron pellets he imported one year before the trust receipt was executed. As

held by the Supreme Court, where the execution of a trust receipt agreement was made after the goods covered by it had been purchased by and delivered to the entrustee and the latter as a consequence acquired ownership to the goods, the transaction does not involve a trust receipt but a simple loan even though the parties denominated the transaction as one of trust receipt. (BAR 2013)

1. Loan/Security Feature

2. Ownership of the Goods, Documents and Instruments under a Trust Receipt

A. Maine Den, Inc. opened an irrevocable letter of credit with Fair / Bank, in connection with Maine Den, Inc.'s importation of spare parts for its textile mills. The imported parts were released to Maine Den, Inc. after it executed a trust receipt in favor of Fair Bank. When Maine Den, Inc. was unable to pay its obligation under the trust receipt, Fair Bank sued Maine Den, Inc. for estafa under the Trust Receipts Law. The court, how dismissed the suit. Was the dismissal justified? Why or why not? (2015)

Answer:

The dismissal of the complaint for estafa is justified. Under recent jurisprudence, the Supreme Court held that transactions referred to in relation to trust receipts mainly involved sales and if the entruster knew even before the execution of the alleged trust receipt agreement that the goods subject of the trust receipt were never intended by the entrustee for resale or for the manufacture of items to be sold, the agreement is not a trust receipt transaction but a simple loan, notwithstanding the label. In this case, the object of the trust receipt, spare parts for textile mills, was for the use of the entrustee and never intended for sale. As such, the transaction is a simple loan (Ng v. People, GR No. 173905, April 23, 2010; Land Bank v. Perez, GR No. 166884, June 13, 2012 and Hur Ting Yang v. People, GR No. 195117, Aug. 14, 2013).

Will the principle of res perit domino apply in trust receipt transaction?

Answer:

No. This is because the loss of the goods, documents or instruments which are the subject of a trust receipt pending their disposition, irrespective of whether or not it was due to the fault or negligence of the entrustee, shall not extinguish the entrustee's obligation to the entruster for the value thereof. Also, while the entruster is made to appear as owner of the goods covered by the trust receipt, such ownership is only a legal fiction to enhance the entruster's security interest over the goods. (Section 10 of PD 115; Rosario Textile Mills Corp v. Home Bankers Savings and Trust Company, 462 SCRA 88)

B. Rights of the Entruster

a. Validity of the Security Interest as Against the Creditors of the Entrustee/Innocent Purchasers for Value

Upon execution of a trust receipt over goods, the party who is obliged to release such goods and who retains security interest on those goods, is called the

- a. Holder.
- b. Shipper.
- c. Entrustee.
- d. Entrustor.

Answer:

d. Entrustor. (BAR 2011)

Which phrase best completes the statement—In accordance with the Trust Receipt Law, purchasers of the goods from the Entrustee will:

- a. Get the goods only as a collateral;
- b. Not get good title to the goods;
- c. Only get security interest over the goods;
- d. Get good title to the goods.

Answer:

d. Get good title to the goods. (BAR 2012)

C. Obligation and Liability of the Entrustee

Who is the Entrustee in a Trust Receipt arrangement?

- a. The owner of the goods;
- b. The one who holds the goods and receives the proceeds from the sale of the goods;
- c. The person to whom goods are delivered for sale and who bears the risk of the loss;
- d. The party who acquires security interest in the goods.

Answer:

c. The person to whom goods are delivered for sale and who bears the risk of the loss. (BAR 2012)

1. Payment/Delivery of Proceeds of Sale or Disposition of Goods, Documents or Instruments

CCC Car, Inc. obtained a loan from BBB Bank, which fund was used to import 10 units of Mercedes Benz S Class vehicles. Upon arrival of the vehicles and before the release of said vehicles to CCC Car, Inc, X and Y, the president and treasurer, respectively, of CCC signed the Trust Receipt to cover the value of the 10 units of Mercedes Benz S class vehicles, after which, the vehicles were all delivered to the

car display room of CCC. Sales of the vehicles were slow, and it took a month to dispose the 10 units. CCC wanted to be in business and to save on various documentations requires by the bank, decided that instead of turning over the proceeds of the sales, CCC used the proceeds to buy another 10 units of BMW 3 series.

Is the action of CCC legally justified?

Answer:

No. It is the obligation of CCC, as entrustee, to receive the proceed of the sale of the Mercedes Benz S class vehicles in trust for BBB Bank, as entruster, and turn over the same to BBB Bank to the extent of the amount owing to the latter or as appears in the trust receipt. (BAR 2012)

- 2. Return of Goods, Documents or Instruments in Case of Sale
- 3. Liability for Loss of Goods, Documents or Instruments

Morgan, a lawyer, received a lot of diving and other water sports • equipment as payment of his professional fees by Dennis, his client in a child 'custody case. Dennis owned a diving and water sports dealership in Anilao, Batangas. Morgan decided to name Dennis as entrustee because he did not have any experience in selling such specialized sports equipment. They executed a trust receipt agreement, with Morgan as entruster and Dennis as en:trustee. Before the sports equipment could be sold, a strong typhoon hit Batangas. Anilao and other parts of Bahamas experienced power outage. Tak- - ing advantage of the total darkness, unidentified thieves destroyed the padlocks of the establishment of Dennis, and carted off the equipment inside. Morgan demanded that Dennis pay the value of the stolen equipment, but the latter refused on the ground that he also had suffered from the effects of the typhoon, and insisted that the cause of the loss was fortuitous event or force majewre.

Is the justification of Dennis warranted? Explain your answer. (4%) (2017 BAR)

SUGGESTED ANSWER

The justification of Dennis is not warranted. Under the trust receipt law, the loss of goods which are the subject of a trust receipt, pending their disposition, irrespective of whether or not it was due to the fault or negligence of the entrustee, shall not extinguish the obligation of the entrustee for the value thereof (Pres. Dec. 115, Sec. 10, January 29, 1973).

ALTERNATIVE ANSWER

The transaction is not really a trust receipt within the ambit of PD 115 since there is no loan component in the transaction. In a trust receipt, the entruster granted the loan to finance the acquisition of the goods, which goods are held in trust for the benefit of the

entruster pending their disposition. Not being a trust receipt (where force majeure would not have been a defense), the supposed entrustee 'snot liable for the loss of the sports equipment following general principle that force majeure exempts the obligor from liability.

Anton imported perfumes from Taiwan and these were released to him by the bank under a trust receipt. While the perfumes were in Anton's warehouse, thieves broke in and stole all of them.

Who will shoulder the loss of the stolen perfumes?

- a. The loss of the perfumes will be borne by the bank in whose behalf the perfumes were held in trust;
- b. Anton will bear the loss;
- c. The exporter can hold both the bank and Anton liable for the loss;
- d. The exporter from whom Anton bought the perfumes will bear the loss;
- e. No one bears the loss for an unforeseen event.

Answer:

b. Anton will bear the loss. (BAR 2013)

4. Penal Sanction

TRUE or FALSE — EXPLAIN BRIEFLY YOUR ANSWER.

(a) A conviction under the Trust Receipts Law shall bar a pros- ecution for estafa under the Revised Penal Code. (2%)

SUGGESTED ANSWER

True, because the criminal violation of the trust receip agreement as when the entrustee does not deliver the proceeds of the sale of the goods subject of the trust receipt or fails to return the goods in case of non-sale already constitutes estate under the Revised Penal Code.

E received goods from T for display and sale in E's store. E was to turn over to T the proceeds of any sale and return the ones unsold. To document their agreement, E executed a trust receipt in T's favor covering the goods. When E failed to turn over the proceeds from the sale of the goods or return the ones unsold despite demand, he was charged in court for estafa. E moved to dismiss on the ground that his liability is only civil. Is he correct?

- a. No, since he committed fraud when he promised to pay for the goods and did not.
- b. No, since his breach of the trust receipt agreement subjects him to both civil and criminal liability for estafa.
- c. Yes, since E cannot be charged with estafa over goods covered a trust receipt.

d. Yes, since it was merely a consignment sale and the buyer could not pay.

Answer:

b. No, since his breach of the trust receipt agreement subjects him to both civil and criminal liability for estafa. (BAR 2011)

CCC Car, Inc. obtained a loan from BBB Bank, which fund was used to import 10 units of Mercedes Benz S Class vehicles. Upon arrival of the vehicles and before the release of said vehicles to CCC Car, Inc, X and Y, the president and treasurer, respectively, of CCC signed the Trust Receipt to cover the value of the 10 units of Mercedes Benz S class vehicles, after which, the vehicles were all delivered to the car display room of CCC. Sales of the vehicles were slow, and it took a month to dispose the 10 units. CCC wanted to be in business and to save on various documentations requires by the bank, decided that instead of turning over the proceeds of the sales, CCC used the proceeds to buy another 10 units of BMW 3 series.

Will the corporate officers of CCC be held liable under the circumstances? Explain your answer.

Answer:

Yes, particularly the president and the treasurer of CCC who both signed the trust receipts in the problem. Section 13 of the Trust receipts Law provides that if the violation or offense is committed by a corporation, partnership, association, or other juridical entity, the penalty provided for in the law shall be imposed upon the directors, officers, employees or other officials or persons therein responsible for the offense, without prejudice to the civil liabilities arising from the criminal offense. (BAR 2012)

BBB Banking Corporation issued a Letter of Credit in the amount of P5 M, for the purchase of 5 tons of corn by X, upon arrival of the goods, the goods were delivered to the warehouse of X, thereafter, he was asked to sign a Trust Receipt covering the goods. When the goods were sold, X did not deliver the proceeds to BBB Banking Corporation, arguing that he will need the fund for the subsequent importation. Is there sufficient basis to sue for criminal action?

- a. Yes, because X's failure to turn over the proceeds to the bank is a violation of the Trust Receipt Law;
- b. No, because the trust receipt was signed only after the delivery of the goods. When the trust receipt was signed, the ownership of the goods was already with X;
- c. Yes, because violation of Trust Receipt Law is mala prohibita, intention is irrelevant;
- d. No, because X has a valid reason not to deliver the proceeds to BBB Banking Corporation.

Answer:

A. Yes, because X's failure to turn over the proceeds to the bank is a violation of the Trust Receipt Law

C. Yes, because violation of Trust Receipt Law is mala prohibita, intention is irrelevant. (BAR 2012)

X secured a loan from BBB Bank to pay for the importation of some dried fruits. Upon arrival of the goods consisting of dried fruits imported by X but before delivery to him, a trust receipt was executed by X to cover the transfer of the dried fruits to his possession. The dried fruits were so saleable but instead of turning over the proceeds of the sale, X used the funds to pay for the medical expenses of his mother who was sick of cancer of the bone. Which statement is most accurate?

- a. X cannot be held criminally liable because although he did not pay the bank he used the proceeds for a good reason;
- b. Fraud or deceit is a necessary element to hold X criminally liable for non-payment under the Trust Receipts Law;
- c. X can be held criminally liable under the Trust Receipts Law regardless of the purpose or intention for the use of the proceeds;
- d. X cannot be held criminally liable because the underlying obligation is one of simple loan.

Answer:

c. X can be held criminally liable under the Trust Receipts Law regardless of the purpose or intention for the use of the proceeds. (BAR 2012)

X is the President of AAA Products Corporation. X signs all the Trust Receipts documents for certain importations of the company. In the event of failure to deliver the proceeds of the sale of the goods to the bank, which statement is most accurate?

- a. The criminal liability will not attach to X as president because of separate juridical personality;
- b. For violation of Trust Receipts Law, the law specifically provides for the imposition of penalty upon directors/officers of the corporation;
- c. The officer will not be held criminally accountable because he is just signing the trust receipt for and in behalf of the corporation;
- d. The officer of the corporation will be held liable provided it is clear that the officer concerned participated in the decision not to pay.

Answer:

b. For violation of Trust Receipts Law, the law specifically provides for the imposition of penalty upon directors/officers of the corporation. (BAR 2012)

D. Remedies Available

E. Warehouseman's Lien

Safe Warehouse, Inc. (Safe) issued on various dates negotiable warehouse receipts to Peter, Paul, and Mary covering certain goods deposited by the latter with the former. Peter, Paul, and Mary then negotiated and endorsed the warehouse receipts to Cyrus, Magnus, and Charles upon payment by the latter of valuable consideration for the warehouse receipts. Cyrus, Magnus, and Charles were not aware of, nor were they parties to any irregularity or infirmity affecting the title or the face of the warehouse receipts. On due dates of the warehouse receipts, Cyrus, Magnus, and Charle demanded that Safe surrender the goods to them. Safe refused because it warehouseman's claim must first be paid. Cyrus, Magnus, and Charles refuse to pay, and insisted that such claim was the liability of Peter, Paul, and Mary. (2017 BAR)

(a) What is a warehouseman's claim? (3%)

SUGGESTED ANSWER

- (a) A warehouseman's lien consists of the storage charge as well as other fees and charges as may be stipulated in the warehous receipt.
- (b) Is Safe's refusal to surrender the goods to Cyrus, Magnus, and Charles legally justified? Explain your answer. (3%)

SUGGESTED ANSWER

(b) Yes, Safe's refusal to surrender the goods is justified. Under the Warehouse Receipts Law, the warehouseman may withhold delivery of the goods unless the demand-to deliver is accompanied by an offer to pay the warehouseman's lien. The lien is possessory in nature. It attaches to the goods regardless of who is the owner thereof.

III. Negotiable Instruments Law

A. Forms, Interpretation and other General Principles

X issued a check in favor of his creditor, Y. It reads: "Pay to Y the amount of Seven Thousand Hundred Pesos (Php700,000.00). Signed, X." What amount should be construed as true in such case?

- **a.** Php 700,000.00.
- **b.** Php 700.00.
- **c.** Php 7,000.00.
- **d.** Php 700,100.00.

Answer:

a. Php 700,000.00. (BAR 2011)

P sold to M a pair of gecko (tuko) for P50,000. M issued a promissory note to P promising to pay the money within 90 days. Unknown to P and M, a law was passed a month before the sale that prohibits and declares void any agreement to sell gecko in the country. If X acquired the note in good faith and for value, may he enforce payment on it?

- a. No, since the law declared void the contract on which the promissory note was founded.
- b. No, since it was not X who bought the gecko.
- c. Yes, since he is a holder in due course of a note which is distinct from the sale of gecko.
- d. Yes, since he is a holder in due course and P and M were not aware of the law that prohibited the sale of gecko.

Answer:

a. No, since the law declared void the contract on which the promissory note was founded. (BAR 2011)

Negotiable instruments are used as substitutes for money, which means—

- a. That they can be considered legal tender.
- b. That when negotiated, they can be used to pay indebtedness;
- c. That at all times the delivery of the instrument is equivalent to delivery of the case:
- d. That at all times negotiation of the instruments requires proper indorsement.

Answer:

b. That when negotiated, they can be used to pay indebtedness; (BAR 2012)

In a negotiable instrument, when the sum is expressed both in numbers and in words and there is discrepancy between the words and numbers—

- a. The sum expressed in words will prevail over the one expressed in numbers:
- b. The sum expressed in numbers will prevail over the one expressed in words:
- c. The instrument becomes void because of the discrepancy;
- d. This will render the instrument invalid.

Answer:

a. The sum expressed in words will prevail over the one expressed in numbers. (BAR 2012)

1. Requisites of Negotiability

TRUE or FALSE. A document, dated July 15, 2009, that reads: "Pay to X or order the sum of P5,000.00 five days after his pet dog, Sparky, dies. Signed Y." is a negotiable instrument.

True. The document is subject to a term and not a condition. The dying of the dog is a day which is certain to com. Therefore, the order to pay is unconditional, in compliance with Section 1 of the NIL. (BAR 2009)

Lorenzo drew a bill of exchange in the amount of P100,000 payable to Barbara or order, with his wife, Diana, as drawee. At the time the bill was drawn, Diana was unaware that Barbara is Lorenzo's paramour.

Barbara then negotiated the bill to her sister, Elena, who paid for it for value, and who did not know who Lorenzo was. On due date, Elena presented the bill to Diana for payment, but the latter promptly dishonored the instrument because, by then, Diana had already learned of her husband's dalliance.

Does the illicit cause or consideration adversely affect the negotiability of the bill? Explain.

Answer:

No. The illicit cause or consideration does not adversely affect the negotiability of the bill, especially in the hands of a holder in due course. Under Sec. 1 of the NIL, the bill of exchange is a negotiable instrument. Every negotiable instrument is deemed prima facie to have been issued for valuable consideration, and every person whose signature appears thereon is deemed to have become a party thereto for value. (BAR 2009)

A promissory note states, on its face: "I, X, promise to pay Y the amount of P5,000.00 five days after completion of the on-going construction of my house. Signed, X." Is the note negotiable?

- a. Yes, since it is payable at a fixed period after the occurrence of a specified event.
- b. No, since it is payable at a fixed period after the occurrence of an event which may not happen.
- c. Yes, since it is payable at a fixed period or determinable future time.
- d. No, since it should be payable at a fixed period before the occurrence of a specified event.

Answer:

b. No, since it is payable at a fixed period after the occurrence of an event which may not happen. (BAR 2011)

A writes a promissory note in favor of his creditor, B. it says: Subject to my option, I promise to pay B P1 M or his order to give P1 M worth of cement or to authorize him to sell my house worth P1 M. signed, A." Is the note negotiable?

a. No, because the exercise of the option to pay lies with A, the maker and debtor.

- b. No, because it authorizes the sale of collateral securities in case the note is not paid at maturity.
- c. Yes, because the note is really payable to B or his order, the other provisions being merely optional.
- d. Yes, because an election to require something to be done in lieu of payment of money does not affect negotiability.

a. No, because the exercise of the option to pay lies with A, the maker and debtor. (BAR 2011)

B borrowed P1 M from L and offered to him his BMW car worth P1 M as collateral. B then executed a promissory note that reads: "I, B, promise to pay L or bearer the amount of P1 M and to keep my BMW car (loan collateral) free from any other encumbrance. Signed, B." Is this note negotiable?

- a. Yes, since it is payable to bearer.
- b. Yes, since it contains an unconditional promise to pay a sum certain in money.
- c. No, since the promise to just pay a sum of money is unclear.
- d. No, since it contains a promise to do an act in addition to the payment of money.

Answer:

d. No, since it contains a promise to do an act in addition to the payment of money. (BAR 2011)

Indicate and explain whether the promissory note is negotiable or non-negotiable.

- a. I promise to pay A or bearer P100,000 from my inheritance which I will get after the death of my father.
- b. I promise to pay A or bearer P100,000 plus the interest rate of 90—day treasury bills.
- c. I promise to pay A or bearer P100,000 if A passes the 2012 bar exams.
- d. I promise to pay A or bearer P100,000 on or before December 30, 2012.
- e. I promise to pay A or bearer P100,000.

Answer:

a. Not negotiable. There is no unconditional promise to pay a sum certain in money as the promise is to pay the amount out of a particular funds, i.e., the inheritance from the father of the promisor.

b. Not negotiable. There is no unconditional promise to pay a sum certain in money. The promise to pay "the interest rate of 90—day treasury bills" is vague because, first, there are no 90—day treasury bills; second, the promise does not specify whether the so-called "interest rate" is that established at the primary market (where new T-bills are sold for the first time by the Bureau of Treasury) or at the secondary market (where T bill can be bought and sold after they have been issued in the primary market); and

third, T-bills are conventionally quoted in terms of their discount rate, rather than their interest rate. They do not pay any interest directly; instead, they are sold at a discount of their face value and thus "earn" by selling at face value upon maturity.

- c. Not negotiable. The promise to pay is subject to a condition, i.e., that A will pass the 2012 bar exams.
- d. Negotiable. It conforms fully with the requirements of negotiability under Section 1 of NIL.
- e. Negotiable. It conforms fully with the requirements of negotiability under Section 1 of NIL. It is payable on demand because the note does not express a time for its payment. (BAR 2012)

X issued a promissory note which states, "I promise to pay Y or order P100,000 or 1 unit Volvo Sedan." Which statement is most accurate?

- a. The promissory note is negotiable because the forms of payment are clearly stated;
- b. The promissory note is non-negotiable because the option as to which form of payment is with the maker;
- c. The promissory note is an invalid instrument because there is more than one form of payment;
- d. The promissory note can be negotiated by way of delivery.

Answer:

b. The promissory note is non-negotiable because the option as to which form of payment is with the maker (BAR 2012)

X issued a promissory note which states "I promise to pay Y or bearer the amount of HK\$50,000 on or before December 30, 2013." Is the promissory note negotiable?

- a. No, the promis<mark>sory note becomes invalid because t</mark>he amount is in foreign currency;
- b. Yes, the promissory note is negotiable even though the amount is stated in foreign currency;
- c. No, the promissory note is not negotiable because the amount is in foreign currency;
- d. Yes, the promissory note is negotiable because the Hong Kong dollar is a known foreign currency in the Philippines.

Answer:

b. Yes, the promissory note is negotiable even though the amount is stated in foreign currency (BAR 2012)

As payment for a debt, X issued a promissory note in favor of Y but the promissory note on its face was marked non-negotiable. Then Y instead of

indorsing the promissory note, assigned the same in favor of Z to whom he owed some debt also. Which statement is most accurate?

- a. Z cannot claim payment from X on the basis of the promissory note because it is marked nonnegotiable;
- b. Z can claim payment from X even though it is marked non-negotiable;
- c. Z can claim payment from Y because under the NIL, negotiation and assignment is one and the same;
- d. Z can claim payment from Y only because he was the endorser of the promissory note.

Answer:

b. Z can claim payment from X even though it is marked non-negotiable; (BAR 2012)

Antonio issued the following instrument:

August 10, 2013 Makati City

P100,000.00

Sixty days after date, I promise to pay Bobby or his designated representative the sum of ONE HUNDRED THOUSAND PESOS (P100,000.00) from my BPI Acct. No. 1234 if, by this due date, the sun still sets in the west to usher in the evening and rises in the east the following morning to welcome the day.

(Sqd.) Antonio Reyes

Explain each requirement of negotiability present or absent in the instrument.

Answer:

- a. The instrument contains a promise to pay and was signed by the maker, Antonio Reyes.
- b. The promise to pay is unconditional insofar as the reference to the setting of the sun in the west in the evening and its rising in east in the morning are concerned. These are certain to happen. The promise to pay is conditional, because the money will be taken from a particular fund, BPI Acct. No. 1234.
- c. The instrument contains a promise to pay a sum certain in money, P100,000.00.
- d. The money is payable at a determinable future time, 60 days after August 10, 2013.
- e. The instrument is not payable to order or to bearer. (BAR 2013)

Which of the following instruments is negotiable if all the other requirements of negotiability are met?

a. A promissory note with promise to pay out of the U.S. Dollar account of the maker in XYZ Bank.

- b. A promissory note which designates the U.S. Dollar currency in which payment is to be made.
- c. A promissory note which contains in addition a promise to paint the portrait of the bearer.
- d. A promissory note made payable to the order of Jose Cruz or Josefa Cruz.

b. A promissory note which designates the US Dollar currency in which payment is to be made (BAR 2014)

- a. Order Instrument
- b. Bearer Instrument

M makes a promissory note that states: "I, M, promise to pay P5,000.00 to B or bearer. Signed, M." M negotiated the note by delivery to B, B to N, N to O. B had known that M was bankrupt when M issued the note. Who would be liable to O?

- a. M and N sine they may be assumed to know of M's bankruptcy.
- b. N, being O's immediate negotiator of a bearer note.
- c. B, M, and N, being indorsers by delivery of a bearer note.
- d. B, having known of M's bankruptcy.

Answer:

b. N, being O's immediate negotiator of a bearer note. (BAR 2011)

X delivered a check issued by him and payable to the order of CASH to Y in payment for certain obligations incurred by X in favor of Y. Y then delivered the checks to Z in payment for certain obligations. Which statement is most accurate?

- a. Z can encash the check even though Y did not indorse the check;
- b. Z cannot encash the check for lacking in proper endorsement;
- c. Y is the only one liable because he was the one who delivered the check to Z:
- d. The negotiation is not valid because the check is an instrument payable to order.

Answer:

a. Z can encash the check even though Y did not indorse the check. (BAR 2012)

Which phrase best completes the statement— A check which is payable to bearer is a bearer instrument and:

- a. Negotiation can be made by delivery only;
- b. Negotiation must be by written indorsement;
- c. Negotiation must be by specific indorsement;
- d. Negotiation must be by indorsement and delivery.

Answer:

- a. Negotiation can be made by delivery only; (BAR 2012)
 - 2. Kinds of Negotiable Instruments
 - a. Bill of Exchange
 - b. Promissory Note

When can you treat a bill of exchange as a promissory note? (2015)

Answer:

A bill of exchange may be treated as a promissory note in the following instances.

- 1. The drawee is a fictitious person or a person not having the capacity to contract;
- 2. The drawer and the drawee are one and the same person.
- 3. Where the instrument is so ambiguous that there is a doubt as to whether the instrument is a bill or a note, the holder may treat it either as a bill or note, at the option of the holder (Secs. 130 and 17 of the NIL).

P authorized A to sign a bill of exchange in hi (P's) name. the bill reads: "Pay to B or order the sum of P1 M. Signed, A (for and in behalf of P)." The bill was drawn on P. B indorsed the bill to C, C to D, and D to E. May E treat the bill as a promissory note?

- a. No, because the instrument is payable to order and the same person.
- b. Yes, because the drawer and the drawee are one and the same person.
- c. No, because the instrument is a bill of exchange.
- d. Yes, because A was only an agent of P.

Answer:

b. Yes, because the drawer and the drawee are one and the same person. (BAR 2011)

If the drawer and the drawee are the same person, the holder may present the instrument for payment without need of a previous presentment for acceptance. In such case, the holder treats it as a

- a. Non-negotiable instrument.
- b. Promissory note.
- c. Letter of credit.
- d. Check.

Answer:

b. Promissory note. (BAR 2011)

A promissory note which is undated is presumed to be—

- A. Dated as of the date of issue:
- B. Dated as of the date of the first indorsement:
- C. Promissory note is invalid because there is no date;
- D. Dated on due date.

a. Dated as of the date of issue. (BAR 2012)

B. Completion and Delivery

- 1. Insertion of Date
- 2. Completion of Blanks

3. Incomplete and Undelivered Instruments

- 4. Complete but Undelivered Instruments
- C. Signature
 - 1. Signing in Trade Name

A check was issued to Tiger Woods. But what was written as payee is the word "Tiger Woods". To validly endorse the check—

- a. Tiger Woods must sign his real name;
- b. Tiger Woods must sign both his real name and assumed name;
- c. Tiger Woods can sign his assumed name;
- d. The check has become non-negotiable.

Answer:

c. Tiger Woods can sign his assumed name. (BAR 2012)

2. Signature of Agent

In a signature by procuration, the principal is bound only in case the agent acted within the actual limits of his authority. The signature of the agent in such a case operates as notice that he has

- a. A qualified authority to sign.
- b. A limited authority to sign.
- c. A special authority to sign.
- d. A full authority to sign.

Answer:

b. A limited authority to sign. (BAR 2011)

Under the NIL, a signature by the procuration operates as a notice that the agent has but a limited authority to sign. Thus, a person who takes a bill that is drawn, accepted, or indorsed by procuration is duty-bound to inquire into the extent of the agent's authority by:

- a. Examining the agent's special power of attorney.
- b. Examining the bill to determine the extent of such authority.
- c. Asking the agent about the extent of such authority.
- d. Asking the principal about the extent of such authority.

b. Examining the bill to determine the extent of such authority. (BAR 2011)

3. Indorsement by Minor or Corporation

A bill of exchange has T for its drawee, U as drawer, and F as holder. When F went to T for presentment, F learned that T is only 15 years old. F wants to recover from U but the latter insists that a notice of dishonor must first be made the instrument being a bill of exchange. Is he correct?

- a. Yes, since a notice of dishonor is essential to charging the drawer.
- b. No, since T can waive the requirement of notice of dishonor.
- c. No, since F can treat U as maker due to minority of T, the drawee.
- d. Yes, since in a bill of exchange, notice of dishonor is at all times required.

Answer:

c. No, since F can treat U as maker due to minority of T, the drawee. (BAR 2011)

Y, as President of and in behalf of AAA Corporation, as a way to accommodate X, one of its stockholders, endorsed the check issued by X. Which statement is most accurate?

- a. It is an ultra vires act;
- b. It is a valid indorsement;
- c. The corporation will be held liable to any holder in due course;
- d. It is an invalid indorsement.

Answer:

- a. It is an ultra vires act.
- d. It is a valid indorsement. (BAR 2012)

4. Forgery

TRUE or FALSE — EXPLAIN BRIEFLY YOUR ANSWER.

(e) Forgery is a real defense but may only be raised against a holder not in due course. (2%) (2017 BAR)

SUGGESTED ANSWER

(e) False, because forgery, as a real defense, can be raised wen against a holder in due course.

After securing a PI million loan from B, A drew in B's favor a bill of exchange with C as drawee. The bill reads:

"October 1, 2016.

Pay to the order of B the sum of P1 million.

To: C (drawee). Signed, A."

A then delivered the bill to B who, however, lost it. It turned out that it was stolen by D, B's brother. D lost no time in forging B's signature and negotiated it to E who acquired it for value and in good faith.

May E recover on the bill from C, the drawee? Explain. (2016 Bar)

SUGGESTED ANSWER

No, E cannot recover from C, the drawee. The forged endorsement of B did not result in the transfer of title in favur of E as no right can be acquired under such forged endorsement

Nadine has a checking account with Fair & Square Bank. One day, she lost her checkbook and the finder was able to forge her signature and encash the forged check. Will Nadine be able to recover the amount debited from her checking account from Fair & Square Bank? Justify your answer. (2015)

Answer:

Yes, Nadine should be able to recover the amount debited from her checking account from Fair and Square Bank. The Bank is supposed to know the signature of its clients. The Bank was thus negligent in not detecting the forgery of Nadine's signature and paying the check. Under the circumstances, there was no negligence on the part of Nadine which would preclude her from invoking forgery (*Philippine National Bank v. Quimpo, 158 SCRA 582*).

To cover his medical bill, A issued a check payable to Dr. Prospero Fuego. He put the check in a sealed envelope and gave it to X, his trusted messenger for 8 years, for delivery to Dr. Fuego. X, suspecting that the envelope contained a check, opened it, forged Dr. Fuego's signature on the back of the check, and deposited the check in his own savings account with the PNB. The PNB credited the amount of the check to X's account after it had been cleared by the drawee, the PCIB. When A asked X for Dr. Fuego's receipt, X replied that Dr. Fuego was out of town but his secretary received the check.

One week later, A called Dr. Fuego and was surprised to discover that the latter never got the check. X feigning illness, had been absent for the last 2 days and, therefore, could not be questioned, A immediately went to the PCIB and found that his check had been cleared 4 days before. Upon PCIB's immediate inquiry from the PNB, the latter informed the former that X had already been paid the amount of the check and had in fact closed his account 2 days before.

A demands that the PCIB recredit his account with the amount of the check. PCIB, in turn, demands that PNB reimburse it.

Decide with reasons.

As against the PCIB, A is entitled to a recredit of the amount of the check. Under the NIL, a forged signature is wholly inoperative to give any right to any party to enforce payment thereof or to give a discharge thereof, unless the party against whom such right is being enforced is precluded from setting up forgery. Under this provision, the PCIB, the drawee bank, because of the forged signature of Dr. Fuego, did not obtain any right to discharge the instrument by clearing/paying it and must therefore account to A for doing so. A bank is duty bound to pay only according to the order of the drawer. Here the order of A was to pay Dr. Fuego or anyone who legally obtains his indorsement. The PCIB did not follow A's order and must therefore account to him.

On the other hand, the PNB must also account to the PCIB because it paid to X the forger who had no right to enforce payment of the check, by clearing the check, the PCIB cannot be said to be in estoppel as it was not aware of the forgery. Unlike the case of the forgery of the drawer's signature where the drawee by paying/clearing admits the genuineness of such signature, the PCIB by paying or clearing the check had not impliedly warranted that any indorsement on the check is genuine. It was incumbent on the PNB to satisfy itself that Dr. Fuego's signature was genuine before paying or receiving the check, and as between two innocent banks, the PNB which made the loss possible, must suffer the burden of such loss. Its remedy lies against X the forger, who is legally liable not only civilly but criminally.

TRUE or FALSE. A bank is bound to know its depositor's signature" is an inflexible rule in determining the liability of a bank in forgery cases.

Answer:

False. In cases of forgery, the forger may not necessarily be a depositor of the bank, especially in the case of a drawee bank. Yet in many cases of forgery, it is the drawee that is held liable for the loss. (BAR 2009)

Forgery of bills of exchange may be subdivided into, a) forgery of an indorsement on the bill and b) forgery of the drawer's signature, which may either be with acceptance by the drawee, or

- a. With acceptance but the bill is paid by the drawee.
- b. Without acceptance but the bill is paid by the drawer.
- c. Without acceptance but the bill is paid by the drawee.
- d. With acceptance but the bill is paid by the drawer.

Answer:

c. Without acceptance but the bill is paid by the drawee. (BAR 2011)

Due to his debt to C, D wrote a promissory note which is payable to the order of C. C's brother, M, misrepresenting himself as agent of C, obtained the note from D. M then negotiated the note to N after forging the signature of C. May N enforce the note against D?

- a. Yes, since D is the principal debtor.
- b. No, since the signature of C was forged.
- c. No, since it is C who can enforce it, the note being payable to the order of C.
- d. Yes, since D, as maker, is primarily liable on the note.

b. No, since the signature of C was forged. (BAR 2011)

X found a check on the street, drawn by Y against ABC Bank, with Z as payee. X forged Z's signature as an indorser, then indorsed it to ABC Bank which charged it to the Y's account. Y later sued ABC Bank but it set up the forgery as its defense. Will it prosper?

- a. No, since the payee's signature has been forged.
- b. No, since Y's remedy is to run after the forger, X.
- c. Yes, since forgery is only a personal defense.
- d. Yes, since ABC Bank is bound to know the signature of Y, its client.

Answer:

d. Yes, since ABC Bank is bound to know the signature of Y, its client. (BAR 2011)

NB The better answer based on jurisprudence is that ABC Bank is liable because it violated the instruction of the drawer to pay only Y or any party who acquires title by virtue of Y's endorsement. This is not a case of forgery of the drawer's signature where the Bank may be charged for negligence in not detecting the forgery of the drawer's signature.

D. Consideration

E. Accommodation Party

X acted as an accommodation party in signing as a maker of a promissory note. Which phrase best completes the sentence—This means that X is liable on the instrument to any holder for value:

- a. For as long as the holder does not know that X is only an accommodation party;
- b. Even though the holder knew all along that X is only an accommodation party;
- c. For as long as X did not receive any consideration for acting as accommodation party;
- d. Provided X received consideration for acting as accommodation party.

Answer:

b. Even though the holder knew all along that X is only an accommodation party. (BAR 2012)

F. Negotiation

1. Distinguished from Assignment

Gaudencio, a store owner, obtained a P1 M loan from Bathala Financing Corporation (BFC). As security, Gaudencio executed a "Deed of Assignment of Receivables," assigning 15 checks received from various customers who bought merchandise from his store. The checks were duly indorsed by Gaudencio's customers.

The Deed of Assignment contains the following stipulation:

"If, for any reason, the receivables or any part thereof cannot be paid by the obligors, the ASSIGNOR unconditionally and irrevocably agrees to pay the same, assuming the liability to pay, by way of a penalty, 3% of the total amount unpaid, for the period of delay until the same is fully paid."

When the checks became due, BFC deposited them for collection, but the drawee banks dishonored all the checks for one of the following reasons: "account closed," "payment stopped," "account under garnishment," or "insufficiency of funds". BFC wrote Gaudencio notifying him of the dishonored checks, and demanding payment of the loan. Because Gaudencio did not pay, BFC filed a collection suit.

In his defense, Gaudencio contended that: (a) BFC did not give timely notice of dishonor of the checks; and (b) considering that the checks were duly indorsed, BFC should proceed against the drawers and the indorsers of the checks.

Are Gaudencio's defenses tenable? Explain.

Answer:

No. Gaudencio's defenses are untenable. The cause of action of BFC was really on the contract of loan, with the checks merely serving as collateral to secure the payment of the loan. By virtue of the Deed of Assignment which he signed, Gaudencio undertook to pay for the receivables if for any reason they cannot be paid by the obligors. (BAR 2009)

A issued a check in the amount of P20,000 payable to B. B endorsed the check but only to the extent of P10,000. Which statement is most accurate?

- a. The partial indorsement is not a valid indorsement, although will result in the assignment of that part;
- b. The partial indorsement will invalidate the whole instrument;
- c. The endorsee will be considered as a holder in due course;
- d. The partial indorsement is valid indorsement up to the extent of the P10.000.

Answer:

a. The partial indorsement is not a valid indorsement, although will result in the assignment of that part. (BAR 2012)

A promissory note which does not have the words "or order" or "or bearer" will render the promissory note non-negotiable and, therefore—

- a. It will render the maker not liable;
- b. The note can still be assigned and the maker made liable;
- c. The holder can become holder in due course;
- d. The promissory note can just be delivered and the maker will still be liable.

Answer:

b. The note can still be assigned and the maker made liable. (BAR 2012)

- 2. Modes of Negotiation
- 3. Kinds of Indorsements

A negotiable instrument can be indorsed by way of a restrictive indorsement, which prohibits further negotiation and constitutes the indorsee as agent of the ondorser. As agent, the indorsee has the right, among others, to:

- a. Demand payment of the instrument only.
- b. Notify the drawer of the payment of the instrument.
- c. Receive payment of the instrument.
- d. Instruct that payment be made to the drawee.

Answer:

c. Receive payment of the instrument. (BAR 2011)

X is the holder of an instrument payable to him (X) or his order, with Y as maker. X then indorsed it as follows: "Subject to no recourse, pay to Z. Signed, X." When Z went to collect from Y, it turned out that Y's signature was forged. Z now sues X for collection. Will it prosper?

- a. Yes, because X, as a conditional indorser, warrants that the note is genuine.
- b. Yes, because X, as a qualified indorser, warrants that the note is genuine.
- c. No, because X made a qualified indorsement.
- d. No, because a qualified indorsement does not include the warranty of genuineness.

Answer:

b. Yes, because X, as a qualified indorser, warrants that the note is genuine. (BAR 2011)

P sold to M 10 grams of shabu worth P5,000. As he had no money at the time of the sale, M wrote a promissory note promising to pay P or his order P5,000. P then indorsed the note to X (who did not know about the shabu), and X to Y.

Unable to collect from P, Y then sued X on the note. X set up the defense of illegality of consideration. Is he correct?

- a. No, since X, being a subsequent indorser, warrants that the note is valid and subsisting.
- b. No, since X, a general indorser, warrants that the note is valid and subsisting.
- c. Yes, since a void contract does not give rise to any right.
- d. Yes, since the note was born of an illegal consideration which is real defense.

Answer:

b. No, since X, a general indorser, warrants that the note is valid and subsisting. (BAR 2011)

G. Rights of the Holder

Under the NIL, if the holder has a lien on the instrument which arises either from a contract or by implication of law, he would be a holder for value to the extent of

- a. His successor's interest.
- b. His predecessor's interest.
- c. The lien in his favor.
- d. The amount indicated on the instrument's face.

Answer:

- c. The lien in his favor. (BAR 2011)
 - a. Shelter Principle
 - b. Holder in Due Course

Lorenzo drew a bill of exchange in the amount of P100,000 payable to Barbara or order, with his wife, Diana, as drawee. At the time the bill was drawn, Diana was unaware that Barbara is Lorenzo's paramour.

Barbara then negotiated the bill to her sister, Elena, who paid for it for value, and who did not know who Lorenzo was. On due date, Elena presented the bill to Diana for payment, but the latter promptly dishonored the instrument because, by then, Diana had already learned of her husband's dalliance.

Was the bill lawfully dishonored by Diana? Explain.

Answer:

No, the bill was not lawfully dishonored by Diana. Elena, to whom the instrument was negotiated, was a holder in due course inasmuch as she paid value therefor in good faith. (BAR 2009)

A holder in due course holds the instrument free from any defect of title of prior parties and free from defenses available to prior parties among themselves. An example of such defense is-

- a. Fraud in inducement.
- b. Duress amounting to forgery.
- c. Fraud in esse contractus.
- d. Alteration.

Answer:

a.Fraud in inducement. (BAR 2011)

X borrowed money from Y in the amount of P1 M and as payment, issued a check. Y then endorsed the check to his sister Z for no consideration. When Z deposited the check to her account, the check was dishonored for insufficiency of funds.

Is Z a holder in due course? Explain your answer.

Answer:

Z is not a holder in due course. She did not give any valuable consideration for the check. To be a holder in due course, the holder must have taken the check in good faith and for value. (BAR 2012)

Arnold, representing himself as an agent of Brian for the sale of Brian's car, approached Dennis who appeared interested in buying the car. At Arnold's prodding, Dennis issued a crossed check payable to Brian for P25,000 on the understanding that the check would only be shown to Brian as evidence of Dennis' good faith and interest in buying the car. Instead, Arnold used the check to pay for the medical expenses of his wife in Brian's clinic after Brian, a doctor, treated her.

Is Brian a holder in due course?

- a. Yes, Brian is a HIDC because he was the payee of the check and he received it for services rendered;
- b. Yes, Brian is a HIDC because he did not need to go behind the check that was payable to him;
- c. No, Brian is not a HIDC because Dennis issued the check only as evidence of good faith and interest in buying the car;
- d. No, Brian is not a HIDC because Brian should have been placed on notice: the check was crossed in his favor and Arnold was not the drawer;
- e. No, Brian is not a HIDC because the requisite consideration to Dennis was not present.

Answer:

d. No, Brian is not a HIDC because Brian should have been placed on notice: the check was crossed in his favor and Arnold was not the drawer. (BAR 2013)

c. Defenses Against the Holder

H. Parties And Their Liabilities

a. Maker

X executed a promissory note with a face value of P50,000, payable to the order of Y. Y indorsed the note to Z, to whom Y owed P30,000. If X has no defense at all against Y, for how much may Z collect from X?

- a. P20,000, as he is a holder for value to the extent of the difference between Y's debt and the value of the note.
- b. P30,000, as he is a holder for value to the extent of his lien.
- c. P50,000, but with the obligation to hold P20,000 for Y's benefit.
- d. None, as Z's remedy is to run after his debtor, Y.

Answer:

c. P50,000, but with the obligation to hold P20,000 for Y's benefit. (BAR 2011)

b. Drawer

D draws a bill of exchange that states: "One month from date, pay to B or his order P100,000. Signed, D." The drawee named in the bill is E. B negotiated the bill to M, M to N, N to O, and O to P. Due to nonacceptance and after proceedings for dishonor were made, P asked O to pay, which O did. From whom may O recover?

- a. B, being the payee.
- b. N, as indorser to O.
- c. E, being the drawee.
- d. D. being the drawer.

Answer:

d. D, being the drawer. (BAR 2011)

NB he may recover from any one of N, B and D because of their liability as endorser and drawer, respectively provided notice of dishonor given to each of them

X borrowed money from Y in the amount of P1 M and as payment, issued a check. Y then endorsed the check to his sister Z for no consideration. When Z deposited the check to her account, the check was dishonored for insufficiency of funds.

Who is liable on the check? The drawer or the indorser? Explain your answer.

Answer:

X, the drawer, will be liable. As drawer, X engaged that on due presentment the check would be paid according to its tenor and that if it is dishonored and he is given notice of dishonor, he will pay the amount to the holder. No notice of dishonor need be given to X if he is aware that he has insufficient funds in his account. Under Section 114(d) of the

NIL, notice of dishonor is not required to be given to the drawer where he has no right to expect that the drawee will honor the instrument.

Z cannot hold Y, the endorser, liable as the latter can raise the defense that there was no valuable consideration for the endorsement of the check. (BAR 2012)

c. Acceptor

A bill of exchange has D as drawer, E as drawee and F as payee. The bill was then indorsed to G, G to H, and H to I, the current holder presented the bill to E for acceptance. E accepted but, as it later turned out, D is a fictitious person. Is E freed from liability?

- a. No, since by accepting, E admits the existence of the drawer.
- b. No, since by accepting, E warrants that he is solvent.
- c. Yes, if E was not aware of that fact at the time of acceptance.
- d. Yes, since a bill of exchange with a fictitious drawer is void and inexistent.

Answer:

a. No, since by accepting, E admits the existence of the drawer. (BAR 2011)

d. Indorser

May the indorsee of a promissory note indorsed to him "for deposit" file a suit against the indorser?

- a. Yes, as long as the indorser received value for the restrictive indorsement.
- b. Yes, as long as the indorser received value for the conditional indorsement.
- c. Yes, whether or not the indorser received value for the conditional indorsement.
- d. Yes, whether or not the indorser received value for the restrictive indorsement.

Answer:

a. Yes, as long as the indorser received value for the restrictive indorsement. (BAR 2011)

Z wrote out an instrument that states: "Pay to X the amount of P1 M for collection only. Signed, Z." X indorsed it to his creditor, Y, to whom he owed P1 M. Y now wants to collect and satisfy X's debt through the P1 M on the check. May he validly do so?

- a. Yes, since the indorsement to Y is for P1 M.
- b. No, since Z is not a party to the loan between X and Y.
- c. No, since X is merely an agent of Z, his only right being to collect.
- d. Yes. since X owed Y P1 M.

c. No, since X is merely an agent of Z, his only right being to collect. (BAR 2011)

Which of the following indorsers expressly warrants in negotiating a instrument that 1) it is genuine and true; 2) he has a good title to it; 3) all prior parties have capacity to negotiate; and 4) it is valid and subsisting at the time of his indorsement?

- a. The irregular indorser.
- b. The regular indorser.
- c. The general indorser.
- d. The qualified indorser.

Answer:

c. The general indorser. (BAR 2011)

M, the maker, issued a promissory note to P, the payee which states: "I, M, promise to pay P or order the amount of Php1 Million. Signed, M." P negotiated the note by indorsement to N, then N to O also by indorsement, and O to Q, again by indorsement. But before O indorsed the note to Q, O's wife wrote the figure "2" on the note after "Php1" without O's knowledge, making it appear that the note is for Php12 Million. For how much is O liable to Q?

- a. Php 1 Million since it is the original tenor of the note.
- b. Php 1 Million since he warrants that the note is genuine and in all respects what it purports to be.
- c. Php 12 Million since he warrants his solvency and that he has a good title to the note.
- d. Php 12 Million since he warrants that the note is genuine and in all respects what it purports to be.

Answer:

d. Php 12 Million since he warrants that the note is genuine and in all respects what it purports to be. (BAR 2011)

D, debtor of C, wrote a promissory note payable to the order of C. C's brother, M, misrepresenting himself as C's agent, obtained the note from D, then negotiated it to N after forging C's signature. N indorsed it to E, who indorsed it to F, a holder in due course. May F recover from E?

- a. No, since the forgery of C's signature results in the discharge of E.
- b. Yes, since only the forged signature is inoperative and E is bound as indorser.
- c. No, since the signature of C, the payee, was forged.
- d. Yes, since the signature of C is immaterial, he being the payee.

Answer:

b. Yes, since only the forged signature is inoperative and E is bound as indorser. (BAR 2011)

X is the holder of an instrument payable to him (X) or his order, with Y as maker. X then indorsed it as follows: "Subject to no recourse, pay to Z. Signed, X." When Z went to collect from Y, it turned out that Y's signature was forged. Z now sues X for collection. Will it prosper?

- a. Yes, because X, as a conditional indorser, warrants that the note is genuine.
- b. Yes, because X, as a qualified indorser, warrants that the note is genuine.
- c. No, because X made a qualified indorsement.
- d. No, because a qualified indorsement does not include the warranty of genuineness.

Answer:

b. Yes, because X, as a qualified indorser, warrants that the note is genuine. (BAR 2011)

P sold to M 10 grams of shabu worth P5,000. As he had no money at the time of the sale, M wrote a promissory note promising to pay P or his order P5,000. P then indorsed the note to X (who did not know about the shabu), and X to Y. Unable to collect from P, Y then sued X on the note. X set up the defense of illegality of consideration. Is he correct?

- a. No, since X, being a subsequent indorser, warrants that the note is valid and subsisting.
- b. No, since X, a general indorser, warrants that the note is valid and subsisting.
- c. Yes, since a void contract does not give rise to any right.
- d. Yes, since the note was born of an illegal consideration which is real defense.

Answer:

b. No, since X, a general indorser, warrants that the note is valid and subsisting. (BAR 2011)

e. Drawee

Marlon deposited with LYRIC bank a money market placement of P1 M for a term of 31 days. On maturity date, one claiming to be Marlon called up the LYRIC Bank account officer and instructed him to give the manager's check representing the proceeds of the money market placement to Marlon's girlfriend, Ingrid.

The check, which bore the forged signature of Marlon, was deposited in Ingrid's account with YAMAHA Bank. YAMAHA Bank stamped a guaranty on the check reading: "All prior endorsements and/or lack of endorsement guaranteed."

Upon presentment of the check, LYRIC Bank funds the check. Days later, Marlon goes to LYRIC Bank to collect his money market placement and discovers the foregoing transactions.

Marlon thereupon sues LYRIC Bank which in turn files a third-party complaint against YAMAHA Bank. Discuss the respective rights and liabilities of the two banks.

Answer:

Since the money market placement of Marlon is in the nature of a loan to Lyric Bank, and since he did not authorize the release of the money market placement to Ingrid, the obligation of Lyric Bank to him has not been paid. Lyric Bank still has the obligation to pay him.

Since Yamaha Bank indorsed the check bearing the forged endorsement of Marlon and guaranteed all endorsements, including the forged endorsement, when it presented the check to Lyric Bank, it should be held liable to it.

However, since the issuance of the check was attended with the negligence of Lyric Bank, it should share the loss with Yamaha Bank on a 50% basis. (BAR 2010)

A bill of exchange states on its face: "One (1) month after sight, pay to the order of Mr. R the amount of P50,000.00, chargeable to the account of Mr. S. Signed, Mr. T." Mr. S, the drawee, accepted the bill upon presentment by writing on it the words "I shall pay P30,000.00 three (3) months after sight." May he accept under such terms, which varies the command in the bill of exchange?

- a. Yes, since a drawee accepts according to the tenor of his acceptance.
- b. No, since, once he accepts, a drawee is liable according to the tenor of the bill.
- c. Yes, provided the drawer and the payee agree to the acceptance.
- d. No, since he is bound as drawee to accept the bill according to its tenor.

Answer:

a. Yes, since a drawee accepts according to the tenor of his acceptance. (BAR 2011)

The signature of X was forged as drawer of a check. The check was deposited in the account of Y and when deposited was accepted by AAA Bank, the drawee bank. Subsequently, AAA Bank found out that the signature of X was actually forged. Which statement is most accurate?

a. The drawee bank can recover from Y, because the check was deposited in his account;

- b. The drawee bank can recover from X, because he is the drawer even though his signature was forged;
- c. The drawee bank is estopped from denying the genuiness of the signature of the X, the drawer of the check;
- d. The drawee bank can recover from Y because as endorser he warrants the genuiness of the signature.

- c. The drawee bank is estopped from denying the genuineness of the signature of the X, the drawer of the check. (BAR 2012)
 - f. Warranties
- I. Presentment for Payment
 - 1. Necessity of Presentment for Payment
 - 2. Parties to Whom Presentment for Payment Should Be Made

X executed a promissory note in favor of Y by way of accommodation. It says: "Pay to Y or order the amount of P50,000.00. Signed, X." Y then indorsed the note to Z, and Z to T. When T sought collection from Y, the latter countered as indorser that there should have been a presentment first to the maker who dishonors it. Is Y correct?

- a. No, since Y is the real debtor and thus, there is no need for presentment for payment and dishonor by the maker.
- b. Yes, since as an indorser who is secondarily liable, there must first be presentment for payment and dishonor by the maker.
- c. No, since the absolute rule is that there is no need for presentment for payment and dishonor to hold an indorser liable.
- d. Yes, since the secondary liability of Y and Z would only arise after presentment for payment and dishonor by the maker.

Answer:

- a. No, since Y is the real debtor and thus, there is no need for presentment for payment and dishonor by the maker. (BAR 2011)
 - 3. Dispensation with Presentment for Payment
 - 4. Dishonor by Non-Payment
- J. Notice of Dishonor
 - a. Parties to Be Notified
 - b. Parties Who May Give Notice and Dishonor
 - c. Effect of Notice
 - d. Form of Notice
 - e. Waiver
 - f. Dispensation with Notice

Notice of dishonor is not required to be made in all cases. One instance where such notice is not necessary is when the indorser is the one to whom the instrument is suppose to be presented for payment. The rationale here is that the indorser

- a. already knows of the dishonor and it makes no sense to notify him of it.
- b. Is bound to make the acceptance in all cases.
- c. Has no reason to expect the dishonor of the instrument.
- d. Must be made to account for all his actions.

Answer:

- a. Already knows of the dishonor and it makes no sense to notify him of it. (BAR 2011)
 - g. Effect of Failure to Give Notice
- K. Discharge of Negotiable Instrument
 - a. Discharge of Negotiable Instrument

Is a manager's check as good as cash? Why or why not? (2015)

Answer:

Yes, the Supreme Court held in various decisions that a manager's check is good as cash. A manager's check is a check drawn by the bank against itself. It is deemed preaccepted by the bank from the moment of issuance. The check becomes the primary obligation of the bank which issues it and constitutes its written promise to pay. By issuing it, the bank in effect commits its total resources, integrity and honor behind the check (Tan v. CA, 239 SCRA 310; International Corporate Bank v. Gueco, 351 SCRA 516; Metrobank v. Chiok, GR No. 172652, Nov. 26, 2014).

ALTERNATIVE ANSWER:

Manager's check is not legal tender because under *Article 1249* of the *Civil Code*, checks do not produce the effect of payment until encashed or through the fault of the creditor; their value has been impaired. Moreover, under the Central Bank Act, the debtor cannot compel the creditor to accept checks in payment of a debt whether public or private (*Article 60 of RA 7653*).

Bong bought 300 bags of rice from Ben for P300,000. As payment, Bong indorsed to Ben a BPI check issued by Baby in the amount of P300,000. Upon presentment for payment, the BPI check was dishonored because Baby's account from which it was drawn has been closed. To replace the dishonored check, Bong indorsed a crossed DBP check issued also by Baby for P300,000. Again, the check was dishonored because of insufficient funds. Ben sued Bong and Baby on the dishonored BPI check. Bong interposed the defense that the BPI check was discharged by novation when Ben accepted the crossed DBP check as replacement for the BPI check. Bong cited Section 119 of the NIL which provides

that a negotiable instrument is discharged "by any other act which will discharge a simple contract for the payment of money." Is Bong correct?

Answer:

No. Bong is not correct. While Section 119 of the NIL in relation to Article 1231 of the Civil Code provides that one of the modes of discharging a negotiable instrument is by any other act which will discharge a simple contract for the payment of money, such as novation, the acceptance by the holder of another check which replaced the dishonored bank check did not result to novation.

There are only 2 ways which indicate the presence of novation and thereby produce the effect of extinguishing an obligation by another which substitutes the same. First, novation must be explicitly stated and declared in unequivocal terms as novation is never presumed. Secondly, the old and the new obligation must be incompatible on every point.

In the instant case, there was no express agreement that the holder's acceptance of the replacement check will discharge the drawer and endorser from liability. Neither is there incompatibility because both checks were given precisely to terminate a single obligation arising from the same transaction. (BAR 2014)

b. Discharge of Parties Secondarily Liable

The rule is that the intentional cancellation of a person secondarily liable results in the discharge of the latter. With respect to an indorser, the holder's right to cancel his signature is:

- a. Without limitation.
- b. Not limited to the case where the indorsement is necessary to his title.
- c. Limited to the case where the indorsement is not necessary to his title.
- d. Limited to the case where the indorsement is necessary to his title.

Answer:

c. Limited to the case where the indorsement is not necessary to his title. (BAR 2011)

Any agreement binding upon the holder to extend the time of payment or to postpone the holder's right to enforce the instrument results in the discharge of the party secondarily liable unless made with the latter's consent. This agreement refers to one which the holder made with the

- a. Principal debtor
- b. Principal creditor
- c. Secondary creditor
- d. Secondary debtor

Answer:

a. Principal debtor (BAR 2011)

- c. Right of Party Who Discharged Instrument
- d. Renunciation by Holder

L. Material Alteration

- 1. Concept
- 2. Effect of Material Alteration

Alfred issued a check for ₱1,000.00 to Benjamin, his friend, as payment for an electronic gadget. The check was drawn against Alfred's account with Good Bank. Benjamin then indorsed the check specially in favor of Cesar. However, Cesar misplaced the check. Dexter, a dormmate of Cesar, found the check, altered its amount to ₱91,000.00, and forged Cesar's indorsement by way of a blank indorsement in favor of Felix, a known jeweler. Felix then caused the deposit of the check in his account with Solar Bank. As collecting bank, Solar Bank stamped "all previous indorsements guaranteed" on the check. Seeing such stamp of the collecting bank, Good Bank paid the amount of ₱91,000.00 on the check.

May Good Bank claim reimbursement from Alfred? Explain your answer. (4%) (2017 BAR)

SUGGESTED ANSWER

Good Bank may claim reimbursement from Alfred but only for the amount of P1,000. It cannot recover the Php90, 000 difference because payment made under a materially altered check is not payment done in accordance with the instructions of the drawer. When Good Bank did not pay according to the tenor of the instrument, then it has no right to claim reimbursement from Alfred much less the right to deduct the erroneous payment it made from Alfred's account (Metrobank v. Cablizo, G.R. No. 69, December 6, 2006, 510 SCRA 259; Areza v. Express Savings Bank, No. 176697, September 10,2014).

ALTERNATIVE ANSWER

No. Good Bank cannot claim reimbursement from Alfred. The general rule is that in case of forgery of the indorsement of the payee of the check, the drawer cannot debit the drawer's account and the loss shall be borne by the drawee bank. The depository or collecting bank is liable to the drawee bank in case of forged endorsement (or endorsements other than the payee) because it guarantees all prior endorsements.

Can the drawee who accepts a materially altered check recover from the holder and the drawer?

- a. No, he cannot recover from either of them.
- b. Yes from both of them.
- c. Yes but only from the drawer.
- d. Yes but only from the holder.

Answer:

a. No, he cannot recover from either of them. (BAR 2011)

A material alteration of an instrument without the assent of all parties liable thereon results in its avoidance, EXCEPT against a

- a. Prior indorsee.
- b. Subsequent acceptor.
- c. Subsequent indorser.
- d. Prior acceptor.

Answer:

c. Subsequent indorser. (BAR 2011)

M. Acceptance

- a. Definition
- b. Manner

X, drawee of a bill of exchange, wrote the words: "Accepted, with promise to make payment within two day. Signed, X." The drawer questioned the acceptance as invalid. Is the acceptance valid?

- a. Yes, because the acceptance is in reality a clear assent to the order of the drawer to pay.
- b. Yes, because the form of the acceptance is really immaterial.
- c. No, because the acceptance must be a clear assent to the order of the drawer to pay.
- d. No, because the document must not express that the drawee will perform his promise within two days.

Answer:

a. Yes, because the acceptance is in reality a clear assent to the order of the drawer to pay. (BAR 2011)

- c. Time for Acceptance
- d. Rules Governing Acceptance

N. Presentment for Acceptance

P authorized A to sign a negotiable instrument in his (P's) name. It reads: "Pay to B or order the sum of P1 M. Signed, A (for and in behalf of P)." The instrument shows that it was drawn on P. B then indorsed to C, C to D, and D to E. E then treated it as a bill of exchange. Is presentment for acceptance necessary in this case?

- a. No, since the drawer and the drawee are the same person.
- b. No, since the bill is non-negotiable, the drawer and drawee being the same person.
- c. Yes, since the bill is payable to order, presentment is required for acceptance.
- d. Yes, in order to hold all persons liable on the bill.

- a. No, since the drawer and the drawee are the same person. (BAR 2011)
 - a. Time/Place/Manner of Presentment
 - b. Effect of Failure to Make Presentment
 - c. Dishonor by Non-Acceptance

O. Promissory Notes

P. Checks

In 2006, Donald, an American temporarily residing in Cebu City, issued to Rhodora a check for \$50,000.00 drawn against Wells Fargo Bank with offices in San Francisco, California. Rhodora negotiated the check and delivered it to Yaasmin, a Filipina socialite who frequently travelled locally and internationally. Because of her frequent travels, Yaasmin misplaced the check. It was only 11 years later on, in 2017, when she found the check inside a diary kept in her vault in her Hollywood, California house.

Discuss and explain the rights of Yaasmin on the check. (4%) (2017 BAR)

SUGGESTED ANSWER

Yasmin can not enforce the check against Donald and Rhodo since more than ten years had lapsed from check issuance. Action on check is barred by the statute of limitations

ALTERNATIVE ANSWER

This is a case of stale check, a check not presented within reasonable time from issuance; hence, Wells Fargo will be justified in refusing to honor the check if presented for payment. What Yasmin can do is to request Donald, the drawer, to issue a new check to Yasmin in her capacity as the endorsee of Rhodora, the original payee. Donald, the, drawer shall be discharged from liability only if the delay caused prejudice (Art 1249 of the Civil Code).

A stale check is a check—

- a. That cannot anymore be paid although the underlying obligation still exists;
- b. That cannot anymore be paid and the underlying obligation under the check is also extinguished;
- c. That can still be negotiated or indorsed so that whoever is the holder can claim payment therefrom;
- d. Which has not been presented for payment within a period of 30 days.

Answer:

a. That cannot anymore be paid although the underlying obligation still exists (BAR 2012)

Paul George Pua (Pua) filed a complaint for a sum of money against the spouses Benito and Caroline James (Spouses James). In the complaint, Pua prayed that the defendants pay Pua the amount of P8.5 M covered by a check. Pua asserts that defendants owed him a sum of money way back in 1988 for which the Spouses James gave him several checks. The checks, however, had all been dishonored and Pua has not been paid the amount of the loan plus the agreed interest. In 1996, the Spouses James approached Pua to get the computation of their liability including the 2% compounded interest. After bargaining to lower the amount of their liability, the Spouses James gave Pua a postdated check bearing the discounted amount of P8.5 M. Like the 1988 checks, the drawee bank likewise dishonored this check. To prove his allegations, Pua submitted the original copies of the 17 checks issued by Caroline in 1988 and the check issued in 1996, Manilatrust Check No. 750. The Spouses James, on the other hand, completely denied the existence of the debt asserting that they had never approached Pua to borrow money in 1988 or in 1996. They assert, instead, that Pua is simply acting at the instance of his sister, Lilian, to file a false charge against them using a check left to fund a gambling business previously operated by Lilian and Caroline, Decide,

Answer:

The 17 original checks, completed and delivered to Pua, are sufficient by themselves to prove the existence of the loan obligation of Spouses James to Pua. In Pacheco v. Court of Appeals, the Court has expressly recognized that a check "constitutes an evidence of indebtedness" and is a veritable "proof of an obligation." Hence, it can be used "in lieu of and for the same purpose as a promissory note." In fact, in the seminal case of Lozano v. Martinez, the Court pointed out that a check functions more than a promissory note since it not only contains an undertaking to pay an amount of money but is an "order addressed to a bank and partakes of a representation that the drawer has funds on deposit against which the check is drawn, sufficient to ensure payment upon its presentation to the bank." The Court reiterated this rule in Lim v. Mindanao Wines and Liquour Galleria stating that "a check, the entries of which are in writing, could prove a loan transaction." This is the very same principle underpin Section 24 of the NIL which provides that "every negotiable instrument is deemed prima facie to have been issued for a valuable consideration; and every person whose signature appears thereon to have become a party for value." Consequently, the case should be decided in favor of Pua and against Spouses James. (BAR 2014)

A criminal complaint for violation of BP22 was filed by Foton Motors (Foton), an entity engaged in the business of car dealership, against Pura Felipe (Pura) with the office of the City Prosecutor of Quezon City. The office found probable cause to indict Pura and filed an information before the MeTC of Quezon City, for her issuance of a postdated check in the amount of P1,020,000.00 which was subsequently dishonored upon presentment due to "Stop Payment".

Pura issued the check because her son, Freddie, attracted by a huge discount of P220,000, purchased a Foton Blizzard 4x2 from Foton. The term of the transaction was Cash-on-Delivery and no down payment was required. The car was delivered on May 14, 1997, but Freddie failed to pay upon delivery. Despite non-payment, Freddie took possession of the vehicle.

Pura was eventually acquitted of the charge of violating BP 22 but was found civilly liable for the amount of the check plus legal interest. Pura appealed the decision as regards the civil liability, claiming that there was no privity of contract between Foton and Pura. No civil liability could be adjudged against her because of her acquittal from the criminal charge. It was Freddie who was civilly liable to Foton, Pura claimed. Pura added that she could not be an accommodation party either because she only came in after Freddie failed to pay the purchase price, or 6 months after the execution of the contract between Foton and Freddie. Her liability was limited to her act of issuing a worthless check, but by her acquittal in the criminal charge, there was no more basis for her to be held civilly liable to Foton. Pura's act of issuing the subject check did not, by itself, assume the obligation of Freddie to Foton or automatically make her a party to the contract. Is Pura liable?

Answer:

Yes. Pura is liable. The rule is that every act or omission punishable by law has its accompanying civil liability. The civil aspect of every criminal case is based on the principle that every person criminally liable is also civilly liable. If the accused however, is not found to be criminally liable, it does not necessarily mean that she will not likewise be held civilly liable because extinction of the penal action does not carry with it extinction of civil action. Although Pura was not an accommodation party, she cannot escape civil liability. In cases of violation of BP 22, a special law, the intent in issuing a check is immaterial. Pura issued the bouncing check. Thus, regardless of her intent, she remains civilly liable because the act or omission, the making and issuing of the subject check, from which her civil liability arises. (BAR 2014)

1. Definition

A check is—

- a. A bill of exchange:
- b. The same as a promissory note;
- c. Is drawn by a maker;
- d. A non-negotiable instrument

Answer:

a. A bill of exchange. (BAR 2012)

2. Kinds

a. Manager's Check

In payment for his debt in favor of X, Y gave X a Manager's Check in the amount of P100,000 dated May 30, 2012. Which phrase best completes the statement—A Manager's Check:

- a. Is a check issued by a manager of a bank for his own account;
- b. Is a check issued by a manger of a bank in the name of the bank against the bank itself for the account of the bank;
- c. Is like any ordinary check that needs to be presented for payment also;
- d. Is better than a cashier's check in terms of use and effect.

Answer:

b) Is a check issued by a manger of a bank in the name of the bank against the bank itself for the account of the bank. (BAR 2012)

b.Cross Check

- 3. Stopping Payment
- 4. Presentment for Payment
 - a. Time
 - b. Effect of Delay

IV. Insurance Code

A group of Malaysians wanted to invest in the Philippines' insurance business. After negotiations, they agreed to "FIMA Insurance Corp." with a group of Filipino businessmen. FIMA would have a P50 M paid up capital. P40 M of which would come up from the Filipino group. All corporate officers would be Filipinos and 8 out of 10-member Board of Directors would be Filipinos. Can FIMA operate an insurance business in the Philippines?

- a. No, since an insurance company must have at least P74 M paid up capital.
- b. Yes, since there is substantial compliance with our nationalization laws respecting paid-up capital and Filipino dominated Board of Directors.
- c. Yes, since FIMA's paid up capital more than meets the country's nationalization laws.
- d. No, since an insurance company should be 100% owned by Filipinos.

Answer:

a. No, since an insurance company must have at least P74 M paid up capital. (BAR 2011)

A. Concept of Insurance

In return for the 20 years of faithful service of X as a house helper to Y, the latter promised to pay P100,000 to X's heirs if he (X) dies in an accident by fire. X agreed. Is this an insurance contract?

- a. Yes, since all the elements of an insurance contract are present.
- b. Yes, since X's services may be regarded as the consideration.

- c. No, since Y actually made a conditional donation in X's favor.
- d. No, since it is in fact an innominate contract between X and Y.

c. No, since Y actually made a conditional donation in X's favor. (BAR 2011)

- **B. Elements of an Insurance Contract**
- C. Characteristics/Nature and General Principles of Insurance Contract

Absolute Timber Co. (ATC) has been engaged in the logging business in Isabela. To secure one of its shipments of logs to be transported by Andok hipping Co., ATC purchased a marine policy with an all-risk provision. Because of a strong typhoon then hitting Northern Luzon, the vessel sank and the shipment of logs was totally lost. ATC filed its claim, but the insurer denied flhe claim on several grounds, namely: (1) the vessel had not been seaworthy; 2) the vessel's crew had lacked sufficient training; (3) the improper loading of the logs on only one side of the vessel had led to the tilting of the ship to at side during the stormy voyage; and (4) the extremely bad weather had been a fortuitous event.

ATC now seeks your legal advice to know if its claim was sustainable. What is your advice? Explain your answer. (3%)

SUGGESTED ANSWER

ATC's claim is sustainable. The all risk policy that ATC procured from the insurer insures against all causes of conceivable loss or damage xcept when the loss or damage was due to fraud or intentional misconuct committed by ATC (I New World International Development v. NYS Wapan Shipping Corporation, G.R. No. 171468, August 24, 2011). The rounds of denial that the insurer invoked are not due to the fraud or tentional misconduct of the insurer. (2017 BAR)

ALTERNATIVE ANSWER

The claim of Absolute Timber Company that the extreme bad weather is a fortuitous event is not valid. The ship was not seaworthy. Its loss was not due to the perils of the sea, but perils of the ship (Manila eamship Company v. Abdulhaman, G.R. No. L-9534, September 29, 1956, 00 Phil 32). ATC's negligence also bars it from invoking the defense of force majeure. (2017 BAR)

Jason is the proud owner of a newly-built house worth P5 million. As a protection against any possible loss or damage to his house, Jason applied for a fire insurance policy thereon with Shure Insurance Corporation (Shure) on October 11, 2016 and paid the premium in cash. It took the company a week to approve Jason's application. On October 18, 2016, Shure mailed the approved policy to Jason which the latter received five (5) days later. However, Jason's house had been razed by fire which transpired a day before his receipt of the approved policy. Jason filed a written claim with Shure under the insurance policy. Shure

prays for the denial of the claim on the ground that the theory of cognition applies to contracts of insurance.

Decide Jason's claim with reasons. (2016 BAR)

SUGGESTED ANSWER

Jason's claim must be denied.

What governs insurance contract is the cognition theory whereby the insurance contract is perfected only from the time the applicant came to know of the acceptance of the offer by the insurer. In this case, the loss occurred a day prior to Jason's knowledge of the acceptance by Shure of Jason's application. There being no perfected insurance contract, Jason is not entitled to recover from Shure

ALTERNATIVE ANSWER

The insurance contract may be deemed perfected allowing Jason to recover from Shure if there is a binding note or cover receipt duly issued by Shure to Jason

An Insurance Contract is a contract of adhesion, which means that in resolving ambiguities in the provision of the insurance contract –

- a. The general rule is that, the insurance contract is to be interpreted strictly in accordance with what is written in the contract;
- b. Are to be construed liberally in favor of the insured and strictly against the insurer who drafted the insurance policy;
- c. Are to be construed strictly against the insured and liberally in favor of the insurer;
- d. If there is an ambiguity in the insurance contract, this will invalidate the contract.

Answer:

b. Are to be construed liberally in favor of the insured and strictly against the insurer who drafted the insurance policy. (BAR 2012)

An insurance contract is an aleatory contract, which means that—

- a. An insurer will pay the insured equivalent to the amount of the premium;
- b. The obligation of the insurer is to pay depending upon the happening of an uncertain event;
- c. The insured pays a fixed premium for the duration of the policy period and the amount of the premiums paid to the insurer is not necessarily the same amount as what the insured will get upon the happening of an uncertain future event;
- d. The obligation of the insurer is to pay depending upon the happening of an event that is certain to happen.

Answer:

d. The obligation of the insurer is to pay depending upon the happening of an uncertain event. (BAR 2012)

Parties to Insurance Contract

- a. Insurer
- b. Insured
- c. Beneficiary

X is the common law wife of Y. Y loves X so much that he took out a life insurance on his own life and made her the sole beneficiary. Y did this to ensure that X will be financially comfortable when he is gone. Upon the death of Y—

- a. X as sole beneficiary under the life insurance policy on the life of Y will be entitled to the proceeds of the life insurance;
- b. Despite the designation of X as the sole beneficiary, the proceeds of the life insurance will go to the estate of Y;
- c. The proceeds of the life insurance will go to the compulsory heirs of Y;
- d. The proceeds of the life insurance will be divided equally amongst X and the compulsory heirs of Y.

Answer:

b. Despite the designation of X as the sole beneficiary, the proceeds of the life insurance will go to the estate of Y; (BAR 2012)

D. Classes

- a. Marine
 - a. Coverage
 - **b.** Implied Warranties

Paolo, the owner of an ocean-going vessel, offered to transport the logs of Constantino from Manila to Nagoya. Constantino accepted the offer, not knowing that the vessel was manned by an irresponsible crew with deep-seated resentments against Paolo, their employer.

Constantino insured the cargo of logs against both perils of the sea and barratry. The logs were improperly loaded on one side, thereby causing the vessel to tilt on one side. On the way to Nagoya, the crew unbolted the sea valve of the vessel causing water to flood the ship hold. The vessel sank.

Constantino tried to collect from the insurance company which denied liability, given the unworthiness of both the vessel and its crew.

Constantino countered that he was not the owner of the vessel and he could therefore not be responsible for conditions about which he was innocent.

Is the insurance company liable?

No. the insurance company is not liable because there is an implied warranty in every marine insurance that the ship is seaworthy whoever is insuring the cargo, whether it be the shipowner or not. There was a breach of warranty, because the logs were improperly loaded and the crew was irresponsible. It is the obligation of the owner of the cargo to look for a reliable common carrier which keeps its vessel in seaworthy condition. (BAR 2010)

c. Insurable Interest

The newly restored Ford Mustang muscle car was just released from the car restoration shop to its owner, Seth, an avid sportsman. Given his passion for sailing, he needed to go to a round-the-world voyage with his crew on his brandnew 180-meter yacht. Hearing about his coming voyage, Sean, his bosom friend, asked Seth if he could borrow the car for his next roadshow. Sean, who had been in the business of holding motor shows and promotions, proposed to display the restored car of Seth in major cities of the country. Seth agreed and lent the Ford Mustang to Sean. Seth further expressly allowed Sean to use the car even for his own purposes on special occasions dining his absence from the country. Seth and Sean then went together to Bayed Agad Insurance Co. (BAIC) to get separate policies for the car in their respective names.

BAIC consults you as its lawyer on whether separate policies could be issued to Seth and Sean in respect of the same car. (2017 BAR)

(a) What is insurable interest? (2%)

SUGGESTED ANSWER

- (a) Insurable interest is that interest which a person is deemed to have in the subject matter of the insured where he has a relation or connection to it such that the person will derive pecuniary benefit or advantage from the preservation of the subject matter or will suffer pecuniary loss or damage from its destruction, termination or injury by the happening of the event insured against it (44 CJS 870).
- (b) Do Seth and Sean have separate insurable interests? Explain briefly your answer. (3%)

SUGGESTED ANSWER

(b) Seth and Sean have separate insurable interests. Seth's insurable interest is his legal and/or equitable interest over the vehicle as an owner while Sean's insurable interest is the safety of the vehicle which may become the basis of liability in case of

loss or damage to the vehicle (Malayan Insurance Co., Inc. v. Philippine First Insurance Co., G.R. No. 184300 July 11, 2012, 676 SCRA 268).

d. Perils of the Sea and Perils of the Ship

Perils of the ship, under marine insurance law, refer to loss which in the ordinary course of events results from

- a. Natural and inevitable actions of the sea.
- b. Natural and ordinary actions of the sea.
- c. Unnatural and inevitable actions of the sea.
- d. Unnatural and ordinary actions of the sea.

Answer:

a. Natural and inevitable actions of the sea. (BAR 2011)

T Shipping, Co. insured all of its vessels with R insurance, Co. The insurance policies stated that the insurer shall answer for all damages due to perils of the sea. One of the insured's ship, the MV Don Priscilla, ran aground in the Panama Canal when its engine pipes leaked and the oil seeped into the cargo compartment. The leakage was caused by the extensive mileage that the ship had accumulated.

May the insurer be made to answer for the damage to the cargo and the ship?

- a. Yes, because the insurance policy covered any or all damage arising from perils of the sea.
- b. Yes, since there appears to have been no fault on the part of the shipowner and ship captain.
- c. No, since the proximate cause of the damage was the breach of warranty of seaworthiness of the ship.
- d. No, since the proximate cause of the damage was due to ordinary usage of the ship, and thus not due to perils of the sea.

Answer:

d. No, since the proximate cause of the damage was due to ordinary usage of the ship, and thus not due to perils of the sea. (BAR 2011)

e. Concealment

X insured his life for P20 million. X, plays golf and regularly exercises everyday, hence is considered in good health. He did not know, however, that his frequent headache is really caused by his being hypertensive. In his application form for a life insurance for himself, he did not put a check to the question if he is suffering from hypertension, believing that because of his active lifestyle, being hypertensive is a remote possibility. While playing golf one day, X collapsed at

the fairway and was declared dead on arrival at the hospital. His death certificate stated that X suffered a massive heart attack.

[a] Will the beneficiary of X be entitled to the proceeds of the life insurance under the circumstances, despite the non-disclosure that he is hypertensive at the time of application?

[b] If X died in an accident instead of a heart attack, would the fact of X's failure to disclose that he is hypertensive be considered as material information? (2016 Bar)

SUGGESTED ANSWER

- (A) No, the beneficiary of X is not entitled to the proceeds of the life insurance. The hypertension of X is a material fact that should have been disclosed to the insurer. The concealment of such material fact entitles the insurer to rescind the insurance policy. Materiality of the information withheld does not depend on the state of mind of the insured. Neither does it depend on the actual or physical events which ensue. Thus, "good faith" is no defense in concealment. (Sunlife Assurance Co. of Canada v. Court of Appeals, G.R. No. 105135, June 22, 1995, 315 PHIL 270-277)
- (B) Yes, it is still a material information. It is settled that the insured cannot recover even though the material fact not disclosed is not the cause of the loss
 - f. Seaworthiness
 - g. Deviation

T, the captain of MV Don Alan, while asleep in his cabin, dreamt of an Intensity 8 earthquake along the path of his ship. On waking up, he immediately ordered the ship to return to port. True enough, the earthquake and tsunami struck 3 days later and the ship was saved. Was the deviation proper?

- a. Yes, because the deviation was made in good faith and on reasonable ground for believing that it was necessary to avoid a peril.
- b. No, because no reasonable ground for avoiding a peril existed at the time of the deviation.
- c. No, because T relied merely on his supposed gift of prophecy.
- d. Yes, because the deviation took place based on a reasonable belief of the captain.

Answer:

b. No, because no reasonable ground for avoiding a peril existed at the time of the deviation. (BAR 2011)

h. Loss and Abandonment

X Shipping Co., insured its vessel MV Don Teodoro for P100 M with ABC Insurance Co. through T, an agent of X Shipping. During a voyage, the vessel accidentally caught fire and suffered damages estimated at P80 M. T personally informed ABC Insurance that X Shipping was abandoning the ship. Later, ABC

Insurance denied X Shipping's claim for loss on the ground that a notice of abandonment through its agent was improper. Is ABC Insurance right?

- a. Yes, since X Shipping should have ratified its agent's action.
- b. No, since T, as agent of X Shipping who procured the insurance, can also give notice of abandonment for his principal.
- c. Yes, since only the agent of X Shipping relayed the fact of abandonment.
- d. No, since in the first place, the damage was more than 3/4 of the ship's value.

Answer:

b. No, since T, as agent of X Shipping who procured the insurance, can also give notice of abandonment for his principal. (BAR 2011)

A cargo ship of X Shipping Co. ran aground off the coast of Cebu during a storm and lost all its cargo amounting to P50 M. the ship itself suffered damages estimated at P80 M. the cargo owners filed a suit against X Shipping but it invoked the doctrine of limited liability since it vessel suffered an P80 M damage, more than the collective value of all lost cargo. Is X Shipping correct?

- a. Yes, since under the doctrine, the value of the lost cargo and the damage to the ship can be set-off.
- b. No, since each cargo owner has a separate and individual claim for damages.
- c. Yes, since the extent of the ship's damage was greater than that of the value of the lost cargo.
- d. No, since X Shipping neither incurred a total loss nor abandoned its ship.

Answer:

d. No, since X Shipping neither incurred a total loss nor abandoned its ship. (BAR 2011)

For a constructive total loss to exist in marine insurance, it is required that the person insured relinquish his interest in the thing insured. This relinquishment must be

- a. Actual.
- b. Constructive first and if it fails, then actual.
- c. Either actual or constructive.
- d. Constructive.

Answer:

a. Actual. (BAR 2011)

i. Barratry

What is "barratry" in marine insurance?

Answer:

Barratry is any willful misconduct on the part of the master or the crew in pursuance of some unlawful or fraudulent purpose without the consent of the owner and to the prejudice of the interest of the owner. (BAR 2010)

2. Fire

A. Extent of Liability under Open Policy

B. Alteration

On May 13, 1996, PAM, Inc. obtained a P15 M fire insurance policy from Ilocano Insurance covering its machineries and equipment effective for 1 year or until May 14, 1997. The policy expressly stated that the insured properties were located at "Sanyo Precision Phils. Building, Phase III, Lots 4 and 6, Block 15, PEZA, Rosario Cavite." Before its expiration, the policy was renewed on "as is" basis for another year until May, 13, 1998. The subject properties were later transferred to Pace Factory also in PEZA. On October 12, 1997, during the effectivity of the renewed policy, a fire broke out at the Pace Factory which totally burned the insured properties.

The policy forbade the removal of the insured properties unless sanctioned by llocano. Condition 9(c) of the policy provides that "the insurance ceases to attach as regards the property affected unless the insured, before the occurrence of any loss or damage, obtains the sanction of the company signified by endorsement upon the policy x x x (c) if the property insured is removed to any building or place other than in that which is herein stated to be insured." PAM claims that it has substantially complied with notifying llocano for the insurance coverage. Is llocano liable under the policy?

Answer:

llocano is not liable under the policy. With the transfer of the location of the subject properties, without notice and without insurer's consent, after the renewal of the policy, the insured clearly committed concealment, misrepresentation and a breach of material warranty. The Insurance Code provides that a neglect to communicate that which a party knows and ought to communicate, is called concealment. A concealment entitles the injured party to rescind a contract of insurance in case of an alteration in the use or condition of the thing insured. An alteration in the use or condition of a thing insured from that to which it is limited by the policy made without the consent of the insurer, by means within the control of the insured, and increasing the risks, entitles the insurer to rescind the contract of fire insurance. (BAR 2014)

C. Friendly fire vs. Hostile fire

3. Casualty

a. Accident vs Intentional

4. Suretyship

- a. Life
- b. Incontestability Clause

The "incontestability clause" in a Life Insurance Policy means—

- a. That life insurance proceeds cannot be claimed 2 years after the death of the insured:
- b. That 2 years after date of issuance or reinstatement of the life insurance policy, the insurer cannot anymore prove that the policy is void ab initio or rescindable by reason of fraudulent concealment or misrepresentation of the insured:
- c. That the insured can still claim from the insurance policy after 2 years even though premium is not paid;
- d. That the insured can only claim proceeds in a life insurance policy 2 years after death.

Answer:

b. That 2 years after date of issuance or reinstatement of the life insurance policy, the insurer cannot anymore prove that the policy is void ab initio or rescindable by reason of fraudulent concealment or misrepresentation of the insured. (BAR 2012)

X, in January 30, 2009, or 2 years before reaching the age of 65, insured his life for P20 M. for reason unknown to his family, he took his own life 2 days after his 65th birthday. The policy contains no excepted risk. Which statement is most accurate?

- a. The insurer will be liable;
- b. The insurer will not be liable:
- c. The state of sanity of the insured is relevant in cases of suicide in order to hold the insurer liable;
- d. The state of sanity of the insured is irrelevant in cases of suicide in order to hold the insurer liable.

Answer:

a. The insurer will be liable. (BAR 2012)

On July 3, 1993, Delia Sotero (Delia) took out a life insurance policy from Ilocos Bankers Life Insurance Corporation (Ilocos Life) designating Creencia Aban (Aban), her niece, as her beneficiary. Ilocos Life issued Policy No. 747, with a face value of P100,000, in Sotero's favor on August 30, 1993, after the requisite medical examination and payment of the premium.

On April 10, 1996, Sotero died. Aban filed a claim for the insurance proceeds on July 9, 1996. Ilocos Life conducted an investigation into the claim and came out with the following findings:

- a. Sotero did not personally apply for insurance coverage, as she was illiterate.
- b. Sotero was sickly since 1990.

- c. Sotero did not have the financial capability to pay the premium on the policy.
- d. Sotero did not sign the application for insurance.
- e. Aban was the one who filed the insurance application and designated herself as the beneficiary.

For the above reasons and claiming fraud, llocos Life denied Aban's claim on April 16, 1997, but refunded the premium paid on the policy.

A. May the incontestability period set in even in cases of fraud as alleged in this case?

B. Is Aban entitled to claim the proceeds under the policy?

Answer:

A. Yes. The "incontestability clause" is a provision in law that after a policy of life insurance made payable on the death of the insured shall have been in force during the lifetime of the insured for a period of 2 years from the date of its issue or of its last reinstatement, the insurer cannot prove that the policy is void ab initio or is rescindable by reason of fraudulent concealment or misrepresentation of the insured or his agent.

In this case, the policy was issued on August 30, 1993, and the insured died on April 10, 1996. The insurance policy was thus in force for a period of 3 years, 7 months and 24 days. Considering that the insured died after the 2-year period, llocos is, therefore, barred from proving that the policy is void ab initio by reason of the insured's fraudulent concealment or misrepresentation or want of insurable interest on the part of the beneficiary.

B. Yes, Aban is entitled to claim the proceeds. After the 2-year period lapse, or when the insured dies within the period, the insurer must make good on the policy, even though the policy was obtained by fraud, concealment, or misrepresentation, as in this case, when the insured did not personally apply for the policy as she was illiterate and that it was the beneficiary who filled up the insurance application designating herself as beneficiary. (BAR 2014)

e. Compulsory Motor Vehicle Liability Insurance

As a rule, an insurance contract is consensual and voluntary. The exception in the case of:

- a. Inland Marine Insurance
- b. Industrial Life Insurance
- c. Motor Vehicle Liability Life Insurance
- d. Life Insurance

Answer:

c. Motor Vehicle Liability Life Insurance (BAR 2014)

A. No fault indemnity clause

X is a passenger of a jeepney for hire being driven by Y. the jeepney collided with another passenger jeepney being driven by Z who was driving recklessly. As a result of the collision, X suffered injuries. Both passenger jeepneys are covered by Comprehensive Motor Vehicular Insurance Coverage. If X wants to claim under the "no fault indemnity clause", his claim will lie—

- a. Against the insurer of the jeepney being driven by Z who was the one at fault;
- b. The claim shall lie against the insurer of the passenger jeepeney driven by Y because X was his passenger;
- c. X has a choice against whom he wants to make his claim;
- d. None of the above.

Answer:

b. The claim shall lie against the insurer of the passenger jeepeney driven by Y because X was his passenger. (BAR 2012)

- B. Other Rules Concerning Motor Vehicles
- 1. Authorized Driver Clause
- 2. Theft Clause

On May 26, 201, Jess insured with Jack Insurance (Jack) his 2014 Toyota Corolla sedan under a comprehensive motor vehicle insurance policy for one year. On July 1, 2014, Jess' car was unlawfully taken. Hence, he immediately reported the theft to the Traffic management Command (TMC) of the Philippine National Police (PNP), which made Jess accomplish a complaint sheet as part of its procedure. In the complaint sheet, Jess alleged that a certain Ric Silat (Silat) took possession of the subject vehicle to add accessories and improvements thereon. However, Silat failed to return the subject vehicle within the agreed 3-day period. As a result, Jess notified Jack of his claim for reimbursement of the value of the vehicle under the insurance policy.

Jack refused to pay claiming that there is no theft as Jess gave Silat lawful possession of the car. Is Jack correct?

Answer:

No. Jack is not correct. The "theft clause" of a comprehensive motor vehicle insurance policy has been interpreted by the Court in several cases to cover situations like (1) when one takes the motor vehicle of another without the latter's consent even if the motor vehicle is later returned, there is theft—there being intent to gain as the use of the thing unlawfully taken constitutes gain, or (2) when there is taking of a vehicle by another person without the permission or authority from the owner thereof. (BAR 2014)

On February 21, 2013, Barrack entered into a contract of insurance with Matino Insurance Company (Matino) involving a motor vehicle. The policy obligates Matino to pay Barrack the amount of P600,000 in case of loss or damage to said vehicle during the period covered, which is from February 26, 2013 to February 26, 2014.

On April 16, 2013, at about 9:00am, Barrack instructed his driver, JJ, to bring the motor vehicle to a nearby auto shop for tune-up. However, JJ no longer returned and despite diligent efforts to locate the said vehicle, the efforts proved futile. Resultantly, Barrack promptly notified Matino of the said loss and demanded payment of the insurance proceeds of P600,000.

In a letter dated July 5, 2013. Matino denied the claim, reasoning as stated in the contract that "the company shall not be liable for any malicious damage caused by the insured, any member of his family or by a person in the insured's service. Is Matino correct in denying the claim?

Answer:

No. Matino is not correct in denying the claim. An insurance company cannot deny a claim by the owner of a motor vehicle who insured it against loss or damage because the driver he employed stole it. Matino cannot invoke the provision excluding malicious damages caused by a person in the service of the insured. In common ordinary usage, loss means failure to keep possession, while malicious damage is damage resulting from the willful act of the driver. Words which have different meanings shall be understood in the sense which is most in keeping with the nature and object of the insurance contract. If a stipulation admits several meanings, is should be understood as bearing the meaning which is most adequate to render it effectual. It may be shown that the words have a local, technical or peculiar meaning and were so used and understood by the parties. (BAR 2014)

E. Insurable Interest

1. In Life/Health

X, Co. a partnership, is composed of A (capitalist partner), B (capitalist partner) and C (industrial partner). If you were partner A, who between B and C would you have an insurable interest on, such that you may then insure him?

- a. No one, as there is merely a partnership contract among A, B and C.
- b. Both B and C, as they are your partners.
- c. Only C, as he is an industrial partner.
- d. Only B, as he is a capitalist partner.

Answer:

b. Both B and C, as they are your partners. (BAR 2011)

X has been a long-time household helper of Z. X's husband, Y, has also been Z's long-time driver. May Z insure the lives of both X and Y with Z as beneficiary?

- a. Yes, since X and Y render services to Z.
- b. No, since X and Y have no pecuniary interest on the life of Z arising from their employment with him.
- c. No, since Z has no pecuniary interest in the lives of X and Y arising from their employment with him. d. Yes, since X and Y are Z's employees.
- d. Yes, since X and Y are Z's employees.

Answer:

c. No, since Z has no pecuniary interest in the lives of X and Y arising from their employment with him. (BAR 2011)

For both the Life Insurance and Property Insurance, the insurable interest is required to be—

- a. Existing at the time of perfection of the contract and at the time of loss;
- b. Existing at the time of perfection and at the time of loss for property;
- c. Existing at the time of perfection for property insurance but for life insurance both at the time of perfection and at the time of loss;
- d. Existing at the time of perfection only.

Answer:

b. Existing at the time of perfection and at the time of loss for property. (BAR 2012)

X, a minor, contracted an insurance on his own life. Which statement is most accurate?

- a. The life insurance policy is void ab initio;
- b. The life insurance is valid provided it is with the consent of the beneficiary;
- c. The life insurance policy is valid provided the beneficiary is his estate or his parents, or spouse or child;
- d. The life insurance is valid provided the disposition of the proceeds will be subject to the approval of the legal guardian of the minor.

Answer:

c. The life insurance policy is valid provided the beneficiary is his estate or his parents, or spouse or child. (BAR 2012)

In 2010, the PNP declared Kaddafy Benjelani "Public Enemy No. 1" because of his terrorist activities in the country that have resulted in the death of thousands of Filipinos. A ransom of P15 M was placed on Kaddafy Benjelani's head.

Worried about the future of their family, Kaddafy Benjelani's estranged wife, Aurelia, secured in December 2010 a life insurance policy on his life and designated herself as beneficiary.

Is the policy valid and binding?

- a. Yes, the policy is valid and binding because Aurelia has an insurable interest on the life of Kaddafy Benjelani.
- b. No, the policy is not valid and binding because Kaddafy Benjelani has been officially declared a public enemy;
- c. Yes, the policy is valid and binding because it has been in force for more than 2 years;
- d. No, the policy is not valid and binding since the spouses' estrangement removed Aurelia's insurable interest in Benjalani's life;
- e. None of the above.

a. Yes, the policy is valid and binding because Aurelia has an insurable interest on the life of Kaddafy Benjelani. (BAR 2013)

Carlo and Bianca met in the La Boracay festivities. Immediately, they fell in love with each other and got married soon after. They have been cohabiting blissfully as husband and wife, but they did not have any offspring. As the years passed by, Carlo decided to take out an insurance on Bianca's life for P1 M with him (Carlo) as sole beneficiary, given that he did not have a steady source of income and he always depended on Bianca both emotionally and financially. During the term of the insurance, Bianca died of what appeared to be a mysterious cause so that Carlo immediately requested for an autopsy to be conducted. It was established that Bianca died of a natural cause. More than that, it was also established that Bianca was a transgender all along—a fact unknown to Carlo. Can Carlo claim the insurance benefit?

Answer:

Yes. Carlo can claim the insurance benefit. If a person insures the life or health of another person with himself as beneficiary, all his rights, title and interests in the policy shall automatically vest in the person insured. Carlo, as the husband of Bianca, has an insurable interest in the life of the latter. Also, every person has an insurable interest in the life and health of any person on whom he depends wholly or in part for support. The insurable interest in the life of the person insured must exist when the insurance takes effect but need not exist when the loss occurs. Thus, the subsequent knowledge of Carlo, upon the death of Bianca, that the latter is a transgender does not destroy his insurable interest on the life of the insured. (BAR 2014)

A person is said to have an insurable interest in the subject matter insured where he has a relation or connection with, or concern in it that he will derive pecuniary benefit or advantage from its preservation. Which among the following subject matters is not considered insurable?

- a. A partner in a firm on its future profits.
- b. A general creditor on the debtor's property
- c. A judgment creditor on debtor's property
- d. A mortgage creditor on debtor's mortgaged property.

a. A partner in a firm on its future profits. (BAR 2014)

On July 3, 1993, Delia Sotero (Delia) took out a life insurance policy from Ilocos Bankers Life Insurance Corporation (Ilocos Life) designating Creencia Aban (Aban), her niece, as her beneficiary. Ilocos Life issued Policy No. 747, with a face value of P100,000, in Sotero's favor on August 30, 1993, after the requisite medical examination and payment of the premium.

On April 10, 1996, Sotero died. Aban filed a claim for the insurance proceeds on July 9, 1996. Ilocos Life conducted an investigation into the claim and came out with the following findings:

- A. Sotero did not personally apply for insurance coverage, as she was illiterate.
- B. Sotero was sickly since 1990.
- C. Sotero did not have the financial capability to pay the premium on the policy.
- D. Sotero did not sign the application for insurance.
- E. Aban was the one who filed the insurance application and designated herself as the beneficiary.

For the above reasons and claiming fraud, llocos Life denied Aban's claim on April 16, 1997, but refunded the premium paid on the policy.

May Sotero validly designate her niece as beneficiary?

Answer:

Yes. Sotero may validly designate her niece, Aban, as beneficiary. Sotero had insurable interest in her own life, and could validly designate anyone as her beneficiary. (BAR 2014)

2. In Property

Novette entered into a contract for the purchase of certain office supplies. The goods were shipped. While in transit, the goods were insured by Novette. Does she have an insurable interest over the goods even before delivery of the same to her? Explain. (2015)

Answer:

Yes, Novette has an insurable interest in the goods. The contract of sale was already perfected and Novette acquired interest thereon although the goods have yet to be delivered.

Ciriaco leased a commercial apartment from Supreme Building Corporation (SBC). One of the provisions of the 1-year lease contract states:

"18. x x x The LESSEE shall not insure against fire the chattels, merchandise, textiles, goods and effects placed at any stall or store or space in the leased premises without first obtaining the written consent of the LESSOR. If the LESSEE obtains five insurance coverage without the consent of the LESSOR, the insurance policy is deemed assigned and transferred to the LESSRO for the latter's benefit."

Notwithstanding the stipulation in the contract, without the consent of SBC, Ciriaco insured the merchandise inside the premises against loss by fire in the amount of P500,000 with First United Insurance Corporation (FUIC).

A day before the lease contract expired, fire broke out inside the leased premises, damaging Ciriaco's merchandise. Having learned of the insurance earlier procured by Ciriaco, SBC demanded from FUIC that the proceeds of the insurance policy be paid directly to it, as provided in the lease contract.

Who is legally entitled to receive the insurance proceeds? Explain.

Answer:

Ciriaco is entitled to receive the proceeds of the insurance policy. The stipulation that the policy is deemed assigned and transferred to SBC is void, because SBC has no insurable interest in the merchandise of Ciriaco. (BAR 2009)

X owned a house and lot. X insured the house. The house got burned. Then he sold the partially burnt house and the lot to Y. Which statement is most accurate?

- a. X is not anymore entitled to the proceeds of the insurance policy because he already sold the partially burnt house and lot;
- b. X is still entitled to the proceeds of the insurance policy because what is material is that at the time of the loss, X is the owner of the house and lot;
- c. No one is entitled to the proceeds because ownership over the house and lot was already transferred;
- d. Y will be the one entitled to the proceeds because he now owns the partially burnt house and lot.

Answer:

b. X is still entitled to the proceeds of the insurance policy because what is material is that at the time of the loss, X is the owner of the house and lot. (BAR 2012)

For both the Life Insurance and Property Insurance, the insurable interest is required to be—

- a. Existing at the time of perfection of the contract and at the time of loss;
- b. Existing at the time of perfection and at the time of loss for property;
- c. Existing at the time of perfection for property insurance but for life insurance both at the time of perfection and at the time of loss;
- d. Existing at the time of perfection only.

- b. Existing at the time of perfection and at the time of loss for property. (BAR 2012)
- 3. Double Insurance, Over Insurance, Co-Insurance and Re-Insurance TRUE or FALSE EXPLAIN BRIEFLY YOUR ANSWER.
- (e) The law on life insurance prohibits double insurance. (2%) (2017 BAR)

SUGGESTED ANSWER

(e) False. Double insurance only applies to property insurance.

If an insurance policy prohibits additional insurance on the property insured without the insurer's consent, such provision being valid and reasonable, a violation by the insured

- a. Reduces the value of the policy.
- b. Avoids the policy.
- c. Offsets the value of the policy with the additional insurance's value.
- d. Forfeits premiums already paid.

Answer:

b. Avoids the policy. (BAR 2011)

X borrowed from CCC Bank. She mortgaged her house and lot in favor of the bank. X insured her house. The bank also got the house insured.

- A. Is this double insurance? Explain your answer.
- B. Is this legally valid? Explain your answer.
- C. In case of damage, can X and CCC bank separately claim for the insurance proceeds?

Answer:

- A. No, there is no double insurance. Double insurance exists where the same person is insured by several insurers separately with respect to the same subject and interest.
- B. Yes, X and CCC Bank can both insure the house as they have different insurable interests therein. X, the borrower-mortgagor, has an insurable interest in the house being the owner thereof while CCC Bank, the lender, also has an insurable interest in the house as mortgagee thereof.
- C. Yes. If X obtained an open policy then she could claim an amount corresponding to the extent of the damage based on the value of the house determined as of the date the damaged occurred, but not to exceed the face value of the insurance policy; however, if she obtained a valued policy then she could claim an amount corresponding to the extent of the damage based on the agreed upon valuation of the house.

As for CCC Bank, it could claim an amount corresponding to the extent of the damage but not to exceed the amount of the loan it extended to X or so much thereof as may remain unpaid. (BAR 2012)

X insured the building she owns with 2 insurance companies for the same amount. In case of damage—

- a. X cannot claim from any of the 2 insurers because with the double insurance, the insurance coverage becomes automatically void;
- b. The 2 insurers will be solidarily liable to the extent of the loss;
- c. The 2 insurers will be proportionately liable;
- d. X can choose who he wants to claim against.

Answer:

d. X can choose who he wants to claim against. (BAR 2012)

4. Multiple or Several Interests on Same Property

To secure a loan of P10 M, Mario mortgaged his building to Armando. In accordance with the loan arrangements, Mario had the building insured with First Insurance Company for P10 M, designating Armando as the beneficiary.

Armando also took an insurance on the building upon his own interest with Second Insurance Company for P5 M.

The building was totally destroyed by fire, a peril insured against under both insurance policies. It was subsequently determined that the fire had been intentionally started by Mario and that in violation of the loan agreement, he had been storing inflammable materials in the building.

How much, if any, can Armando recover from either or both insurance companies?

Answer:

Armando can receive P5 M from Second Insurance Company. As mortgagee, he had an insurable interest in the building. Armando cannot collect anything from First Insurance Company. First Insurance Company is not liable for the loss of the building. First, it was due to a willful act of Mario, who committed arson. Second, fire insurance policies contain a warranty that the insured will not store hazardous materials within the insured's premises. Mario breached this warranty when he stored inflammable materials in the building. These two factors exonerate First Insurance Company from liability to Armando as mortgagee even though it was Mario who committed them.

What happens to the P10 M debt of Mario to Armando? Explain.

Answer:

Since Armando would have collected P5 M from Second Insurance Company, this amount should be considered as partial payment of the loan. Armando can only collect the balance of P5 M. Second Insurance Company can recover from Mario the amount of P5 M it paid, because it became subrogated to the rights of Armando. (BAR 2010)

X borrowed from CCC Bank. She mortgaged her house and lot in favor of the bank. X insured her house. The bank also got the house insured.

- A. Is this double insurance? Explain your answer.
- B. Is this legally valid? Explain your answer.
- C. In case of damage, can X and CCC bank separately claim for the insurance proceeds?

Answer:

A. No, there is no double insurance. Double insurance exists where the same person is insured by several insurers separately with respect to the same subject and interest.

B. Yes, X and CCC Bank can both insure the house as they have different insurable interests therein. X, the borrower-mortgagor, has an insurable interest in the house being the owner thereof while CCC Bank, the lender, also has an insurable interest in the house as mortgagee thereof.

C. Yes. If X obtained an open policy then she could claim an amount corresponding to the extent of the damage based on the value of the house determined as of the date the damaged occurred, but not to exceed the face value of the insurance policy; however, if she obtained a valued policy then she could claim an amount corresponding to the extent of the damage based on the agreed upon valuation of the house.

As for CCC Bank, it could claim an amount corresponding to the extent of the damage but not to exceed the amount of the loan it extended to X or so much thereof as may remain unpaid. (BAR 2012)

A house and lot is covered by a real estate mortgage (REM) in favor of ZZZ Bank. The Bank required that the house be insured. The owner of the policy failed to endorse nor assign the policy to the bank. However, the Deed of REM has an express provision which says that the insurance policy is also endorsed with the signing of the REM. Will this be sufficient?

- a. No, insurance policy must be expressly endorsed to the bank so that the bank will have a right in the proceeds of such insurance in the event of loss;
- b. The express provision contained in the Deed of REM to the effect that the policy is also endorsed is sufficient;
- c. Endorsement of the Insurance Policy in any form is not legally allowed;
- d. Endorsement of the Insurance Policy must be in a formal document to be valid.

a. No, insurance policy must be expressly endorsed to the bank so that the bank will have a right in the proceeds of such insurance in the event of loss (BAR 2012)

F. Perfection of the Contract of Insurance

Antarctica Life Assurance Corporation (ALAC) publicly offered a specially designed insurance policy covering persons between the ages of 50 to 75 who may be afflicted with serious and debilitating illnesses. Quirco applied for insurance coverage, stating that he was already 80 years old. Nonetheless, ALAC approved his application.

Quirco then requested ALAC for the issuance of a cover note while he was trying to raise funds to pay the insurance premium. ALAC granted the request. 10 days after he received the cover note, Quirco had a heart seizure and had to be hospitalized. He then filed a claim on the policy.

Can ALAC validly deny the claim on the ground that the insurance coverage, as publicly offered was available only to persons 50 to 75 years of age? Why or why not?

Answer:

No. by approving the application of Quirino who disclosed that he was already 80 years old, ALAC waived the age requirement. ALAC is now stopped from raising such defense of age of the insured.

Did ALAC's issuance of a cover note result in the perfection of an insurance contract between Quirco and ALAC? Explain.

Answer:

Yes. The issuance of a cover note resulted in the perfection of the contract of insurance. In that case, it is only because there is delay in the issuance of the policy that the cover note was issued.

The cover note is a receipt whereby the company agrees to insure the insured for 60 days pending the issuance of a regular policy. No separate premium is to be paid on a cover note. It is not a separate policy but is integrated in the regular policy to be subsequently issued. (BAR 2009) Armando, a resident of Manila, borrowed P3 M from Bernardo, offering as security his 500 shares of stock worth P1.5 M in Xerxes Corporation, and his 2007 BMW sedan, valued at P2 M. the mortgage on the shares of stock was registered in the Office of the Register of Deeds of Makati City where Xerxes Corporation has its principal office. The mortgage on the car was registered in the Office of the Register of Deeds of Manila. Armando executed a single Affidavit of Good Faith, covering both mortgages.

Armando defaulted on the payment of his obligation; thus, Bernardo foreclosed on the two chattel mortgages. Armando filed suit to nullify the foreclosure and the mortgages, raising the following issues:

The execution of only one Affidavit of Good Faith for both mortgages invalidated the two mortgages; and

The mortgage on the shares of stocks should have been registered in the Office of the Register Deeds of Manila where he resides, as well as in the stock and transfer book of Xerxes Corporation.

Rule on the foregoing issues with reasons.

Answer:

The execution of only one Affidavit of Good Faith for both mortgages is not a ground to nullify the said mortgages and the foreclosure thereof. Said mortgages are valid as between immediate parties, although they cannot bind third parties.

The mortgage on the shares of stock should be registered in the chattel mortgage registry in the register of Deeds of Makati City where the corporation has its principal office and also in the Register of Deeds of Manila where the mortgagor resides. Registration of chattel mortgage in the stock and transfer book is not required to make the chattel mortgage valid. Registration of dealings in the stock and transfer book under Section 63 of the Corporation Code applies only to sale or disposition of shares, and has no application to mortgages and other forms of encumbrances.

Assume that Bernardo extrajudicially foreclosed on the mortgages, and both the car and the shared of stock were sold at public auction. If the proceeds from such public sale should be 1-million short of Armando's total obligation, can Bernardo recover the deficiency? Why or why not?

Answer:

Yes. Bernardo can recover the deficiency. Chattels are given as mere security, and not as payment or pledge.

1. Offer and Acceptance/Consensual

On June 1, 2011, X mailed to Y Insurance, Co. his application for life insurance, with payment for 5 years of premium enclosed in it. On July 21, 2011, the insurance company accepted the application and mailed, on the same day, its acceptance plus the cover note. It reached X's residence on August 11, 2011. But, as it happened, on August 4, 2011, X figured in a car accident. He died a day later. May X's heir recover on the insurance policy?

a. Yes, since under the Cognition Theory, the insurance contract was perfected upon acceptance by the insurer of X's application.

- b. No, since there is no privity of contract between the insurer and X's heirs.
- c. No, since X had no knowledge of the insurer's acceptance of his application before he died.
- d. Yes, since under the Manifestation Theory, the insurance contract was perfected upon acceptance of the insurer of X's application.

c. No, since X had no knowledge of the insurer's acceptance of his application before he died. (BAR 2011)

- A. Delay in Acceptance
- **B.** Delivery of Policy

On September 25, 2013, Danny Marcial (Danny) procured an insurance on his life with a face value of P5 M from RN Insurance Company (RN), with his wife Tina Marcial (Tina) as sole beneficiary. On the same day, Danny issued an undated check to RN for the full amount of the premium. On October 1, 2013, RN issued the policy covering Danny's life insurance. On October 5, 2013, Danny met a tragic accident and died. Tina claimed the insurance benefit, but RN was quick to deny the claim because at the time of Danny's death, the check was not yet encashed and therefore the premium remained unpaid.

Is RN correct? Will your answer be the same if the check is dated October 15, 2013?

Answer:

No. RN is not correct. After the issuance of the check by Danny for the full amount of the premium, the unconditional delivery of an insurance policy of RN to Danny corresponding to the terms of the application ordinarily consummates the contract, and the policy as delivered becomes the final contract between the parties. Where the parties, so intend, the insurance becomes effective at the time of the delivery of the policy notwithstanding the fact that the check was not yet encashed. My answer will still be the same even if the check is dated October 15, 2013 since an acknowledgment in a policy of the receipt of premium is conclusive evidence of its payment for the purpose of making the policy binding. (BAR 2014)

C. Transfer of Policy

d. Kinds of Policy

2. Premium Payment

Will an insurance policy be binding even if the premium is unpaid? What if it were partially paid? (2015)

Answer:

As a general rule, the insurance policy is not valid and binding unless the premium thereof has been paid. This is the cash and carry rule under the Insurance Code. Premium is the consideration for the undertaking of the insurer to indemnify the insured against a specified peril. There are exceptions, however, one of them is when there is an agreement allowing the insured to pay the premium in installments and partial payment has been made at the time of the loss (Makati Tuscany Condominium Corporation v. CA, 215 SCRA 463).

Enrique obtained from Seguro Insurance Company a comprehensive motor vehicle insurance to cover his top of the line Aston Martin. The policy was issued on March 31, 2010 and, on even date, Enrique paid the premium with a personal check postdated April 6, 2010.

On April 5, 2010, the car was involved in an accident that resulted in its total loss.

On April 10, 2010, the drawee bank returned Enrique's check with the notation "Insufficient Funds." Upon notification, Enrique immediately deposited additional funds with the bank and asked the insurer to redeposit the check.

Enrique thereupon claimed indemnity from the insurer. Is the insurer liable under the insurance coverage? Why or why not?

Answer:

The insurer is not liable under the insurance policy. Under Art 1249 of the Civil Code, the delivery of a check produces the effect of payment only when it is encashed. The loss occurred on April 5, 2010. When the check was deposited, it was returned on April 10, 2010, for insufficiency of funds. The check was honored only after Enrique deposited additional funds with the bank. Hence, it did not produce the effect of payment. (BAR 2010)

Stable Insurance Co. (SIC) and St. Peter Manufacturing Co. (SPMC) have had a long-standing insurance relationship with each other; SPMC secured the comprehensive fire insurance on its plant and facilities from SIC. The standing business practice between them has been to allow SPMC a credit period of 90 days from the renewal of the policy within which to pay the premium.

Soon after the new policy was issued and before premium payments could be made, a fire gutted the covered plant and facilities to the ground. The day after the fire, SPMC issued a manager's check to SIC for the fire insurance premium, for which it was issued a receipt; a week later SPMC issued its notice of loss.

SIC responded by issuing its own manager's check for the amount of the premiums SPMC had paid, and denied SPMC's claim on the ground that under the

"cash and carry" principle governing fire insurance, no coverage existed at the time the fire occurred because the insurance premium had not been paid.

Is SPMC entitled to recover for the loss from SIC?

Answer:

SPMC is entitled to recover for the loss from SIC. SIC granted a credit term to pay the premiums. This is not against the law, because the standing business practice of allowing SPMC to pay the premiums after 60 or 90 days, was relied upon in good faith by SPMC. SIC is in estoppel. (BAR 2013)

- 3. Non-Default Options in Life Insurance
- 4. Reinstatement of a Lapsed Policy of Life Insurance
- 5. Refund of Premiums

G. Rescission of Insurance Contracts

Shipowner X, in applying for a marine insurance policy from ABC, Co., stated that his vessel usually sails middle of August and with normally 100 tons of cargo. It turned out later that the vessel departed on the first week of September and with only 10 tons of cargo. Will this avoid the policy that was issued?

- A. Yes, because there was breach of implied warranty.
- B. No, because there was no intent to breach an implied warranty.
- C. Yes, because it relates to a material representation.
- D. No, because there was only representation of intention.

Answer:

d. No, because there was only representation of intention. (BAR 2011)

When X insured his building, X indicated in the application that it is a residential building, but actually the building was being used as a warehouse for some hazardous materials. What is the effect on the insurance policy, if any?

- a. The insurance policy can be cancelled because of the change in the use;
- b. The insurance policy will automatically be changed;
- c. The insurance policy need not be changed;
- d. The insurance policy is fixed regardless of the changes in the use.

Answer:

Any of the above should be given full credit. (BAR 2012)

1. Concealment

X, in the hospital for kidney dysfunction, was about to be discharged when he met his friend Y. X told Y the reason for his hospitalization. A month later, X applied for an insurance covering serious illness from ABC Insurance, Co., where Y was working as Corporate Secretary. Since X had already told Y about his

hospitalization, he no longer answered a question regarding it in the application form. Would this constitute concealment?

- a. Yes, since the previous hospitalization would influence the insurer in deciding whether to grant X's application.
- b. No, since Y may be regarded as ABC's agent and he already knew of X's previous hospitalization.
- c. Yes, it would constitute concealment that amounts to misrepresentation on X's part.
- d. No, since the previous illness is not a material fact to the insurance coverage.

Answer:

a. Yes, since the previous hospitalization would influence the insurer in deciding whether to grant X's application. (BAR 2011)

An insured, who gains knowledge of a material fact already after the effectivity of the insurance policy, is not obliged to divulge it. The reason for this is that the test of concealment of material fact is determined.

- a. At the time of the issuance of the policy.
- b. At any time before the payment of premium.
- c. At the time of the payment of the premium.
- d. At any time before the policy becomes effective.

Answer:

d. any time before the policy becomes effective. (BAR 2011)

Benny applied for life insurance for P1.5 M. the insurance company approved his application and issued an insurance policy effective Nov. 6, 2008. Benny named his children as his beneficiaries. On April 6, 2010, Benny died of hapatoma, a liver ailment.

The insurance company denied the children's claim for the proceeds of the insurance policy on the ground that Benny failed to disclose in his application 2 previous consultations with his doctors for diabetes and hypertension, and that he had been diagnosed to be suffering from hepatoma. The insurance company also rescinded the policy and refunded the premiums paid.

Was the insurance company correct?

Answer:

The insurance company correctly rescinded the policy because of concealment. Benny did not disclose that he was suffering from diabetes, hypertension, and hepatoma. The concealment is material because these are serious ailments. Benny died less than 2 years from the date of the issuance of the policy. (BAR 2013)

On May 13, 1996, PAM, Inc. obtained a P15 M fire insurance policy from Ilocano Insurance covering its machineries and equipment effective for 1 year or until May 14, 1997. The policy expressly stated that the insured properties were located at "Sanyo Precision Phils. Building, Phase III, Lots 4 and 6, Block 15, PEZA, Rosario Cavite." Before its expiration, the policy was renewed on "as is" basis for another year until May, 13, 1998. The subject properties were later transferred to Pace Factory also in PEZA. On October 12, 1997, during the effectivity of the renewed policy, a fire broke out at the Pace Factory which totally burned the insured properties.

The policy forbade the removal of the insured properties unless sanctioned by llocano. Condition 9(c) of the policy provides that "the insurance ceases to attach as regards the property affected unless the insured, before the occurrence of any loss or damage, obtains the sanction of the company signified by endorsement upon the policy $x \times x \times (c)$ if the property insured is removed to any building or place other than in that which is herein stated to be insured." PAM claims that it has substantially complied with notifying llocano for the insurance coverage. Is llocano liable under the policy?

Answer:

llocano is not liable under the policy. With the transfer of the location of the subject properties, without notice and without insurer's consent, after the renewal of the policy, the insured clearly committed concealment, misrepresentation and a breach of material warranty. The Insurance Code provides that a neglect to communicate that which a party knows and ought to communicate, is called concealment. A concealment entitles the injured party to rescind a contract of insurance in case of an alteration in the use or condition of the thing insured. An alteration in the use or condition of a thing insured from that to which it is limited by the policy made without the consent of the insurer, by means within the control of the insured, and increasing the risks, entitles the insurer to rescind the contract of fire insurance. (BAR 2014)

2. Misrepresentation/Omissions

3. Breach of Warranties

Julie and Alma formed a business partnership. Under the business name Pino Shop, the partnership engaged in a sale of construction materials. Julie insured the stocks in trade of Pino Shop with WGC Insurance Company for P350,000. Subsequently, she again got an insurance contract with RSI for P1 M and then from EIC for P200,000. A fire of unknown origin gutted the store of the partnership. Julie filed her claims with the 3 insurance companies. However, her claims were denied separately for breach of policy condition which required the insured to give notice of any insurance effected covering the stocks in trade. Julie went to court and contended that she should not be blamed for the omission, alleging that the insurance agents for WGC, RSI and EIC knew of the existence of the additional insurance coverage and that she was not informed

about the requirement that such other or additional insurance should be stated in the policy.

May she recover on her fire insurance policies? Explain.

Answer:

No, because she is guilty of violation of a warranty/ condition. (BAR 1992)

To secure a loan of P10 M, Mario mortgaged his building to Armando. In accordance with the loan arrangements, Mario had the building insured with First Insurance Company for P10 M, designating Armando as the beneficiary.

Armando also took an insurance on the building upon his own interest with Second Insurance Company for P5 M.

The building was totally destroyed by fire, a peril insured against under both insurance policies. It was subsequently determined that the fire had been intentionally started by Mario and that in violation of the loan agreement, he had been storing inflammable materials in the building.

How much, if any, can Armando recover from either or both insurance companies?

Answer:

Armando can receive P5 M from Second Insurance Company. As mortgagee, he had an insurable interest in the building. Armando cannot collect anything from First Insurance Company. First Insurance Company is not liable for the loss of the building. First, it was due to a willful act of Mario, who committed arson. Second, fire insurance policies contain a warranty that the insured will not store hazardous materials within the insured's premises. Mario breached this warranty when he stored inflammable materials in the building. These two factors exonerate First Insurance Company from liability to Armando as mortgagee even though it was Mario who committed them. (BAR 2010)

H. Claims Settlement and Subrogation

- a. Notice and Proof of Loss
- b. Guidelines on Claims Settlement
 - a. Unfair Claims Settlement; Sanctions
 - b. Prescription of Action
 - c. Subrogation

Where the insurer was made to pay the insured for a loss covered by the insurance contract, such insurer can run after the third person who caused the loss through subrogation. What is the basis for conferring the right of subrogation to the insurer?

a. Their express stipulation in the contract of insurance.

- b. The equitable assignment that results from the insurer's payment of the insured.
- c. The insured's formal assignment of his right to indemnification to the insurer.
- d. The insured's endorsement of its claim to the insurer.

b. The equitable assignment that results from the insurer's payment of the insured. (BAR 2011)

ELP Insurance, Inc. issued a Marine Policy No. 888 in favor of FCL Corp. to insure the shipment of 132 bundles of electric copper cathodes against all risks. Subsequently, the cargoes were shipped on board the vessel "M/V Menchu" from Leyte to Pier 10, North Harbor, Manila.

Upon arrival, FCL Corp. engaged the services of CGM, Inc. for the release and withdrawal of the cargoes from the pier and the subsequent delivery to its warehouses/plants in Valenzuela City. The goods were loaded on board 12 trucks owned by CGM, Inc., driven by its employed drivers and accompanied by its employed truck helpers. Of the 12 trucks en route to Valenzuela City, only 11 reached the destination. One truck, loaded with 11 bundles of copper cathodes, failed to deliver its cargo.

Because of this incident, FCL Corp. filed with ELP Insurance, Inc. a claim for insurance indemnity in the amount of P1.5 M. After the requisite investigation and adjustment, ELP Insurance, Inc. paid FCL Corp. the amount of P1,350,000.00 as insurance indemnity.

ELP Insurance, Inc., thereafter, filed a complaint for damages against CGM, Inc. before the RTC, seeking reimbursement of the amount it had paid to FCL Corp. for the loss of the subject cargo. CGM, Inc. denied the claim on the basis that it is not privy to the contract entered into by and between FCL Corp. and ELP Insurance, Inc., and hence, it is not liable therefor. If you are the judge, how will you decide the case?

Answer:

CGM, Inc. should be held liable for damages against ELP Insurance, Inc. The insurer, upon happening of the risk insured against and after payment to the insured is subrogated to the rights and cause of action of the latter. As such, the insurer has the right to seek reimbursement for all the expenses paid. (BAR 2014)

V. Transportation Laws

A. Common Carrier vs. Private Carrier

1. Extraordinary Diligence and Presumption of Negligence

Are common carriers liable for injuries to passengers even if they have observed ordinary diligence and care? Explain. (2015)

Answer:

Yes, common carriers are liable to injuries to passengers even if the carriers observed ordinary diligence and care because the obligation imposed upon them by law is to exercise extra-ordinary diligence. Common carriers are bound to carry the passengers safely as far as human care and foresight can provide, using the utmost diligence of very cautious persons with a due regard for all the circumstances (Article 1755 of the Civil Code).

2. Liabilities of Common Carriers

Wisconsin Transportation Co., Inc. (WTC) owned and operated an inter-island de luxe bus service plying the Manila-Batangas-Mindoro route. Three friends, namely: Aurelio, Jerome and Florencio rode on the same WTC bus from Manila bound for Mindoro. Aurelio purchased a ticket for himself. Jerome, being a boyhood friend of the bus driver, was allowed a free ride by agreeing to sit during the trip on a stool placed in the aisle. Florencio, already penniless after spending all of his money on beer the night before, just stole a ride in the bus by hiding in the on-board toilet of the bus.

During the trip, the bus collided with another bus coming from the opposite direction. The three friends all suffered serious physical injuries.

What are WTC's liabilities, if any, in favor of Aurelio, Jerome and Florencio? Explain your answer. (4%) (2017 BAR)

SUGGESTED ANSWER

WTC, as a common carrier, is liable to Aurelio for breach of contract of carriage. In case of death or injury to passenger, there is a presumption of fault on the part of the common carrier unless it exercised an extraordinary diligence in ensuring the safety of its passengers. WTC is liable to Jerome for breach of contract of carriage although Jerome was carried grauitously. However, for Jerome, a stipulation limiting the liability of C for negligence is valid but not for willful acts or gross negligence (Article 1758 of the Civil Code). There being no contract of carriage between WTC and Florencio, WTC is not liable to Florencio for breach of contact, but WTC may be liable for a quasi-delict, if its driver was driving negligently.

Nautica Shipping Lines (Nautica) bought a second hand passenger ship from Japan. It modified the design of the bulkhead of the deck of the ship to accommodate more passengers. The ship sunk with its passengers in Tablas Strait due to heavy rains brought by the monsoon. The heirs of the passengers sued Nautica for its liability as a common carrier based on the reconfiguration of the bulkhead which may have compromised the stability of the ship. Nautica raised the defense that the monsoon is a fortuitous event and, at most, its liability is prescribed by the Limited Liability Rule. Decide with reasons. (2016 Bar)

SUGGESTED ANSWER

Nautica Shipping Lines is liable.

The limited liability rule will not apply in this case because there was contributory negligence on the part of the ship owner. The reconfiguration of the bulkhead of the deck of the ship to accommodate more passengers made the vessel unseaworthy (Philippine American Insurance Company v. Court of Appeals, G.R. No. 116940, June 11, 1997, 273 SCRA 262)

ALTERNATIVE ANSWER

Nautica Shipping Lines is not liable.

Monsoon rains have been jurisprudentially considered as force majeure. It being the cause of the accident, the ship owner should not be liable. Reconfiguration of the bulk head to accommodate more passengers per se does not amount to contributory negligence which will bar the ship owner to claim the defense of force majeure provided that it exercised due diligence before, during, and after the incident to prevent loss or injury

A railroad track of the Philippine National Railway (PNR) is located near a busy intersection of Puyat Avenue and Osmena Highway. One afternoon, the intersection was heavily congested, as usual. Juan, the driver of a public utility jeepney (PUJ), drove onto the railroad tracks but could go no farther because of the heavy traffic at the intersection. After the jeepney stopped right on the railroad track, it was hit and overturned by a PNR train, resulting in the death of Kim, a passenger of the PUJ, and injuries to Juan and his other passengers. Juan, the injured passengers and Kim's family sued the PNR for damages for its negligence. It was established that the steel pole barrier before the track was broken, and that the PNR had the last clear chance of avoiding the accident. On the other hand, the PNR raised the defense that the track is for the exclusive use of the train and that motorists are aware that it is negligence per se to stop their vehicles on the tracks. Decide the case and explain. (2016 Bar)

SUGGESTED ANSWER

The case shall be decided in favor of the injured passengers and Kim's family. PNR had the last clear chance of avoiding the injury but did not exercise the diligence expected of it under the circumstances.

ALTERNATIVE ANSWER

The driver of the PUJ and PNR are solidarily liable since the PUJ was guilty of contributory negligence. It is settled in jurisprudence that the tortfeasor and the common carrier are solidarily liable in case of death or injury to passengers of the carrier.

One of the passenger buses owned by Continental Transit Corporation (CTC), plying its usual route, figured in a collision with another bus owned by Unniversla Transport Inc. (UTI). Among those injured inside the CTC bus were: Romeo, a stow away; Samuel, a pickpocket then in the act of robbing his seatmate when the collision occurred; Teresita, the bus driver's mistress who usually accompanied the driver on his trips for free; and Uriel, a holder of a free riding pass he won in a raffle held by CTC.

Do Romeo, Samuel, Teresita, and Uriel have a cause of action for damages against UTI? Explain.

Answer:

Romeo, Samuel, Teresita, and Uriel may sue UTI on the basis of quasi-delict since they have no pre-existing contractual relationship with UTI. They may allege that the collision was due to the negligence of driver of UTI and UTI was negligent in the selection and supervision of its driver. (BAR 2009)

X, while driving his Toyota Altis, tried to cross the railway tract of PNR along Blumetritt Avenida Ext., Manila. The train as it approached Blumentritt, applied its horn as a warning to all the vehicles that might be crossing the railway tract, but there was really nobody manning the crossing. X was listening to his iPod touch, hence, he did not hear the sound of the horn of the train and so his car was hit by the train. As a result of the accident, X suffered some injuries and his car was totally destroyed as a result of the impact. Is PNR liable?

- a. PNR is not liable because X should have known that he was crossing a place designated as crossing for train, and therefore should have been more careful;
- b. PNR is a liable because Railroad companies owe to the public a duty of exercising a reasonable degree of care to avoid injury to person and property at railroad crossings which means a flagman or a watchman should have been posted to warn the public at all times;
- c. PNR is not liable because it blew its horn when it was about to cross the railway along Blumentritt Avenida Ext.;
- d. PNR is not liable because X was negligent, for listening to his iPod touch while driving.

Answer:

a. PNR is not liable because X should have known that he was crossing a place designated as crossing for train, and therefore should have been more careful. (BAR 2012)

A. Defenses of Common Carriers

One of the passenger buses owned by Continental Transit Corporation (CTC), plying its usual route, figured in a collision with another bus owned by Unniversla Transport Inc. (UTI). Among those injured inside the CTC bus were: Romeo, a stow away; Samuel, a pickpocket then in the act of robbing his seatmate when the collision occurred; Teresita, the bus driver's mistress who usually accompanied the driver on his trips for free; and Uriel, a holder of a free riding pass he won in a raffle held by CTC.

What, if any, are the valid defenses that CTC and UTI can raise in the respective actions against them? Explain.

Answer:

With respect to Romeo, Samuel and Teresita, since there was no pre-existing contractual relationship between them and CTC, CTC can raise the defense that it exercised the due diligence of a good father of a family in the selection of its driver.

It can raise the same defense against Uriel if there is a stipulation that exempts it from liability for simple negligence, but not for willful acts or gross negligence.

CTC cam also raise against all the plaintiffs the defense that the collision was due exclusively to the negligence of the driver of UTI, and this constitutes a fortuitous event, because there was no concurrent negligence on the part of its own driver.

CTC can also raise against Samuel the defense that he was engaged in a seriously illegal act at the time of the collision, which can render him liable for damages on the basis of quasi-delict.

Since UTI had no pre-existing contractual relationship with any of the plaintiffs, it can raise the defense that it exercised due diligence in the selection and supervision of its driver, that the collision was due exclusively to the negligence of the driver of CTC, and that Samuel was committing a seriously illegal act at the time of the collision. (BAR 2009)

B, while drunk, accepted a passenger in his taxicab. B then drove the taxi recklessly, and inevitably, it crashed into an electric post, resulting in serious physical injuries to the passengers. The latter then filed a suit for tort against B's operator, A, but A raised the defense of having exercised extraordinary diligence in the safety of the passenger. Is his defense tenable?

- a. Yes, as a common carrier can rebut the presumption of negligence by raising such a defense.
- b. No, as in tort actions, the proper defense is due diligence in the selection and supervision of the employee by the employer.

- c. No, as B, the common carrier's employee, was obviously negligent due to his intoxication.
- d. Yes, as a common carrier can invoke extraordinary diligence in the safety of passengers in tort cases.

b. No, as in tort actions, the proper defense is due diligence in the selection and supervision of the employee by the employer. (BAR 2011)

B. Vigilance over Goods

- 1. Exempting Causes
 - a. Requirement of Absence of Negligence
 - b. Absence of Delay
 - c. Due Diligence to Prevent or Lessen the Loss
- 2. Contributory Negligence
- 3. Duration of Liability
 - a. Delivery of Goods to Common Carrier
 - b. Actual or Constructive Delivery

The liability of a common carrier for the goods it transports begins from the time of

- a. Conditional receipt.
- b. Constructive receipt.
- c. Actual receipt.
- d. Either actual or constructive receipt.

Answer:

d. Either actual or constructive receipt. (BAR 2011)

c. Temporary Unloading or Storage

S delivered 10 boxes of cellphones to Trek Bus Liner, for transport from Manila to llocos Sur on the following day, for which S paid the freightage. Meanwhile, the boxes were stored in the bus liner's bodega. That night, however, a robber broke into the bodega and stole S's boxes. S sues Trek Bus Liner for contractual breach but the latter argues that S has no cause of action based on such breach since the loss occurred while the goods awaited transport. Who is correct?

- a. The bus liner since the goods were not lost while being transported.
- b. S since the goods were unconditionally placed with T for transportation
- c. S since the freightage for the goods had been paid.
- d. The bus liner since the loss was due to a fortuitous event.

- b. S since the goods were unconditionally placed with T for transportation. (BAR 2011)
- 4. Stipulation for Limitation of Liability
- a. Void Stipulations
- b. Limitation of Liability to Fixed Amount
- c. Limitation of Liability in Absence of Declaration of Greater Value
- 5. Liability for Baggage of Passengers
- a. Checked-In Baggage
- b. Baggage in Possession of Passengers
- C. Safety of Passengers

In a contract of carriage, the common carrier I liable for the injury or death of a passenger resulting from its employee's fault although the latter acted beyond the scope of his authority. This is based on the

- a. Rule that the carrier has an implied duty to transport the passenger safely.
- b. Rule that the carrier has an express duty to transport the passenger safely.
- c. Doctrine of Respondeat Superior.
- d. Rule in culpa aquiliana.

Answer:

a. Rule that the carrier has an implied duty to transport the passenger safely. (BAR 2011)

Fil-Asia Air Flight 916 was on a scheduled passenger flight from Manila when it crashed as it landed at the Cagayan de Oro airport; the pilot miscalculated the plane's approach and undershot the runway. Of the 150 people on board, 10 passengers died at the crash scene.

Of the 10 who dies, one was a passenger who managed to leave the plane but was run over by an ambulance coming to the rescue. Another was an airline employee who hitched a free ride to Cagayan de Oro and who was not in the passenger manifest.

It appears from the Civil Aeronautics Authority investigation that the co-pilot who had control of the plane's landing had less than the required flying and landing time experience, and should not have been in control of the plane at the time. He was allowed to fly as a co-pilot because of the scarcity of pilots—Philippine pilots have been recruited by foreign airlines under vastly improved flying terms and wages so that newer and less trained pilots are being locally deployed. The main

pilot, on the other hand, had a very high level of blood alcohol at the time of the crash.

You are part of the team that the victims hired to handle the case for them as a group. In your case conference, the following questions came up:

- a. Explain the causes of action legally possible under the given facts against the airline and the pilots; whom will you specifically implead in these causes of action?
- b. How will you handle the cases of the passenger run over by the ambulance and the airline employee allowed to hitch a free ride to Cagayan de Oro?

Answer:

a. A complaint for breach of contract of carriage can be filed against Fil-Asia air for failure to exercise extraordinary diligence in transporting the passengers safely from their point of embarkation to their destination.

A complaint based on a quasi-delict can be filed against the pilots because of their fault and negligence. FilAsia Air can be included for negligence in the selection and supervision of the pilots.

A third cause of action may be a criminal prosecution for reckless imprudence resulting in homicide against two pilots. The airline will be subsidiarily liable for the civil liability only after the pilots are convicted and found to be insolvent.

b. It is the driver of the ambulance and his employer who should be held liable for damages, because a passenger was run over. This is in accordance with Articles 2176 and 2180 of the Civil Code. There could also be a criminal prosecution for reckless imprudence resulting in homicide against the ambulance driver and the consequent civil liability.

Since the airline employee was being transported gratuitously, Fil-Asia Air was not required to exercise extraordinary diligence for his safety and only ordinary care. (BAR 2013)

1. Void Stipulations

2. Duration of Liability

a. Waiting for Carrier or Boarding of Carrier

P, a sales girl in a flower shop at the Ayala Station of the Metro Rail Transit (MRT) bought two tokens or tickets, one for her ride to work and another for her ride home. She got to her flower shop where she usually worked from 8:00am-5:00pm.

At about 3:00pm, while P was attending to her duties at the flower shop, two crews of the MRT got into a fight near the flower shop, causing injuries to P in the process. Can P sue the MRT for contractual breach as she was within the MRT premises where she would shortly take her ride home?

- a. No, since the incident took place, not in the MRT train coach, but at the MRT station.
- b. No, since P had no intention to board an MRT train coach when the incident occurred.
- c. Yes, since she already had a ticket for her ride home and was in the MRT's premises at the time of the incident.
- d. Yes, since she bought a round trip ticket and MRT had a duty while she was at its station to keep her safe for her return trip.

Answer:

b. No, since P had no intention to board an MRT train coach when the incident occurred. (BAR 2011)

b. Arrival at Destination

3. Liability for Acts of Others

a. Employees

The AAA Bus Company picks up passengers along EDSA, X, the conductor, while on board the bus, drew his gun and randomly shot the passengers inside. As a result, Y, a passenger, was shot and died instantly. Is AAA Bus Company liable?

- a. The bus company is not liable for as long as the bus company can show that when they hired X, they did the right selection process;
- b. The bus company cannot be held liable because what X did is not part of his responsibility;
- c. The bus company is liable because common carriers are liable for the negligence or willful act of its employees even though they acted beyond the scope of their responsibility;
- d. The bus company is not liable because there is no way that the bus company can anticipate the act of X.

Answer:

c. The bus company is liable because common carriers are liable for the negligence or willful act of its employees even though they acted beyond the scope of their responsibility. (BAR 2012)

b. Other Passengers and Strangers

P rode a Sentinel Liner bus going to Baguio from Manila. At a stop-over in Tarlac, the bus driver, the conductor, and the passengers disembarked for lunch. P decided, however, to remain in the bus, the door of which was not locked. At this

point, V, a vendor, sneaked into the bus and offered P some refreshments. When P rudely declined, V attacked him, resulting in P suffering from bruises and contusions. Does he have cause to sue Sentinel Liner?

- a. Yes, since the carrier's crew did nothing to protect a passenger who remained in the bus during the stop-over.
- b. No, since the carrier's crew could not have foreseen the attack.
- c. Yes, since the bus is liable for anything that goes wrong in the course of the trip.
- d. No, since the attack on P took place when the bus was at a stop-over.

Answer:

a. Yes, since the carrier's crew did nothing to protect a passenger who remained in the bus during the stopover. (BAR 2011)

- 4. Extent of Liability for Damages
- a. Registered Owner Rule (Kabit-system)

X owns a fleet of taxicabs. He operates it through what is known as boundary system. Y drives one of such taxicabs and pays X a fixed amount of P1,000 daily under the boundary system. This means that anything above P1,000 would be the earnings of Y. Y, driving recklessly, hit an old lady crossing the street. Which statement is most accurate?

- a. X as the owner is exempt from liability because he was not the one driving;
- b. X as the owner is exempt from liability because precisely the arrangement is one under the "boundary system";
- c. X will not be exempt from liability because he remains to be the registered owner and the boundary system will not allow the circumvention of the law to avoid liability;
- d. Y is the only one liable because he drove recklessly.

Answer:

c. X will not be exempt from liability because he remains to be the registered owner and the boundary system will not allow the circumvention of the law to avoid liability. (BAR 2012)

X owns a passenger jeepney covered by Certificate of Public Convenience. He allowed Y to use its Certificate of Convenience for a consideration. Y therefore was operating the passenger jeepney under the same Certificate of Public Convenience (Kabit System) under the name of X. the passenger jeepney met an accident. Who will be liable?

- a. Y, the one actually operating the jeepney, will be liable to the injured party;
- b. X will be the one liable to the injured party despite the fact that it is Y who is actually operating the jeepney, because while the Kabit System is tolerated, the public should not be inconvenienced by the arrangement;
- c. X will not be held liable if he can prove that he is not the owner anymore;
- d. Public Policy dictates that the real owner, even not the registered one, will

be hld liable.

Answer:

b. X will be the one liable to the injured party despite the fact that it is Y who is actually operating the jeepney, because while the Kabit System is tolerated, the public should not be inconvenienced by the arrangement. (BAR 2012)

D. Bill of Lading

1. Three-Fold Character

Discuss the three-fold character of a bill of lading. (2015)

Answer:

A bill of lading is considered a receipt for the goods shipped to the common carrier. It also serves as the contract by which three parties, namely, the shipper, the carrier and the consignee undertake specific responsibilities and assumed stipulated obligations. Third, it is the evidence of the existence of the contract of carriage providing for the terms and conditions thereof (Keng Hua Paper Products vs. Court of Appeals, 286 SCRA 257).

2. Delivery of Goods

X is a trader of school supplies in Calapan, Oriental Mindoro. To bring the school supplies to Calapan, it has to be transported by a vessel. Because there were so many passengers, the 2 boxes of schools supplies were loaded but the shipping company was not able to issue the Bill of lading. So, on board, the Ship Captain issued the Bill of Lading. So, on board, the Ship Captain issued instead a "shipping receipt" to X indicating the 2 boxes of school supplies being part of the cargo of the vessel. Which phrase therefore, is the most accurate?

- a. The owner of the vessel is not liable because no bill of lading was issued to X hence, no contract of carriage was perfected;
- b. It is possible to have a contract of carriage of cargo even without a bill of lading, and the "shipping receipt" would be sufficient;
- c. The only acceptable document of title is a Bill of Lading;
- d. None of the above.

Answer:

b. It is possible to have a contract of carriage of cargo even without a bill of lading, and the "shipping receipt" would be sufficient. (BAR 2012)

- a. Period of Delivery
- b. Delivery Without Surrender of Bill of Lading

c. Refusal of Consignee to Take Delivery

- 3. Period for Filing Claims
- 4. Period for Filing Actions
- **E. Maritime Commerce**

1. Charter Parties

a. Bareboat/Demise Charter

Onassis Shipping, Inc. (Onassis) operated passenger vessels and cargo trucks, and offered its services to the general public. In line with its vision and mission to protect the environment, Go-Green Asia (Go-Green), an NGO affiliated with Greenpeace, entered into a contract with Onassis whereby GoGreen would operate with its own crew the MN Dolphin, an ocean-going passenger vessel of Onassis. While on its way to Palawan carrying Go-Green's invited guests who were international and local observers desirous of checking certain environmental concerns in the area, the MN Dolphin encountered high waves and strong winds caused by a typhoon in the West Philippine Sea. The rough seas led to serious physical injuries to some of the guests.

Discuss the liabilities of Onassis and Go-Green to the passengers of the MN Dolphin. Explain briefly your answer. (3%) (2017 BAR)

SUGGESTED ANSWER

The contract that Onassis and Greenpeace entered into is a bareboat or demise charter because Greenpeace was not only given possession of the vessel but also the command and control of the navigation as result of its authority to hire its own crew who will man the vessel. The bareboat charter effectively converts Onassis from a common carrier a private carrier (Federal Phoenix Assurance v. Fortune Sea Carrier, Inc. G.R. No. 188118, November 23, 2015). Being a mere lessor and having ceased to be the owner of the vessel with respect to the navigation, Onassis has no liability to the passengers who contracted with Greenpeace. Greenpeace is the one liable to the passengers for the injuries they so tamed in the course of the navigation.

- b. Time Charter
- c. Voyage/Trip Charter
- 2. Liability of Ship Owners and Shipping Agents
 - a. Liability for Acts of Captain
 - b. Limited Liability Rule
 - c. Exceptions to Limited Liability
- 3. Accidents and Damages in Maritime Commerce
 - a. General Average and Particular Average

What is a "Jason clause" in a charter party? (2%) (2015)

Answer:

The Jason clause derives its name from The Jason 225 US 32 (1912) decided by the US Supreme Court under the Harter Act. By the Jason clause, a shipowner (provided he had exercised due diligence to make the ship seaworthy and properly manned, equipped and supplied) could claim a general average contribution from cargo, even where the damage was caused by faulty navigation of the vessel, provided that the bill of lading excluded liability for such faults.

NB. This is not a familiar principle in Philippine maritime commerce and the question is not consistent with the norm of asking questions to test the knowledge of entry level lawyers. It is respectfully submitted that the question should be given outright credit in favor of the examinees regardless of their answer.

Global Transport Services, Inc (GTSI) operates a fleet of cargo vessels plying interisland routes. One of its vessels, MV Donna Juana, left the port of Manila for Cebu laden with, among other goods, 10,000 television sets consigned to Romualdo, a TV retailer in Cebu.

When the vessel was about 10 nautical miles away from Manila, the ship captain heard on the radio that a typhoon which, as announced by PAG-ASA, was on its way out of the country, had suddenly veered back into Philippine territory. The captain realized that MV Dona Juana would traverse the storm's path, but decided to proceed with the voyage. True enough, the vessel sailed into the storm. The captain ordered the jettison of the 10,000 television sets, along with some other cargo, in order to lighten the vessel and make it easier to steer the vessel out of the path of the typhoon. Eventually, the vessel, with its crew intact, arrived safely in Cebu.

Will you characterize the jettison of Romualdo's TV sets as an average? If so, what kind of an average, and why? If not, why not?

Answer:

The jettison of Romualdo's TV sets resulted in a general average loss, which entitles him compensation or indemnification from the shipowner and the owners of the cargoes saved by the jettison.

Against whom does Romualdo have a cause of action for indemnity of his lost TV sets? Explain.

Answer:

Romualdo has a cause of action for his lost TV sets against the shipowner and the owners of the cargoes saved by the jettison. The jettison of the TV sets resulted in a general average loss, entitling Romualdo to indemnity for the lost TV sets. (BAR 2009)

What are the types of averages in marine commerce?

The types of averages are particular and general average. Particular averages include all expenses and damages caused to the vessel or to the cargo which did not inure to the common benefit and profit of all the persons interested in the vessel and the cargo. General averages include all damages and expenses which are deliberately caused to save the vessel, its cargo, or both at the same time, from real and known risk. (BAR 2010)

An importer of Christmas toys loaded 100 boxes of Santa Clause talking dolls aboard a ship in Korea bound for Manila. With the intention of smuggling 1/2 of his cargo, he took a bill of lading for only 50 boxes to save the more precious cargo.

Is the importer entitled to receive any indemnity for average?

Answer:

No. The importer is not entitled to receive any indemnity for average. In order that the goods jettisoned may be included in the general average and the owner be entitled to indemnity, it is necessary that their existence on board be proven by means of the bill of lading. (BAR 2010)

b. Collisions

- c. Doctrine of Inscrutable Fault
- d. Salvage
- e. Maritime Protest
- 4. Carriage of Goods by Sea Act (COGSA)

 a. Application

Akiro of Tokyo, Japan sent various goods to his friend Juan in Cebu City, Philippines, through one of the vessels of Worthwell Shippers, Inc., an American corporation. En route to Cebu City, the vessel had two stops, first in Hong Kong, and second, in Manila.

While travelling from Tokyo to Hong Kong, the goods were damaged.

What law will govern?

- a. Japanese law:
- b. Hong Kong law;
- c. Chinese law;
- d. Philippine law:
- e. American law.

d. Philippine law (BAR 2013)

b. Notice of Loss or Damage

c. Period of Prescription

AA entered into a contract with BB for the latter to transport ladies wear from Manila to France with transshipment via Taiwan. Somehow the goods were not loaded in Taiwan on time, hence, these arrived in France "off-season1/2." the AAvaluewas by only the paid buyer.

AA claimed damages from BB. BB invoked prescription as a defense under the COGSA. Considering the "loss of value" of the ladies wear as claimed by AA, is BB's defense tenable? Explain.

Answer:

No. the defense of BB is not tenable. The 1 year prescriptive period in the COGSA applies only in case the goods were not delivered or were delivered in a damaged condition. It does not apply to damages as a result of delay in the delivery of the goods. The prescription of the action is governed by Article 1144 of the Civil Code, which provides for a prescriptive period of 10 years in case of actions based on a written contract. (BAR 2010)

Akiro of Tokyo, Japan sent various goods to his friend Juan in Cebu City, Philippines, through one of the vessels of Worthwell Shippers, Inc., an American corporation. En route to Cebu City, the vessel had two stops, first in Hong Kong, and second, in Manila.

Assuming Philippine law is to be applicable and Juan fails to file a claim with the carrier, may he still commence an action to recover damages with the court?

- a. No, the failure to file a claim with the carrier is a condition precedent for recovery;
- b. Yes, provided he files the complaint within 10 years from delivery;
- c. Yes, provided he files the complaint within 10 years from discovery of the damage;
- d. Yes, provided he files the complaint within 1 year from delivery;
- e. Yes, provided he files the complaint within 1 year from discovery of the damage;

Answer:

d. Yes, provided he files the complaint within 1 year from delivery. (BAR 2013)

On December 1, 2010, Kore A Corporation shipped from South Korea to LT Corporation in Manila some 300,000 sheets of high-grade special steel. The

shipment was insured against all risk by NA Insurance (NA). The carrying vessel arrived at the Port of Manila on January 10, 2011. When the shipment was discharged, it was noted that 25,000 sheets were damaged and in bad order. The entire shipment was turned over to the custody of ATI, the arrastre operator, on January 21, 2011 for storage and safekeeping, pending its withdrawal by the consignee's authorized customs broker, RVM.

On January 26 and 29, 2011, the subject shipment was withdrawn by RVM from the custody of ATI. On January 29, 2011, prior to the withdrawal of the last batch of the shipment, a joint inspection of the cargo was conducted per the Request for bad Order Survey (RBO) dated January 28, 2011. The examination report showed that 30,000 sheets of steel were damaged and in bad order.

NA Insurance paid LT Corporation the amount of P30 M for the 30,000 sheets that were damaged, as shown in the Subrogation Receipt dated January 13, 2013. Thereafter, NA Insurance demanded reparation against ATI for the goods damaged in its custody, in the amount of P5 M. ATI alleged that the COGSA applies in this case since the goods were shipped from a foreign port to the Philippines. NA Insurance claims that the COGSA does not apply, since ATI is not a shipper or carrier. Who is correct?

Answer:

NA Insurance is correct. ATI should be ordered to pay NA Insurance notwithstanding the lapse of the one year prescriptive period for filing a suit under the COGSA. The term "carriage of goods" under Section 1 in COGSA, covers the period from the time when the goods are loaded to the time when they are discharged from the ship infer that the period of time when the goods have been discharged from the ship and given to the custody of the arrastre operator is not covered by the COGSA. The COGSA does not mention that an arrastre operator may invoke the prescriptive period of one year; hence, it does not cover the arrastre operator. (BAR 2014)

- d. Limitation of Liability
- a. Bottomry
- F. The Warsaw Convention
 - 1. Applicability
 - 2. Limitation of Liability
 - a. Liability to Passengers
 - b. Liability for Checked Baggage
 - c. Liability for Hand carried Baggage

X took PAL Flight PR 102 to Los Angeles, USA. She had 2 luggage checked-in and was 2 baggage checks. When X reached Los Angeles, 1 of the 2 checked-in luggage could not be found. Which statement is most accurate?

- a. PAL is liable for the loss of the checked-in-luggage under the provision of the Warsaw Convention on Air Transport;
- b. PAL is liable for the loss only if the baggage check expressly states that the airline shall be liable in case of loss;
- c. PAL cannot be held liable because that is the risk that a passenger takes when she checks-in her baggage;
- d. PAL can only be held liable if it can be proven that PAL was negligent.

- a. PAL is liable for the loss of the checked-in-luggage under the provision of the Warsaw Convention on Air Transport. (BAR 2012)
 - 3. Willful Misconduct
- **G. Public Service Act**

Under the Public Service Act, an administrative agency has the power to approve provisionally the rates of public utilities without a hearing in case of urgent public needs. The exercise of this power is

- a. Supervisory
- b. Absolute
- c. Discretionary
- d. Mandatory

Answer:

- c. Discretionary. (BAR 2011)
 - a. Certificate of Public Convenience
 - b. Prior Operator Rule

VI. The Corporation Code
A. Corporation

Under the Nell Doctrine, so called because it was first pronounced by the Supreme Court in the 1965 ruling in Nell v. Pacific Farms, Inc. (GR No. 20850, November 29, 1965, 15 SCRA 415), the general rule is that where one corporation sells or otherwise transfers all of its assets to another corporation, the latter is not liable for the debts and liabilities of the transferor.

State the exceptions to the Nell Doctrine. (4%) (2017 BAR)

SUGGESTED ANSWER

The exceptions to the Nell doctrine are as follows:

- (I) When the buyer expressly or impliedly assumes the liabilities of the seller;
- (II) If the sale amounts to a merger or consolidation;
- (III) If the sale is entered into fraudulently or made in bad faith;
- (IV) If the buyer is merely a continuation of the personality of the seller or the so called business enterprise transfer rule.

Your client Dianne approaches you for legal advice on putting up a medium-sized restaurant business that will specialize in a novel type of cuisine. As Dianne feels that the business is a little risky, she wonders whether she should use a corporation as the business vehicle, or just run it as a single proprietorship. She already has an existing corporation that is producing meat products profitably and is also considering the alternative of simply setting up the restaurant as a branch office of the existing corporation.

Briefly explain to your client what you see as the legal advantages and disadvantages of using a separate corporation, a single proprietorship, or a branch of an existing corporation for the proposed restaurant business.

Answer:

If Dianne will set up a separate corporation, her liability for its obligations and losses will be limited to the amount of her subscription in the absence of showing that there is a ground to disregard its separate juridical personality. If she were to operate a single proprietorship, her liability for its debts and losses will be unlimited.

The formation and the operation of a corporation require a great deal of paper work and record-keeping. This is not the situation in the case of a single proprietorship.

If she were to set-up the restaurant as a branch office an existing corporation, the corporation will have more funds as capital than if she were to form a separate corporation. However, all the assets of the existing corporation will be liable for the debts and losses of the restaurant business. (BAR 2010)

Stock Corporation and Non-stock Corporation

- a. Definition
- b. Attributes of the Corporation
- c. Distinguished from Partnership
- **B. Other Classes of Corporations**
 - 1. De facto vs. De jure

The Articles of Incorporation of AAA Corporation was approved by SEC. After the receipt of the Certificate of Approval from the SEC, AAA Corporation decided to immediately start the operation of its business despite the fact that it has no approved By-Laws. What is the legal status of the AAA Corporation?

- a. A de jure corporation;
- b. A de facto corporation;
- c. A corporation by estoppels;
- d. An unregistered corporation.

Answer:

a. A de jure corporation. (BAR 2012)

An alternative answer is that it is a de facto corporation as held in Sawadyaan vs Court of Appeals (2005 case)

2. Corporation by Estoppel

Unknown to the other four proponents, Enrico (who had been given the task of attending to the Articles of Incorporation of the proposed corporation, Auto Mo, Ayos Ko) misappropriated the filing fees and never filed the Articles of Incorporation with the SEC. instead, he prepared and presented to the proposed incorporators a falsified SEC certificate approving the Articles. Relying on the falsified SEC certificate, the latter began assuming and discharging corporate powers.

Auto Mo, Ayos Ko is a _____.

- A. De jure corporation;
- B. De facto corporation;
- C. Corporation by estoppel;
- D. General partnership;
- E. None of the above.

Answer:

- c) Corporation by estoppel— if the term "latter" refers to the incorporators.
- e) None of the above—if the term "latter" refers to Enrico. (BAR 2013)
 - C. Corporations going public vs. Corporations going private
 - C. Nationality of Corporation

TRUE or FALSE — EXPLAIN BRIEFLY YOUR ANSWER.

(b) The term capital in relation to public utilities under Sec. 11 Art. XII of the 1987 Constitution refers to the total outstanding capital sto comprising both common and non-voting preferred shares. (2%)

SUGGESTED ANSWER

(b) False, because it only relates to common and voting preferred shares as held in Heirs of Gamboa is. Taves (QR. No. 176579, Oct ber 9, 2012). To construe broadly the term capital as the total outstandin capital stock including both common and non voting preferred shar grossly contravenes the intent and letter of the Constitution that the St shall develop a self-reliant and independent national economy effective controlled by Filipino citizens. Control means owning the shares that allowed to vote the directors of the corporation who will manage and c trol the business affairs thereof.

[Note: An answer based on the most recent case of Roy v. Herbosa, G.R. 207246, April 18,2017 (a case decided after the cut-off date of the 2017 exams) where the SC held that the term capital means both the voting sh and the total outstanding eapital stock should also be considered correct].

- 1. Place of Incorporation Test
- 2. Control Test

Several American doctors wanted to set up a group clinic in the Philippines so they could render modern medical services. If the clinic is to be incorporated under our laws, what is the required foreign equity participation in such a corporation?

- 1. 40%
- 2. 0%
- 3. 60%
- 4. 70%

Answer:

b. 0% (BAR 2011)

3. Grandfather Rule

In 2015, R Corp., a domestic company that is wholly owned by Filipinos, filed its opposition to the applications for Mineral Production Sharing Agreements (MPSA) of O Corp., P Corp., and Q Corp. which were pending before the Panel of Arbitrators (POA) of the Department of Environment and Natural Resources (DENR). The three corporations wanted to undertake exploration and mining activities in the province of Isabela. The oppositor alleged that at least 60% of the capital shareholdings of the applicants are owned by B Corp., a 100% Chinese corporation, in violation of Sec. 2, Art. XII of the Constitution. The applicants countered that they are qualified corporations as defined under the Philippine Mining Act of 1995 and the Foreign Investments Act of 1991 since B Corp. holds only 40% of the capital stocks in each of them and not 60% as alleged by R Corp.

The Summary of Significant Accounting Policies statement of B Corp. reveals that the joint venture agreements of B Corp. with Sigma Corp. and Delta Corp. involve the 0 Corp., P Corp., and Q Corp. The ownership of the layered corporations and joint venture agreements show that B Corp. practically exercises control over the 0, P and Q corporations. 0, P and Q corporations contend that the control test should be applied and its MPSA applications granted. On the other hand, R Corp. argues that the "grandfather rule" should be applied. Decide with reasons. (2016 Bar)

SUGGESTED ANSWER:

The grandfather rule should apply. The Supreme Court held in a similar case that even though on paper the capital shareholding in a mining corporation is 60% owned by Filipinos and 40% by foreigners, if there is a doubt as to the locus of the beneficial ownership and control, the grandfather rule should apply. Based on the facts, B Corporation, a Chinese corporation, practically exercises control over O, P, and Q Corporations. Such circumstance creates a doubt as to where control and beneficial ownership reside that warrants application of the grandfather rule (Narra Nickel Mining and Development Corporation v. Redmont Consolidated Mines Corp., G.R. No. 195580, April 21, 2014).

Rules on Partly-Nationalized Business

The Articles of Incorporation of ABC Transport Co., a public utility, provides for 10 members in its Board of Directors. What is the prescribed minimum number of Filipino citizens in its Board?

- a. 10
- b. 6
- c. 7
- d. 5

Answer:

b. 6 (BAR 2011)

Bell Philippines, Inc. (BelPhil) is a public utility company, duly incorporated and registered with the SEC. its authorized capital stock consists of voting common shares and non-voting preferred shares, with equal par values of P100/share. Currently, the issued and outstanding capital stock of BelPhil consists only of common shares shared between Bayani Cruz, a Filipino with 60% of the issued common shares, and Bernard Fleet, a Canadian, with 40%.

To secure additional working fund, BelPhil issued preferred shares to Bernard Fleet equivalent to the currently outstanding common shares. A suit was filed questioning the corporate action on the ground that the foreign equity holdings in the company would now exceed the 40% foreign equity limit allowed under the Constitution for public utilities.

Rule on the legality of Bernard Fleet's current holdings.

Answer:

The holding of Bernard Fleet equivalent to the outstanding common shares is illegal. His holdings of preferred shares should not exceed 40%. Since the constitutional requirement of 60% Filipino ownership of the capital of public utilities applies not only to voting control but also to beneficial ownership of the corporation, it should also apply to the preferred shares. Preferred shares are also entitled to vote in certain corporate matters. The State shall develop a self-reliant and independent national economy effectively controlled by Filipinos. The effective control here should be mirrored across the board on all kinds of shares. (BAR 2013)

D. Corporate Juridical Personality

1. Doctrine of Separate Juridical Personality

Data Realty, Inc. (DR') was engaged in realty development. The 'family of Matteo owned 100% of the capital stock of OR!. Matteo was also the President and Chairman of the Board of Directors. Other members of Matteo's family held the major positions in DIU. Because of a nasty takeover fight with D&E Realty Co., Inc. (D&E), another realty developer, for the control of smaller realty company with vast landholdings, DRI and D&E engaged in an ;expensive litigation that eventually led to a money judgment being rendered h favor of D&E. Meantime, DR!, facing inability to pay its liabilities as they fall due but still holding substantial assets, filed a petition for voluntary rehabilitation. Trying to beat the consequences of rehabilitation proceedings, D&E moved in the trial court for the issuance of a writ of execution. The trial court also happened to be the rehabilitation court. The writ of execution was issued. Serving the writ of execution, Metro, the court sheriff who had just passed his Credit Transactions subject in law school, garnished Matteo's bank accounts, and levied hi's real properties, including his house and lot in Makati.

Are the garnishment and levy of Matteo's assets lawful and proper Explain your answer. (4%) (2017 BAR)

SUGGESTED ANSWER

The garnishment and levy of Matteo's assets are not valid, because Mateo is not covered by the rehabilitation proceedings or any stay order that the rehabilitation court may issue. It is DRI, with a legal personality separate and distinct from Matteo, which filed the petition for rehabilitation and would have been entitled to the effects of any commencement order (and stay order) that the court may issue. The commencement order would have the effect of setting aside any seizure o property or attempt to enforce a claim against the debtor. It would have been different if Matteo acted as surety and the court issues a commencement order with stay order, the effects of which are

retroactive to the filing of the petition. In which event, the garnish meat of his deposits and level of assets would have been valid.

ALTERNATIVE ANSWER

On the assumption that DRI's legal personality may be pierce to make it one and the same with Matteo, the garnishment of deposits an levy of assets are lawful and proper because the court has not issued yet commencement order prior to the garnishment and levy.

X Corp. operates a call center that received orders for pizzas on behalf of Y Corp. which operates a chain of pizza restaurants. The two companies have the same set of corporate officers. After 2 years, X Corp. dismissed its call center agents for no apparent reason. The agents filed a collective suit for illegal dismissal against both X Corp. and Y Corp. based on the doctrine of piercing the veil of corporate fiction. The latter set up a defense that the agents are in the employ of X Corp. which is a separate juridical entity. Is the defense appropriate?

- a. No, since the doctrine would apply, the two companies having the same set of corporate officers.
- b. No, the real employer is Y Corp., the pizza company, with X Corp. serving as an arm for receiving its outside orders for pizzas.
- c. Yes, it is not shown that one company completely dominates the finances, policies, and business practices of the latter.
- d. Yes, since the two companies perform two distinct businesses.

Answer:

c. Yes, it is not shown that one company completely dominates the finances, policies, and business practices of the latter. (BAR 2011)

X sold all his shares in AAA Hotel Corporation to Y. X owns 99% of AAA Hotel Corporation. As the new owner, Y wanted a reorganization of the hotel which is to include primarily the separation of all existing employees and the hiring of new employees. Which statement is most accurate?

- a. With the change in ownership, in effect there is a new juridical entity and therefore all employees are considered separated;
- b. Despite the change in shareholder, there is actually no change in the juridical entity and therefore existing employees cannot automatically be considered separated;
- c. Y, as the new shareholder, has the right to retain only those employees who in his judgment are qualified;
- d. For as long as the existing employees are given their separation pay, they can be terminated.

Answer:

b. Despite the change in shareholder, there is actually no change in the juridical entity and therefore existing employees cannot automatically be considered separated. (BAR 2012)

X owns 99% of the capital stock of SSS Corporation. X also own 99% of TTT Corporation. SSS Corporation obtained a loan from VVV Banks. On due date, SSS Corporate defaulted. TTT Corporation is financially healthy. Which statement is most accurate?

- a. X being a controlling owner of SSS Corporation can automatically be held personally liable for the loan of SSS Corporation;
- b. TTT Corporation, owned by 99% by X, can automatically be held liable;
- c. SSS Corporation and TTT Corporation, although both are owned by X, are 2 distinct corporations with separate juridical personalities hence, the TTT Corporation cannot automatically be held liable for the loan of SSS Corporation;
- d. The principle of piercing the veil of corporation fiction can be applied in this case

Answer:

c. SSS Corporation and TTT Corporation, although both are owned by X, are 2 distinct corporations with separate juridical personalities hence, the TTT Corporation cannot automatically be held liable for the loan of SSS Corporation. (BAR 2012)

In an action for collection of a sum of money, the RTC of Makati City issued a decision finding DSecurities, Inc. liable to Rehouse Corporation for P10 M. Subsequently, the writ of execution was issued but returned unsatisfied because D-Securities had no more assets to satisfy the judgment. Rehouse moved for an Alias Writ of Execution against Fairfield Bank (FB), the parent company of D-Securities. FB opposed the motion on the grounds that it is a separate entity and that it was never made party to the case. The RTC granted the motion and issued the Alias Writ of Execution. In its Resolution, the RTC relied on the following facts: 499,995 out of the 500,000 outstanding shares of stocks of D-Securities are owned by FB; FB had actual knowledge of the subject matter of litigation as the lawyers who represented D-Securities are also the lawyers of FB. As an alter ego, there is no need for a finding of fraud or illegality before the doctrine of piercing the veil of corporate fiction can be applied. The RTC ratiocinated that being one and the same entity in the eyes of the law, the service of summons upon DSecurities has bestowed jurisdiction over both the parent and wholly-owned subsidiary. Is the RTC correct?

Answer:

No, the RTC is not correct. The court must have first acquire jurisdiction over the corporation(s) involved before its or their separate personalities are disregarded; and the doctrine of piercing the veil of corporate entity can only be raised during a full-blown trial over a cause of action duly commenced involving parties duly brought under the

authority of the court by way of service of summons or what passes as such service. (BAR 2014)

- a. Liability for Torts and Crimes
- b. Recovery of Moral Damages
- 2. Doctrine of Piercing the Corporate Veil
 - a. Grounds for Application of Doctrine
 - b. Test in Determining Applicability

E. Incorporation and Organization

- 1. Promoter
- a. Liability of Promoter
- b. Liability of Corporation for Promoter's Contracts
- 2. Number and Qualifications of Incorporators

X is a Filipino immigrant residing in Sacramento, California. Y is a Filipino residing Quezon City. Z is a resident alien residing in Makati City. GGG Corporation is a domestic corporation—40% owned by foreigners and 60% owned by Filipinos, with T as authorized representative. CCC Corporation is a foreign corporation registered with the Philippines SEC, KKK Corporation is a domestic corporation (100%) Filipino owned. S is a Filipino, 16 years of age, and daughter of Y.

- a. Who can be incorporators? Who can be subscribers?
- b. What are the differences between an incorporator and a subscriber, if there are any?

Answer:

A. X, Y, Z and T could all be incorporators and subscribers. Note, however, that Section 10 of the Corporation Code requires that there must be at least 5 but not more than 15 incorporators (who must all be natural persons) and that a majority of the incorporators must be residents of the Philippines. S, being a minor, could neither be an incorporator nor a subscriber. GGG Corporation, CCC Corporation, and KKK Corporation could not be incorporators as they are not natural persons. However, they could be subscribers.

B. Some of the differences are as follows: first, all the incorporators are required to sign and acknowledge the Articles of Incorporation while the subscribers, as such, are not subject to the same requirement; second, the incorporators are all required to be natural persons while the subscribers could either be natural or juridical persons; and third, the number of incorporators cannot exceed 15 while the number of subscribers could be more than 15 (subject to compliance, in the appropriate cases, with the requirements of the SRC). (BAR 2012)

NB We have to add that there is a Philippine residency requirement for majority of the incorporators whereas there is no such requirement for subscribers.

3. Corporate Name — Limitations on Use of Corporate Name

A, the proprietor of a fleet of 10 taxicabs, decides to adopt, as his business name, "A Transport Co., Inc." May this be allowed?

- a. No, it would be deceptive since he is a proprietor, not a corporation.
- b. No, since "A" is a generic name, not suitable for registration.
- c. Yes, since his line of business is public transportation.
- d. Yes, since such name would give his business a corporate identity.

Answer:

a. No, it would be deceptive since he is a proprietor, not a corporation. (BAR 2011)

- 4. Corporate Term
- 5. Minimum Capital Stock and Subscription Requirements
- 6. Articles of Incorporation

The Articles of Incorporation must be accompanied by a Treasurer's Affidavit certifying under oath, among others, that the total subscription paid is:

- a. Not less than P25,000.00
- b. Not more than P5,000.00
- c. Not less than P5,000.00
- d. Not more than P25,000.00

Answer:

c. Not less than P5,000.00 (BAR 2011)

a. Nature and Function of Articles

Triple A Corporation (Triple A) was incorporated in 1960, with 500 founder's shares and 78 common shares as its initial capital stock subscription. However, Triple A registered its stock and transfer books only in 1978, and recorded merely 33 common shares as the corporation's issued and outstanding shares.

In 1982, Juancho, the sole heir of one of the original incorporators filed a petition with the SEC for the registration of his property rights over 120 founder's shares and 12 common shares. The petition was supported by a copy of the Articles of Incorporation indicating the incorporators' initial capital stock subscription. Will the petition be granted? Why or why not?

Answer:

Yes. The articles of incorporation defines the charter of the corporation and the contractual relationship between the State and the corporation, the State and the stockholders, and between the corporation and the stockholders. Its contents are thus

binding upon both the corporation and the stockholders, conferring on Juancho a clear right to have his stockholding recorded. (BAR 2009)

b. Contents

c. Amendment

Guetze and his wife have 3 chidren: Neymar, 25, who is now based in Rio de Janeiro, Brazil; Muelter, 23, who has migrated to Munich, Germany; and James, 21, who resides in Bogota, Colombia. Neymar and Muelter have since renounced their Philippine citizenship in favor of their country of residence. Nearing 70 years old, Guetze decided to incorporate his business in Binondo, Manila. He asked his wife and 3 children to act as incorporators with 1 share of stock each, while he owned 999,996 shares of the 1,000,000 shares of the capital stock.

Assuming the corporation has been properly registered, may the Articles of Incorporation now be amended to reduce the number of directors to two—Guetze and his wife—to reflect the real owners of the shares of stock?

Answer:

No, the Articles of Incorporation may not be amended to reduce the number of directors to two. Section 14 of the Corporation Code requires that the Articles of Incorporation shall contain the number of directors, which shall not be less than 5 nor more than 15. Hence, the reduction of the number of directors to two, to reflect the real owners of the shares of stock, is not valid (BAR 2014)

d. Non-Amendable Items

7. Registration and Issuance of Certificate of Incorporation

You have been asked to incorporate a new company to be called FSB Savings & Mortgage Bank, Inc. List the documents that you must submit to the SEC to obtain a certificate of incorporation for FSB Savings & Mortgage Bank, Inc.

Answer:

The documents to be submitted to the SEC to incorporate a new company to be called FSB Savings & Mortgage Bank, Inc., to obtain the certificate of incorporation for said company, are:

- a. Articles of Incorporation;
- b. Treasurer's affidavit:
- c. Certificate of Authority from the Monetary Board of the BSP;
- d. Verification slip from the records of the SEC whether or not the proposed name has already been adopted by another corporation, partnership or association:
- e. Letter undertaking to change the proposed name if already adopted by another corporation, partnership or association;

- f. Bank certificate of deposit concerning the paid-up capital;
- g. Letter authorizing the SEC or Monetary Board or its duly authorized representative to examine the bank records regarding the deposit of the paid-up capital;
- h. Registration sheet.

A corporation organized under the Corporation Code commences to have corporate existence and juridical personality and is deemed incorporated:

- a. From the date the application for incorporation is filed with the SEC.
- b. From the date the SEC issues a certificate of incorporation under its official seal.
- c. 30 days after the date the application for incorporation is filed with the SEC.
- d. 30 days after the date the SEC issues a certificate of incorporation under its official seal.

Answer:

b. From the date the SEC issues a certificate of incorporation under its official seal. (BAR 2014)

Guetze and his wife have 3 chidren: Neymar, 25, who is now based in Rio de Janeiro, Brazil; Muelter, 23, who has migrated to Munich, Germany; and James, 21, who resides in Bogota, Colombia. Neymar and Muelter have since renounced their Philippine citizenship in favor of their country of residence. Nearing 70 years old, Guetze decided to incorporate his business in Binondo, Manila. He asked his wife and 3 children to act as incorporators with 1 share of stock each, while he owned 999,996 shares of the 1,000,000 shares of the capital stock.

Assuming all other requirements are met, should the SEC accept or reject the Articles of Incorporation? Why?

Answer:

Yes, the SEC should accept the Articles of Incorporation. If the Articles of Incorporation substantially comply with the statute and all other requirements are met, the SEC has no discretion, but may be compelled by mandamus to file them. The discretion exercised by SEC does not extend to the merits of an application for incorporation, although it may be exercised as to matters of form. (BAR 2014)

NB As an alternative answer, the SEC should reject the articles of incorporation because majority of the incorporators are not Philippine residents.

8. Adoption of By-Laws

- a. Nature and Functions of By-Laws
- b. Requisites of Valid By-Laws
 - c. Binding Effects

d. Amendment or Revision

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In a special meeting called for the purpose, 2/3 of the stockholders representing the outstanding capital stock in X Co. authorized the company's Board of Directors to amend its By-laws. By majority vote, the Board then approved the amendment. Is the amendment valid?

- a. No, since the stockholders cannot delegate their right to amend the By-laws to the Board.
- b. Yes, since the majority votes in the Board was sufficient to amend the Bylaws.
- c. No, because, the voting in the Board should have been by a majority of a quorum.
- d. Yes, since the votes of 2/3 of the stockholders and majority of the Board were secured.

Suggested Answer:

a. No, since the stockholders cannot delegate their right to amend the By-laws to the Board. (BAR 2011)

NB The correct answer is d) because under Section 48 of the Corporation Code, the stockholders representing at least 2/3s of the outstanding capital stock may delegate to the Board the authority to amend the by laws

F. Corporate Powers

1. General Powers, Theory of General Capacity

a. Enter into Contracts

AAA Corporation is a wholly owned subsidiary of BBB Corporation. To support the business of AAA Corporation, BBB Corporation agreed to give its corporate guarantee to the loan of AAA Corporation. What is required so that the corporate quarantee will be valid?

- a. It only requires the approval of the Board of Directors of BBB Corporation;
- The Articles of Incorporation must provide such power and be approved by the Board of Directors;
- c. Providing corporate guarantee to another corporation is a necessary exercise of power of a corporation;
- d. It would require both the approval of the Board of Directors and the stockholders on record.

Suggested Answer:

a. It only requires the approval of the Board of Directors of BBB Corporation. (BAR 2012)

NB Alternative answer is b because generally a corporation can not guarantee the obligation of another even though it is a wholly-owned subsidiary unless the articles of incorporation allows it.

i. Doctrine of Apparent Authority

2. Specific Powers, Theory of Specific Capacity

a. Power to Extend or Shorten Corporate Term

The corporate term of a stock corporation is that which is stated in its Articles of Incorporation. It may be extended or shortened by an amendment of the Articles when approved by majority of its Board of Directors and:

- a. Approved and ratified by at least 2/3 of all stockholders
- b. Approved by at least 2/3 of the stockholders representing the outstanding capital stock.
- c. Ratified by at least 2/3 of all stockholders.
- d. Ratified by at least 2/3 of the stockholders representing the outstanding capital stock.

Suggested Answer:

d. Ratified by at least 2/3 of the stockholders representing the outstanding capital stock. (BAR 2011)

NB: Under Section 11 of the Revised Corporation Code "A corporation shall have perpetual existence unless its articles of incorporation provides otherwise.

T Corp. has a corporate term of 20 years under its Articles of Incorporation or from June 1, 1980 to June 1, 2000. On June 1, 1991 it amended its Articles of Incorporation to extend its life by 15 years from June 1, 1980 to June 1, 2015. The SEC approved this amendment. On June 1, 2011, however, T Corp. decided to shorten its term by 1 year or until June 1, 2014. Both the 1991 and 2011 amendments were approved by majority vote of its Board of Directors and ratified in a special meeting by its stockholders representing at least 2/3 of its outstanding capital stock. The SEC, however, disapproved the 2011 amendment on the ground that it cannot be made earlier than 5 years prior to the expiration date of the corporate term, which is June 1, 2014. Is this SEC disapproval correct?

- a. No, since the 5-year rule on amendment of corporate term applies only to extension, not shortening, of term.
- b. Yes, any amendment affecting corporate term cannot be made earlier than 5 years prior to the corporation's expiration date.

- c. No, since a corporation can in fact have a corporate life of 50 years.
- d. Yes, the amendment to shorten corporate term cannot be made earlier than 5 years prior to the corporation's expiration date.

a. No, since the 5-year rule on amendment of corporate term applies only to extension, not shortening, of term. (BAR 2011)

NB: Under Section 11 of the Revised Corporation Code "A corporate term for a specific period may be extended or shortened by amending the articles of incorporation: Provided, That no extension may be made earlier than three (3) years prior to the original or subsequent expiry date(s) unless there are justifiable reasons for an earlier extension as may be determined by the Commission: Provided, further, That such extension of the corporate term shall take effect only on the day following the original or subsequent expiry date(s)."

a. Power to Increase or Decrease Capital Stock or Incur, Create, Increase Bonded Indebtedness

If ABC Corporation will increase its authorized capital stock, the Corporation Code requires—

- a. The approval of the majority of the Board of Directors only;
- b. The approval of the majority of the stockholders and the Board of Directors;
- c. The approval of 2/3 of the shareholders of the outstanding capital stock as well as the approval of the SEC;
- d. The approval of the majority of the Board of Directors and approval of the shareholders holding 2/3 share of the outstanding capital stock.

Suggested Answer:

Examinees should be given full credit for whatever answer they gave as the question is vague. (BAR 2012)

c. Power to Deny Pre-Emptive Rights

ABC Corp. increased its capital stocks from P10 M to P15 M and, in the process, issued 1,000 new shares divided into Common Shares "B" and common shares "C". T, a stockholder owning 500 shares, insists on buying the newly issued shares through a right of pre-emption. The company claims, however, that its Bylaws deny T any right of pre-emption. Is the corporation correct?

- a. No, since the by-laws cannot deny a shareholder his right of preemption.
- b. Yes, but the denial of his pre-emptive right extends only to 500 shares.
- c. Yes, since the denial of the right under the By-laws is binding on T.

d. No, since pre-emptive rights are governed by the articles of incorporation.

Suggested Answer:

a. No, since the by-laws cannot deny a shareholder his right of pre-emption. (BAR 2011)

d. Power to Sell or Dispose of Corporate Assets

e. Power to Acquire Own Shares

ABC Holdings Company, a Hong Kong company, owns 10% of XYZ Bank. Because of the peace and order situation in the Philippines, ABC Holding Company wanted to sell its shareholdings in XYZ Bank. Unfortunately, nobody is interested to buy a 10% shareholdings in a bank. The board of directors of XYZ Bank thought that it would be a good idea to buy back the shares owned by ABC Holding Company. Which statement is most accurate?

- a. Buying back the shares by XYZ Bank is absolutely not allowed;
- b. Buying back the shares may be allowed provided it is with the approval of the Monetary Board and disposed of within 6 months;
- c. Buying back the shares may be allowed provided such shares will be disposed of within 10 years;
- d. Buying back the shares may be done anytime provided the Board of Directors will approve the same.

Suggested Answer:

b. Buying back the shares may be allowed provided it is with the approval of the Monetary Board and disposed of within 6 months. (BAR 2012)

f. Power to Invest Corporate Funds in Another Corporation or Business

g. Power to Declare Dividends

DEF Corporation has retained surplus profits in excess of 100% of its paid in capital stock. However, it is unable to declare dividends, because it had entered into a loan agreement with a certain creditor wherein the declaration of dividends is not allowed without the consent of such creditor. If DEF Corporation cannot obtain this consent; will it be justified in not declaring dividends to its stockholders? Explain. (2015)

Suggested Answer:

Yes. As a general rule, Stock corporations are prohibited from retaining surplus profits in excess of 100% of their paid-in capital stock. However, Stock Corporations are allowed to retain surplus profits in excess of 100 of their paid-in capital stock when the corporation is prohibited under any loan agreement with any financial institution or creditor; whether local or foreign, from declaring dividends without the consent of the

creditor and such consent has not been secured. This one of the execptions provided under Section 43 of the Corporation Code.

The rule is that no stock dividend shall be issued without the approval of stockholders representing at least 2/3 of the outstanding capital stock at a regular or special meeting called for the purpose. As to other forms of dividends:

- a. A mere majority of the entire Board of Directors applies.
- b. A mere majority of the quorum of the Board of Directors applies.
- c. A mere majority of the votes of stockholders representing the outstanding capital stock applies.
- d. The same rule of 2/3 votes applies.

Suggested Answer:

a. A mere majority of the quorum of the Board of Directors applies. (BAR 2011)

ABC Corporation declared stock dividends to its stockholders. The stock dividends were approved by the Board of Directors of ABC Corporation. In the subsequent year, however, the Board again approved the redemption of all stock dividends and to pay the shareholdings in cash. Which statement is most accurate?

- a. The redemption of the stock dividends can be validly approved but hr Board without any conditions;
- b. The redemption of stock dividends may only be allowed if there are sufficient earnings and should not be violative of the trust fund doctrine;
- c. The redemption of the shares may be taken from the existing property and other assets of the corporation;
- d. None of the above.

Suggested Answer:

Examinee should be giver full credit for whatever answer they gave as the question is vague. (BAR 2012)

On September 15, 2007, XYZ Corporation issued to Paterno 800 preferred shares with the following terms:

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

- a. The right to receive a quarterly dividend of 1% cumulative participating;
- b. These shares may be redeemed, by drawing of lots, at any time after 2 years from date of issue, at the option of the Corporation; $x \times x$."

Today, Paterno sues XYZ Corporation for specific performance, for the payment of dividends on, and to compel the redemption of, the preferred shares, under the

terms and conditions provided in the stock certificates. Will the suit prosper? Explain.

Suggested Answer:

No. the suit will not prosper. Paterno cannot compel XYZ Corporation to pay dividends, which have to be declared by the Board of Directors and the latter cannot do so, unless there are sufficient unrestricted retained earnings. Otherwise, the corporation will be forced to use its capital to make said payments in violation of the trust fund doctrine. Likewise, redemption of shares cannot be compelled. While the certificate allows such redemption, the option and discretion to do so are clearly vested in the Corporation. (BAR 2009)

TRUE OR FALSE. Dividends on shares of stock can only be declared out of unrestricted retained earnings of the corporation.

Suggested Answer:

True. Dividends on shares of stock of a corporation, whether cash dividend or stock dividend, can be validly declared only out of unrestricted retained earnings. It cannot be declared out of the capital. Otherwise, such declaration of dividend will violate the trust fund doctrine. (BAR 2009)

- h. Power to Enter Into Management Contract
- i. Ultra Vires Acts
- a. Applicability of Ultra Vires Doctrine
- b. Consequences of Ultra Vires Acts
- 3. How Exercised
 - a. By the Corporation

When is there an ultra vires act on the part of (a) the corporation.

SUGGESTED ANSWER

Under Sec. 45 of the Corporation Code, no corporation shall possess or exercise any corporate power except those conferred by the Code or by its articles of incorporation and except such as are necessary or incidental to the exercise of the powers so conferred. When the corporation does an act or engages in an activity which is outside of its express, implied or incidental powers set out in its articles of incorporation, the act is deemed to be *ultra vires*. (BAR 2009)

- b. By the Shareholders
- c. By the Board of Directors

X Corp., whose business purpose is to manufacture and sell vehicles, invested its funds in Y Corp., an investment firm, through a resolution of its Board of

Directors. The investment grew tremendously on account of Y Corp's excellent business judgment. But a minority stockholder in X Corp. assails the investment as ultra vires. Is he right and, if so, what is the status of the investment?

- a. Yes, it is an ultra vires act of the corporation itself but voidable only, subject to stockholder's ratification.
- b. Yes, it is an ultra vires act of its Board of Directors and thus void.
- c. Yes, it is an ultra vires act of its Board of Directors but voidable only, subject to stockholders' ratification.
- d. Yes, it is an ultra vires act of the corporation itself and, consequently, void.

Suggested Answer:

c. Yes, it is an ultra vires act of its Board of Directors but voidable only, subject to stockholders' ratification. (BAR 2011)

When is there an ultra vires act on the part of (b) the board of directors.

Suggested Answer:

When the Board engages in an activity or enters into a contract without the ratificatory vote of the stockholders in those instances where the Corporation Code so requires such ratificatory vote, such as when the corporation is made to invest in another corporation or engage in a business which is not in pursuit of its primary purpose, the board resolution not ratified by stockholders owning or representing at least 2/3 of the outstanding capital stock would make the transaction void, as being *ultra vires*. (BAR 2009)

d. By the Officers

Define: Doctrine of apparent authority. (2015)

Suggested Answer:

By the doctrine of apparent authority, the corporation will be estopped from denying the agent's authority if it knowingly permits one of its officers or any other agent to act within the scope of an apparent authority and it holds him out to the public as possessing the power to do those acts (Advance Paper Corporation v. Arma Traders Corporation, GR No. 176897, Dec. 11, 2013)

Y, as President of and in behalf of AAA Corporation, as a way to accommodate X, one of its stockholders, endorsed the check issued by X. Which statement is most accurate?

- a. It is an ultra vires act;
- b. It is a valid indorsement;
- c. The corporation will be held liable to any holder in due course;
- d. It is an invalid indorsement.

Suggested Answer:

- a. It is an ultra vires act.
- d. It is a valid indorsement. (BAR 2012)

When is there an ultra vires act on the part of (c) the corporate officers.

Suggested Answer:

When a corporate officer enters into a contract on behalf of the corporation without having been so expressly or impliedly authorized by the board of Directors, even when the act or contract falls within the corporation's express, implied or incidental power, then the unauthorized act of the corporate officer is deemed to be *ultra vires*. (BAR 2009)

4. Trust Fund Doctrine

Define: Trust fund doctrine. (2015)

Suggested Answer:

By the trust fund doctrine subscriptions to the capital stock of a corporation constitute a fund to which the creditors have the right to look for satisfaction of their claims. The scope of the doctrine encompasses not only the capital stock but also other property and assets generally regarded in equity as a trust fund for the payment of corporate debts (Halley v. Printwell, GR No. 157549, May 30, 2011; Ong v. Tiu, 401 SCRA 1).

G. Board of Directors and Trustees

Section 38 of the SRC defines an independent director as a person who must not have a relation with the corporation which would interfere with his exercise of independent judgment in carrying out the responsibilities of a director. To ensure independence therefore, he must be—

- a. Nominated and elected by the entire shareholders:
- b. Nominated and elected by the minority shareholders;
- c. Nominated and elected by the majority shareholders;
- d. Appointed by the board.

Suggested Answer:

c. Nominated and elected by the majority shareholders. (BAR 2012)

1. Doctrine of Centralized Management

What vote is needed to consider every decision to be valid corporate act?

- a. A majority of the directors present at the meeting
- b. 2/3 of the directors present at the meeting
- c. A majority of the directors present at the meeting at which there is a quorum

d. 2/3 of the directors present at the meeting at which there is a quorum

Suggested Answer:

c. A majority of the directors present at the meeting at which there is a quorum (BAR 2014)

2. Business Judgment Rule

X, the President of ZZZ Corporation, was authorized by the Board of Directors of ZZZ Corporation to obtain a loan from YYY Bank and to sign documents in behalf of the corporation. X personally negotiated for the loan and got the loan at very low interest rates. Upon maturity of the loan, ZZZ Corporation was unable to pay. Which statement is most accurate?

- a. Because X was personally acting in behalf of the Corporation, he can be held personally liable;
- b. X, as President, cannot be personally held liable for the obligation of the corporation even though he signed all the loan documents, because the loan was authorized by the Board;
- c. YYY Bank can choose as to who it wants to hold liable for the loan;
- d. If ZZZ Corporation cannot pay, X can be held subsidiarily liable.

Suggested Answer:

b. X, as President, cannot be personally held liable for the obligation of the corporation even though he signed all the loan documents, because the loan was authorized by the Board. (BAR 2012)

3. Tenure, Qualifications and Disqualifications of Directors or Trustees

Your client Dianne approaches you for legal advice on putting up a medium-sized restaurant business that will specialize in a novel type of cuisine. As Dianne feels that the business is a little risky, she wonders whether she should use a corporation as the business vehicle, or just run it as a single proprietorship. She already has an existing corporation that is producing meat products profitably and is also considering the alternative of simply setting up the restaurant as a branch office of the existing corporation.

If you advise your client to use a corporation, what officer position must the corporation at least have?

Suggested Answer:

The corporation must have at least 5 directors. It must also have a president, treasurer, and a secretary.

NB: Under the Revised Corporation Code, a One Person Corporation with a single stockholder is already allowed.

What particular qualifications, if any, are these officers legally required to possess under the Corporation Code?

Suggested Answer:

Every director must own at least 1 share of the capital stock of the corporation, which must be recorded in his name on the books of the corporation, and a majority of the directors must be residents of the Philippines.

The president must also be a director. The secretary must be a resident and citizen of the Philippines. (BAR 2010)

NB: Under the Revised Corporation Code, Treasurer is required to be a resident of the Philippines.

X is a director in T Corp. who was elected to a 1-year term on Feb. 1, 2010. On April 11, 2010, X resigned and was replaced by R, who assumed as director on May 17, 2010. On Nov. 21, 2010, R died. S was then elected in his place. Until which time should S serve as director?

- a. April 11, 2011
- b. Feb. 1, 2011
- c. May 17, 2011
- d. Nov. 21, 2011

Suggested Answer:

B. Feb. 1, 2011 (BAR 2011)

X is a Filipino immigrant residing in Sacramento, California. Y is a Filipino residing Quezon City. Z is a resident alien residing in Makati City. GGG Corporation is a domestic corporation—40% owned by foreigners and 60% owned by Filipinos, with T as authorized representative. CCC Corporation is a foreign corporation registered with the Philippines SEC, KKK Corporation is a domestic corporation (100%) Filipino owned. S is a Filipino, 16 years of age, and daughter of Y.

Who are qualified to become members of the board of directors of the corporation?

Suggested Answer:

X, Y, Z and T could be directors (subject to the residency requirement mentioned in (a) above and any nationality requirement under the law governing the business of the corporation) but not GGG Corporation, CCC Corporation, and KKK Corporation as they are not natural persons. However, the aforementioned corporations could have their respective representatives nominated and possibly elected as directors by the stockholders. Each director must own at least one share of the capital stock of the corporation. (BAR 2012)

4. Elections

The term 1 year of the Board of Directors of AAA Corporation expired last February 15, 2012. No new election of the Board of Directors was called, hence, the existing members of the Board continue as Directors in hold over capacity. Which statement is most accurate?

- a. This is allowed provided there is a valid and justifiable reason for not calling for an election of the new members of the Board;
- b. This is not allowed because the term of the directors must only be for a period of 1 year;
- c. The positions of the members of the Board of Directors will be automatically declared vacant;
- d. Acting as member of the Board of Directors in a hold over capacity must be ratified by the stockholders.

Suggested Answer:

a. This is allowed provided there is a valid and justifiable reason for not calling for an election of the new members of the Board. (BAR 2012)

In the November 2010 stockholder's meeting of Greenville Corporation, 8 directors were elected to the board. The directors assumed their posts in January 2011. Since no stockholders' meeting was held in November 2011, the 8 directors served in a holdover capacity and thus continued discharging their powers.

In June 2012, 2 of Greenville Corporation's directors—Director A and Director B—resigned from the board. Relying on Section 29 of the Corporation Code, the remaining 6 directors elected 2 new directors to fill in the vacancy caused by the resignation of Directors A and B.

Stockholder X questioned the election of the new directors, initially, through a letter-complaint addressed to the board, and later (when his letter-complaint went unheeded), through a derivative suit filed with the court. He claimed that the vacancy in the board should be filled up by the vote of the stockholders of Greenville Corporation. Greenville Corporation's directors defended the legality of their action, claiming as well that Stockholder X's derivative suit was improper.

Rule on the issued raised.

Suggested Answer:

The remaining directors cannot elect new directors to fill in the two vacancies. The board of directors may fill up vacancy only if the ground is not due to expiration of term, removal or increase in the number of board seats. In this case, the term of the two directors expired after 1 year. They remained in office in a hold-over capacity only until their resignation. The hold-over period is not part of their term. The vacancies should be filled up by election by the stockholders.

The derivative suit was improper. In a derivative suit, the corporation, not the individual stockholder, must be the aggrieved party and that the stockholder is suing on behalf of the corporation. What stockholder X is asserting is his individual right as a stockholder to elect the two directors. The case partakes more of an election contest under the rules on intra-corporate controversy. (BAR 2013)

a. Cumulative Voting/Straight Voting

EFG Foundation, Inc., a non-profit organization, scheduled an election for its sixmember Board of Trustees. X, Y and Z, who are minority members of the foundation, wish to exercise cumulative voting in order to protect their interest, although the Foundation's Articles and By-laws are silent on the matter. As to each of the three, what is the maximum number of votes that he/she can cast?

- a. 6
- b. 9
- c. 12
- d. 3

Suggested Answer:

a. 6 (BAR 2011)

In elections for the Board of Trustees of non-stock corporations, members may cast as many votes as there are trustees to be elected but may not cast more than one vote for one candidate. This is true-

- a. Unless set aside by the members in a plenary session.
- b. In every case even if the Board of Trustees resolves otherwise.
- c. Unless otherwise provided in the Articles of Incorporation or in the Bylaws.
- d. In every case even if the majority of the members decide otherwise during the elections.

Suggested Answer:

c. Unless otherwise provided in the Articles of Incorporation or in the By-laws. (BAR 2011)

b. Quorum

To constitute a quorum for the transaction of corporate business, only a majority of the number of Board of Directors is required:

- a. As fixed by the corporate by-laws
- b. As fixed in the articles of incorporation
- c. Actually serving in the board
- d. Actually serving in the board but constituting a quorum

Suggested Answer:

b. As fixed in the articles of incorporation (BAR 2014)

5. Removal

Henry is a board director in XYZ Corporation. For being the "fiscalizer" in the Board, the majority of the board directors want him removed and his shares sold at auction, so he can no longer participate even in the stockholders' meetings. Henry approaches you for advice on whether he can be removed as board director and stockholder even without cause. What is your advice? Explain "amotion" and the procedure in removing a director. (2016 Bar)

SUGGESTED ANSWER

No, Henry cannot be removed by his fellow directors. The power to remove belongs to the stockholders and the SEC. Moreover, the removal has to be with cause because it is intended to deprive minority stockholders of the right of representation.

Amotion is the premature ousting of a director or officer from his post in the corporation

Any director or trustee of a corporation may be removed from office by vote of the stockholders holding or representing at least two-thirds (2/3) of the outstanding capital stock, or in a nonstock corporation, by a vote of at least two-thirds (2/3) of the member entitled to vote: Provided, That such removal shall take place either at a regular meeting of the corporation or at a special meeting called for the purpose, and in either case, after previous notice to stockholders or members of the corporation of the intention to propose such removal at the meeting.

The Commission shall, motu propio or upon verified complaint, and after due notice and hearing, order the removal of a director or trustee elected despite the disqualification, or whose disqualification arose or is discovered subsequent to an election.

A law was passed disqualifying former members of Congress from sitting in the Board of Directors of GOCC. Because of this, the Board of Directors of ABC Corp., a GOCC, disqualified C, a former Congressman, from continuing to sit as one of its members. C objected, however, insisting that under the Corporation Code members of the board of directors of corporations may only be removed by vote of stockholders holding 2/3 of its outstanding capital stock in a regular or special meeting called for that purpose. Is C correct?

- a. Yes, since the new law cannot be applied to members of the board of directors already elected prior to its passage.
- b. No, since the disqualification takes effect by operation of law, it is sufficient that he was declared no longer member of the board.
- c. Yes, since the provisions of the Corporation Code applies as well to GOCC.
- d. No, since the board has the power to oust him even without the new law.

Suggested Answer:

b. No, since the disqualification takes effect by operation of law, it is sufficient that he was declared no longer member of the board. (BAR 2011)

6. Filling of Vacancies

7. Compensation

8. Fiduciaries Duties and Liability Rules

The Board of Directors of XYZ Corp. unanimously passed a resolution approving the taking of steps that in reality amounted to willful tax evasion. On discovering this, the government filed tax evasion charges against the company's members of the board of directors. The directors invoked the defense that they have no personal liability, being mere directors of a fictional being. Are they correct?

- a. No, since as a rule only natural persons like the members of the board of directors can commit corporate crimes.
- b. Yes, since it is the corporation that did not pay the tax and it has a personality distinct from its directors.
- c. Yes, since the directors officially and collectively performed acts that are imputable only to the corporation.
- d. No, since the law makes directors of the corporation solidarily liable for gross negligence and bad faith in the discharge of their duties.

Suggested Answer:

- d. No, since the law makes directors of the corporation solidarily liable for gross negligence and bad faith in the discharge of their duties. (BAR 2011)
- A, B, C, D, E, are all duly elected members of the Board of Directors of XYZ Corporation. F, the general manager, entered into a supply contract with an American firm. The contract was duly approved by the Board of Directors. However, with the knowledge and consent of F, no deliveries were made to the American firm. As a result of the non-delivery of the promised supplies, the American firm incurred damages. The American firm would like to file a suit for damages. Can the American firm sue:
 - a. The members of the Board of Directors individually, because they approved the transaction?
 - b. The corporation?
 - c. F, the general manager, personally, because the non-delivery was with his knowledge and consent?
 - d. Explain the rules on liabilities of a corporation for the act of its corporation officers and the liabilities of the corporate officers and Board of Directors of a corporation acting in behalf of the corporation.

Suggested Answer:

a. No. in approving the transaction, the directors were not acting in their personal capacities but rather on behalf of XYZ Corporation exercising the powers of the

corporation and conducting its business. The problem contains no facts that would indicate that the directors acted otherwise.

- b. Yes. The Board approved the supply contract and the General Manager entered into the contract, both of them acting on behalf of the XYZ Corporation.
- c. Yes, F could be sued in his personal capacity because he knowingly consented to the non-delivery of the promised supplies contrary to the contract that was duly approved by the Board of Directors. The problem does not indicate any circumstance that would excuse or favorably explain the action of F.
- d. A corporation would be liable for the acts of its Board of Directors and officers if the said acts were performed by them in accordance with the powers granted to them under the Corporation Code, the articles of incorporation and by-laws of the corporation, the laws and regulations governing the business of, or otherwise applicable to, the corporation, and, in the case of officers, the resolution approved by the Board of Directors.

As the directors have a personality separate from that of the corporation, they would be personally liable only if they acted willfully and knowingly vote for or assent to a patently unlawful act of the corporation, or when they are guilty of gross negligence or bad faith in directing the affairs of the corporation, or when they acquire any personal or pecuniary interest in conflict with their duty as directors, which acts result in damages to the corporation, its stockholders or other persons, when they agree to hold themselves personally and solidarily liable with the corporation, or when they are made, by a specific provision of law, to personally answer for the corporate action. (BAR 2012)

- 9. Responsibility for Crimes
- 10. Inside Information
- 11. Contracts
 - a. By Self-Dealing Directors with the Corporation
 - b. Between Corporations with Interlocking Directors

The Corporation Code sanctions a contract between two or more corporations which have interlocking directors, provided there is no fraud that attends it and it is fair and reasonable under the circumstances. The interest of an interlocking director in one corporation may be either substantial or nominal. It is nominal if his interest:

- a. Does not exceed 25% of the outstanding capital stock.
- b. Exceeds 25% of the outstanding capital stock.
- c. Exceeds 20% of the outstanding capital stock.
- d. Does not exceed 20% of the outstanding capital stock.

Suggested Answer:

d. Does not exceed 20% of the outstanding capital stock. (BAR 2011)

c. Management Contracts

12. Officers and Executive Committee

X is a Filipino immigrant residing in Sacramento, California. Y is a Filipino residing Quezon City. Z is a resident alien residing in Makati City. GGG Corporation is a domestic corporation—40% owned by foreigners and 60% owned by Filipinos, with T as authorized representative. CCC Corporation is a foreign corporation registered with the Philippines SEC, KKK Corporation is a domestic corporation (100%) Filipino owned. S is a Filipino, 16 years of age, and daughter of Y.

- A. Who are qualified to act as Treasurer of the company?
- B. Who can be appointed Corporate Secretary?

Suggested Answer:

A. The Corporation Code does not impose any nationality or residency requirement in respect of the Treasurer. Any such requirement or any other reasonable requirement may be adopted by the corporation and reflected in its by-laws, or required by the law(s) governing the business of the corporation or a law of general application (e.g., the Anti-Dummy Law which applies to all nationalized businesses). Accordingly, anybody with the qualifications required under the by-laws of the corporation or under the law(s) governing the business of the corporation, could be elected Treasurer by the Board of Directors. However, the Treasurer could not be President at the same time.

B. The Secretary is required to be both a resident and a citizen of the Philippines. (BAR 2012)

X, the President of ZZZ Corporation, was authorized by the Board of Directors of ZZZ Corporation to obtain a loan from YYY Bank and to sign documents in behalf of the corporation. X personally negotiated for the loan and got the loan at very low interest rates. Upon maturity of the loan, ZZZ Corporation was unable to pay. Which statement is most accurate?

- a. Because X was personally acting in behalf of the Corporation, he can be held personally liable;
- b. X, as President, cannot be personally held liable for the obligation of the corporation even though he signed all the loan documents, because the loan was authorized by the Board;
- c. YYY Bank can choose as to who it wants to hold liable for the loan;
- d. If ZZZ Corporation cannot pay, X can be held subsidiarily liable.

Suggested Answer:

b. X, as President, cannot be personally held liable for the obligation of the corporation even though he signed all the loan documents, because the loan was authorized by the Board. (BAR 2012)

Pursuant to its By-Laws, Soei Corporation's Board of Directors created an Executive Committee to manage the affairs of the corporation in between board meetings. The Board of Directors appointed the following members of the Executive Committee: the President, Sarah L; the Vice-President, Jane L; and a third member from the board, Juan Riles. On December 1, 2013, the Executive Committee, with Sarah L and Jane L present, met and decided on the following matters:

- a. Purchase of a delivery van for use in the corporation's retail business;
- b. Declaration and approval of the 13th month bonus;
- c. Purchase of an office condominium unit at the Fort; and
- d. Declaration of P10.00 per share cash dividend.

Are the actions of the Executive Committee valid?

Suggested Answer:

The action of the Executive Committee with regard to the purchase of a delivery van for use in the corporation's retail business, declaration and approval of the 13th month bonus, purchase of an office condominium unit at the Fort, and the declaration of P10.00 per share cash dividend is valid, as such matters were taken by a majority vote of all its members, on such matters within the competence of the board and as delegated to it in the by-laws. (BAR 2014)

NB The better answer is that the actions of the Executive Committee on all items are valid except declaration of cash dividends

Guetze and his wife have 3 chidren: Neymar, 25, who is now based in Rio de Janeiro, Brazil; Muelter, 23, who has migrated to Munich, Germany; and James, 21, who resides in Bogota, Colombia. Neymar and Muelter have since renounced their Philippine citizenship in favor of their country of residence. Nearing 70 years old, Guetze decided to incorporate his business in Binondo, Manila. He asked his wife and 3 children to act as incorporators with 1 share of stock each, while he owned 999,996 shares of the 1,000,000 shares of the capital stock.

Being the control freak and micro-manager that he is, Guetze asked you—his astute legal adviser— if he can serve as Chairman of the Board of Directors, as President, and as General Manager of the corporation, all at the same time. Please advise Guetze.

Suggested Answer:

Yes, Guetze can serve as Chairman, as President, and as General Manager of the corporation all at the same time. Section 25 of the Corporation Code provides that "two or more positions may be held concurrently by the same person, except that no one shall act as president and secretary or as president and treasurer at the same time." Such case does not fall within the exception under the aforesaid Section. (BAR 2014)

13. Meetings

- A. Regular or Special
 - i. When and Where
 - ii. Notices
- **B. Who Presides**
- C. Quorum
- D. Rule on Abstention
- H. Stockholders and Members
 - 1. Rights of a Stockholder and Members
 - a. Doctrine of Equality of Shares
- 2. Participation in Management
 - a. Proxy
 - b. Voting Trust
 - c. Cases When Stockholders' Action is Required
 - i. By a Majority Vote
 - ii. By a Two-Thirds Vote
 - iii. By Cumulative Voting
- 3. Proprietary Rights
 - a. Right to Dividends

Ace Cruz subscribed to 100,000 shares of stock of JP Development Corporation, which has a par value of P1 per share. He paid P25,000 and promised to pay the balance before December 31, 2008. JP Development Corporation declared a cash dividend on October 15, 2008, payable on December 1, 2008.

For how many shares is Ace Cruz entitled to be paid cash dividends? Explain.

Suggested Answer:

Ace is entitled to be paid cash dividends for 100,000 shares of stock. Although he has not fully paid for his shares of stock, he is not delinquent and is therefore entitled to all the rights of a stockholder. (BAR 2008)

On September 15, 2007, XYZ Corporation issued to Paterno 800 preferred shares with the following terms:

- "The Preferred Shares shall have the following rights, preferences, qualifications, and limitations, to wit:
- 3. The right to receive a quarterly dividend of 1% cumulative participating;
- 4. These shares may be redeemed, by drawing of lots, at any time after 2 years from date of issue, at the option of the Corporation; $x \times x$."

Today, Paterno sues XYZ Corporation for specific performance, for the payment of dividends on, and to compel the redemption of, the preferred shares, under the terms and conditions provided in the stock certificates. Will the suit prosper? Explain.

Suggested Answer:

No. the suit will not prosper. Paterno cannot compel XYZ Corporation to pay dividends, which have to be declared by the Board of Directors and the latter cannot do so, unless there are sufficient unrestricted retained earnings. Otherwise, the corporation will be forced to use its capital to make said payments in violation of the trust fund doctrine. Likewise, redemption of shares cannot be compelled. While the certificate allows such redemption, the option and discretion to do so are clearly vested in the Corporation. (BAR 2009)

b. Right of Appraisal

Santorini Corporation (Santorini) was in dire straits. In order to firm up its financial standing, it agreed to entertain the merger and takeover offer of Proficient Corporation (Proficient), the leading company in their line of business. Erica, the major stockholder of Santorini, strongly opposed the merger and takeover. The matter of the merger and takeover by Proficient was included in the agenda of the next meeting of Santorini's Board of Directors. However, owing to Erica's serious illness that required her to seek urgent medical treatment and care in Singapore, she failed to attend the meeting and as consequently unable to cast her vote. The Board of Directors approved the merger and takeover. At the time of the meeting, Santorini had been in the red for a number of years owing to its recurring business losses and reverses.

Erica seeks your legal advice regarding her right as a stockholde opposed to the corporate action. Explain your answer. (4%) (2017 BAR)

SUGGESTED ANSWER:

Erica may exercise her appraisal right. Appraisal right is the right of the stockholder to demand the payment of the fair value of his shares after dissenting from a corporate act in the cases specified by law. Merger is one of those insiances (Section 81 of the Corporation Code). It is imperative, however, that she attends the stockholders' meeting or files her written dissent, and otherwise, she cannot exercise such right.

In case of disagreement between the corporation and a withdrawing stockholder who exercises his appraisal right regarding the fair value of his shares, a three-member group shall by majority vote resolve the issue with finality. May the wife of the withdrawing stockholder be named to the threemember group?

- a. No, the wife of the withdrawing shareholder is not a disinterested person.
- b. Yes, since she could best protect her husband's shareholdings.

- c. Yes, since the rules do not discriminate against wives.
- d. No, since the stockholder himself should sit in the three-member group.

a. No, the wife of the withdrawing shareholder is not a disinterested person. (BAR 2011)

The rule is that valuation of the shares of a stockholder who exercises his appraisal rights is determined as of the day prior to the date on which the vote was taken. This is true-

- a. Regardless of any depreciation or appreciation in the share's fair value.
- b. Regardless of any appreciation in the share's fair value.
- c. Regardless of any depreciation in the share's fair value.
- d. Only if there is no appreciation or depreciation in the share's fair value.

Suggested Answer:

a. Regardless of any depreciation or appreciation in the share's fair value. (BAR 2011)

c. Right to Inspect

Sid used to be the majority stockholder and President of Excellent Corporation (Excellent). When Meridian Co., Inc. (Meridian), a local nglomerate, took over control and ownership of Excellent, it brought along its team of officers. Sid thus became a minority stockholder and a minority member of the Board of Directors.

Excellent, being the leading beverage manufacturer in the country, became the monopoly when Meridian's own beverage business was merged th Excellent's, thereby making Excellent virtually the only beverage manufacturer in the country.

Left out and ignored by the management, Sid became a fiscalizer of sorts, questioning during the Board meetings the direction being pursued by Excellent's officers. Ultimately, Sid demanded the inspection of the books and other corporate records of Excellent. The management refused to comply, saying that his right as a minority stockholder has been much reduced.

State under what conditions Sid may properly assert his right to inspect the books and other corporate records of Excellent. Explain your answer. (3%) (2017 BAR)

SUGGESTED ANSWER:

Sid may properly assert his right to inspect the books and other corporate records of Excellent under the following conditions:

1. The purpose of his inspection is legitimate and germane to his interest as a stockholder;

- 2. The right should be exercised during reasonable hours in business day;
- 3. He has not improperly used any information secured in previous examination (Section 74 of the Corporation Code; Terelay Investment v. Yulo, G.R. No. 160924, August 5, 2015, 765 SCRA I).

d. Pre-Emptive Right

So that ABC Corporation could venture into more projects, it needed to raise funds by issuing new shares to increase its capitalization. X, Y, Z, J and G are the 5 existing shareholders of the company. They hold 20% each. How will the additional shares be divided among the existing shareholders?

- a. The existing shareholders can subscribe to the new shares equivalent to their existing shareholdings because the Corporation Code provides that each of the existing stockholders will have preemptive rights to the extent of their existing shareholdings;
- b. The existing shareholders' preemptive rights is equivalent to the percentage that they want;
- c. Each of the existing shareholder can exercise their right of first refusal against each other;
- d. Preemptive rights and right of first refusal are one and the same.

Suggested Answer:

a. The existing shareholders can subscribe to the new shares equivalent to their existing shareholdings because the Corporation Code provides that each of the existing stockholders will have preemptive rights to the extent of their existing shareholdings. (BAR 2012)

e. Right to Vote

The By-laws of the ABC Corporation is silent as to when a stockholder can be qualified to attend the meeting of the stockholders. The Corporate Secretary sent out the notice of the stockholders meeting 2 days before the meeting and at that time X was not yet a stockholder. On the day of the meeting, however, X became a shareholder which was duly recorded in the stock and transfer book. Which statement is most accurate?

- a. X is a stockholder of ABC Corporation as of the time of meeting of the stockholders for the purpose of electing the members of the board;
- b. X is not qualified to elect members of the board because at the time the notice of the meeting was sent, she was not yet a stockholder;
- Qualifications as to who are considered as stockholders on record for purposes of being able to elect members of the board are to be determined by the By-laws alone;
- d. None of the above.

a. X is a stockholder of ABC Corporation as of the time of meeting of the stockholders for the purpose of electing the members of the board. (BAR 2012)

Dennis subscribed to 10,000 shares of XYZ Corporation with a par value of 100 per share. However, he paid only 25% of the subscription or P250,000. No call has been made on the unpaid subscription.

How many shares is Dennis entitled to vote at the annual meeting of the stockholders of XYZ?

- a. 10,000 shares;
- b. 2,500 shares;
- c. 100 shares;
- d. 0 shares:
- e. None of the above.

Suggested Answer:

a. 10,000 shares (BAR 2013)

f. Right of First Refusal

4. Remedial Rights

a. Individual Suit

- b. Representative Suit
- c. Derivative Suit

Royal Links Golf Club obtained a loan from a bank which is secured by a mortgage on a titled lot where holes 1, 2, 3 and 4 are located. The bank informed the Board of Directors (Board) that if the arrearages are not paid within thirty (30) days, it will extra-judicially foreclose the mortgage. The Board decided to offer to the members 200 proprietary membership shares, which are treasury shares, at the price of P175,000.00 per share even when the current market value is P200.000.00.

In behalf and for the benefit of the corporation, Peter, a stockholder, filed a derivative suit against the members of the Board for breach of trust for selling the shares at P25,000.00, lower than its market value, and asked for the nullification of the sales and the removal of the board members. Peter claims the Club incurred a loss of PS million. The Board presented the defense that in its honest belief any delay in the payment of the arrearages will be prejudicial to the Club as the mortgage on its assets will be foreclosed and the sale at a lower price is the best solution to the problem. Decide the suit and explain. (2016 Bar)

SUGGESTED ANSWER:

The derivative suit will not prosper. The complaint did not have all the elements of a derivative suit: a) exhaustion of intra-corporate remedies available under the articles of incorporation, by-laws, and rules and regulations governing the corporation to obtain the remedy the stockholder desires; b) it is not a nuisance suit; and c) appraisal right is not available (Ching v. Subic Bay Golf and Country Club, G.R. No. 174353. September 10, 2014)

ALTERNATIVE ANSWER:

The derivative suit will not prosper, because there was no wrongful act on the part of the board of directors. It falls under the business judgment rule since the board of directors passed the resolution in good faith to prevent the foreclosure on the mortgage on the assets of the corporation, the court cannot review the decision of the board of directors even if the selling price is less than the market value of the shares (Montelibano v. Bacolod Murcia Milling Company, G.R. No. L-15092, May 18, 1962)

X is a minority stockholder of CCC Corporation. Y is a member of the Board of Directors of CCC Corporation and at the same time he is the President. X believes that Y is mismanaging CCC Corporation hence, as a stockholder and in behalf of the other stockholders, he wanted to sue Y. which statement is most accurate?

- a. X can institute a derivative suit in behalf of himself as a stockholder;
- b. A derivative suit must be instituted in behalf of the corporation;
- c. Derivative suit is an exclusive remedy that X can institute;
- d. Derivative suit is not the remedy in this situation.

Suggested Answer:

b. A derivative suit must be instituted in behalf of the corporation. (BAR 2012)

In the November 2010 stockholder's meeting of Greenville Corporation, 8 directors were elected to the board. The directors assumed their posts in January 2011. Since no stockholders' meeting was held in November 2011, the 8 directors served in a holdover capacity and thus continued discharging their powers.

In June 2012, 2 of Greenville Corporation's directors—Director A and Director B—resigned from the board. Relying on Section 29 of the Corporation Code, the remaining 6 directors elected 2 new directors to fill in the vacancy caused by the resignation of Directors A and B.

Stockholder X questioned the election of the new directors, initially, through a letter-complaint addressed to the board, and later (when his letter-complaint went unheeded), through a derivative suit filed with the court. He claimed that the vacancy in the board should be filled up by the vote of the stockholders of Greenville Corporation. Greenville Corporation's directors defended the legality of their action, claiming as well that Stockholder X's derivative suit was improper.

Rule on the issued raised.

The remaining directors cannot elect new directors to fill in the two vacancies. The board of directors may fill up vacancy only if the ground is not due to expiration of term, removal or increase in the number of board seats. In this case, the term of the two directors expired after 1 year. They remained in office in a hold-over capacity only until their resignation. The hold-over period is not part of their term. The vacancies should be filled up by election by the stockholders.

The derivative suit was improper. In a derivative suit, the corporation, not the individual stockholder, must be the aggrieved party and that the stockholder is suing on behalf of the corporation. What stockholder X is asserting is his individual right as a stockholder to elect the two directors. The case partakes more of an election contest under the rules on intra-corporate controversy. (BAR 2013)

A, B, C, D and E were members of the 2003-2004 Board of Directors of FLP Corporation. At the election for the 2004-2005 Board of Directors, not one of them was elected. They filed in court a derivative suit on behalf of FLP Corporation against the newly-elected members of the Board of Directors. They questioned the validity of the election as it was allegedly marred by lack of quorum, and prayed for the nullification of the said election. The 2004-2005 Board of Directors moved to dismiss the complaint because the derivative suit is not proper. Decide.

Suggested Answer:

The derivative suit is not proper. The party-in-interest are the petitioners as stockholders, who were members of the 2003-2004 Board of Directors of FLP Corporation. The cause of action devolves on the petitioners, not on FLP Corporation, which did not have the right to vote. Hence, the complaint filed by A, B, C, D and E is a direct action by the petitioners, who were the members of the Board of Directors of the corporation before the election, against respondents, who are the newly-elected Board of Directors. Under the circumstances, the derivative suit filed by petitioners in behalf of FLP is improper. (BAR 2014)

Will the suit prosper? Why or why not?

Suggested Answer:

No. The suit will not prosper. There is no requisite demand on the officers and directors concerned. There is, therefore, no exhaustion of administrative remedies. (BAR 2009)

NB We have to add that under recent jurisprudence is dismissible unless the following are alleged in the complaint: a) the stockholder is suing on behalf of the corporation to enforce a corporate right or cause of action; b) plaintiff must be a stockholder at the time the cause of action accrued and at the time of filing unless the cause of action is continuing in nature in which case it is enough that he is a plaintiff at the time of filing; c) exhaustion of intra-corporate remedies to obtain the relief he desires under the corporation's articles of incorporation and by-laws; d) no appraisal right is available and

e) complaint is not a nuisance or harassment suit. The first two elements are alleged but the rest were not.

- 5. Obligation of a Stockholder
- 6. Meetings
 - a. Regular or Special
 i. When and Where

ii. Notice

At least 2/3 of the stockholders of Solar Corporation, meeting upon the recommendation of the Board of Directors, declared a 50% stock dividend during their annual meeting. The notice of the annual stockholders' meeting did not mention anything about a stock dividend declaration. The matter was taken up only under the item "Other Business" in the agenda of the meeting. C.K. Senwa, a stockholder, who received his copy of the notice but did not attend the meeting, subsequently learned about the 50% stock dividend declaration. He desires to have the stock dividend declaration cancelled and set aside, and wishes to retain your services as a lawyer for the purpose.

Will you accept the case? Discuss with reasons.

Suggested Answer:

I will not accept the case. Section 43 of the Corporation Code states that no stock dividend shall be issued without the approval of the stockholders representing not less than 2/3 of the outstanding capital stock at a regular or special meeting duly called for that purpose. Conformably with Section 50 of the Corporation Code, a written notice of the holding of the regular meeting sent to the shareholders will suffice. The notice itself specifies the said subject matter. (BAR 1990)

- a. Who Calls the Meetings
- b. Quorum

Triple A Corporation (Triple A) was incorporated in 1960, with 500 founder's shares and 78 common shares as its initial capital stock subscription. However, Triple A registered its stock and transfer books only in 1978, and recorded merely 33 common shares as the corporation's issued and outstanding shares.

In 1982, Juancho, the sole heir of one of the original incorporators filed apetition with the SEC for the registration of his property rights over 120 founder's shares and 12 common shares. The petition was supported by a copy of the Articles of Incorporation indicating the incorporators' initial capital stock subscription.

On May 6, 1992, a special stockholders' meeting was held. At this meeting, what would have constituted a quorum? Explain.

A quorum consists of the majority of the totality of the shares which have been subscribed and issued. Thus the quorum for such meeting would be 289 shares or a majority of the 576 shares issued and outstanding as indicated in the articles of incorporation. This includes the 33 common shares reflected in the stocks and transfer book, there being no mention or showing of any transaction effected from the time of Triple A's incorporation in 1960 up to the said meeting. (BAR 2009)

d. Minutes of the Meetings

I. Capital Structure

- 1. Subscription Agreements
- 2. Consideration for Stocks
- 3. Shares of Stock
- a. Nature of Stock

X owns 10,000 shares in Z Telecoms Corp. As he is in immediate need of money, he offered to sell all his shares to his friend, Y, at a bargain price. Upon receipt of the purchase price from Y, X proceeded to indorse in blank the certificates of shares and delivered these to Y. The latter then went to the corporate secretary of Z Telecoms Corp. and requested the transfer of the shares in his name. The corporate secretary refused since X merely indorsed the certificates in blank to Y. According to the corporate secretary, the certificates should have been specifically indorsed to the purchaser, Y. Was the corporate secretary justified in declining Y's request? Discuss. (2016 Bar)

Suggested Answer:

No, the corporate secretary is not justified in declining Y's request.

Under the Corporation Code, shares of stock covered by a stock certificate may be transferred by the delivery of the certificate endorsed by the stockholder-owner or his authorized representative or other person legally authorized to make the transfer. There is nowhere in the Code that requires that the endorsement be specifically in favour of the purchaser.

PR Corporation owns a beach resort with several cottages. Jaime, the President of PR, occupied one of the cottages for residential purposes. After Jaime's term expired, PR wanted to recover possession of the cottage. Jaime refused to surrender the cottage, contending that as a stockholder and former President, he has a right to possess and enjoy the properties of the corporation.

Is Jaime's contention correct? Explain.

Jaime's contention is not correct. Jaime may own shares of stock in PR Corporation but such ownership does not entitle him to the possession of any specific property of the corporation or a definite portion thereof. Neither is he a co-owner of a corporate property. Properties registered in the name of the corporation are owned by it as an entity separate and distinct from its stockholders.

Stockholders like Jaime only own shares of stock in the corporation. Such shares of stock do not represent specific corporate property. (BAR 1996)

b. Subscription Agreements

It is settled that neither par value nor book value is an accurate indicator of the fair value of a share of stock of a corporation. As to unpaid subscriptions to its shares of stock, as they are regarded as corporate assets, they should be included in the

- a. Capital value.
- b. Book value
- c. Par value.
- d. Market value.

Suggested Answer:

b. Book value. (BAR 2011)

The BIR assessed ABC Corp. for deficiency income tax for taxable year 2010 in the amount of P26,731,208.00, inclusive of surcharge and penalties.

The BIR can

- a. Run after the directors and officers of the ABC Corp. to collect the deficiency tax and their liability will be solidary;
- b. Run after the stockholders of ABC Corp. and their liability will be joint;
- c. Run after the stockholders of ABC Corp. and their liability will be solidary;
- d. Run after the unpaid subscriptions still due to ABC Corp., if any;
- e. None of the above choices is correct'

Suggested Answer:

d. Run after the unpaid subscriptions still due to ABC Corp., if any. (BAR 2013)

c. Consideration for Shares of Stock

d. Watered Stock i. Definition

What is "watered stock" and what is the legal consequence of the issuance of such stock? (2015)

Watered stocks are stocks issued for a consideration less than its par or issued value or for a consideration in any form other than cash, valued in excess of its fair value. Any director or officer of a corporation consenting to the issuance of watered stocks or who, having knowledge thereof, does not forthwith express his objection in writing and file the same with the corporate secretary shall be solidarily liable with the stockholder concerned to the corporation and its creditors for the difference between the fair value received at the time of issuance of the stock and the par or issued value of the same (Section 65 of the Corporation Code).

ii. Liability of Directors for Watered Stocks

iii. Trust Fund Doctrine for Liability for Watered Stocks

- e. Situs of the Shares of Stock
- f. Classes of Shares of Stock

The capital stock of ABC Corporation is divided into common shares and preferred shares. Preferred shares are preferred as to dividends and common shares are those shares which have the regular and ordinary attributes of a share of a corporation. Which statement is most accurate?

- a. This kind of classification may not be allowed or else it will violate the Doctrine of Equality of shares;
- b. Classifications of shares may be allowed for as long as it is clearly stated as such in the Articles of Incorporation of the Corporation;
- c. Classifications of shares is mainly for business purpose to attract investors:
- d. Classifications of shares may be allowed with the approval of the stockholders and the Board of Directors.

Suggested Answer:

d. Classifications of shares may be allowed for as long as it is clearly stated as such in the Articles of Incorporation of the Corporation. (BAR 2012

A corporation generally can issue both par value stock and no par value stock. These are all fixed in the Articles of Incorporation of the corporation. Which of the following corporations may not be allowed to issue no par value shares?

- a. Insurance companies;
- b. Banks:
- c. Trust Companies;
- d. All of the above.

Suggested Answer:

b. Banks. (BAR 2012)

NB The correct answer is all of the above

Preferred shares cannot vote on the proposal ______.

- a. To include other corporate officers in the corporation's by-laws;
- b. To issue corporate bonds;
- c. All of the above;
- d. None of the above.

Suggested Answer:

d. None of the above. (BAR 2013)

ABC Corp. issued redeemable shares. Under the terms of the issuance, the shares shall be redeemed at the end of 10 years from date of issuance, at par value plus a premium of 10%.

Choose the correct statement relating to these redeemable shares.

- a. ABC Corp. would need unrestricted retained earnings to be able to redeem the shares:
- b. Corporations are not allowed to issue redeemable shares; thus, the issuance by ABC Corp. is ultra vires;
- c. Holders of redeemable shared enjoy a preference over creditors;
- d. ABC Corp. may redeem the shared at the end of 10 years without need for unrestricted retained earnings provided that, after the redemption, there are sufficient assets to cover its debts; e) All of the above are incorrect.

Suggested Answer:

- d. ABC Corp. may redeem the shared at the end of 10 years without need for unrestricted retained earnings provided that, after the redemption, there are sufficient assets to cover its debts. (BAR 2013)
 - 4. Payment of Balance of Subscription
 a. Call by Board of Directors
 - b. Notice Requirement
 - c. Sale of Delinquent Shares
 - i. Effect of Delinquency
 - ii. Call by Resolution of the Board of Directors
 - iii. Notice of Sale
 - iv. Auction Sale and the Highest Bidder
- 5. Certificate of Stock
 - a. Nature of the Certificate
 - b. Uncertificated Shares
 - c. Negotiability
 - i. Requirements for Valid Transfer of Stocks
 - d. Issuance

i. Full Payment

X subscribed 10,000 shared in the capital stocks of AAA Corporation. He paid 50% of the 10,000 shares. X asked the Corporate Secretary to issue him the corresponding stock certificate representing the 50% of what he already paid. The Corporate Secretary of the corporation refused. Was the Corporate Secretary correct?

- 1. The Corporate Secretary is correct because the Corporation Code provides that no certificate of stock shall be issued to a subscriber until the shares as subscribed have been fully paid;
- 2. The Corporate Secretary cannot refuse because a Stock Certificate can be issued corresponding to the percentage of shares which were paid;
- The Corporation Secretary cannot refuse because a certificate of Stock can be issued provided it is indicated in the Certificate the actual percentage of what has been paid;
- 4. The Corporate Secretary cannot refuse because it is his legal duty to issue a stock certificate corresponding to the number of shares actually subscribed regardless of the actual payment.

Suggested Answer:

a. The Corporate Secretary is correct because the Corporation Code provides that no certificate of stock shall be issued to a subscriber until the shares as subscribed have been fully paid. (BAR 2012)

ii. Payment Pro-Rata

e. Lost or Destroyed Certificates

6. Stock and Transfer Book

What is a stock and transfer book?

Suggested Answer:

a stock and transfer book is a book which records all stocks in the name of the stockholders alphabetically arranged; the installments paid or unpaid on all stocks for which subscription has been made and the date of payment of any installment, a statement of every alienation, sale or transfer of stock made, the date thereof, and by and to whom made; and such other entries as the by-laws may prescribe. (BAR 2009)

- a. Contents
- b. Who May Make Valid Entries

7. Disposition and Encumbrance of Shares

- a. Allowable Restrictions on the Sale of Shares
- b. Sale of Partially Paid Shares
- c. Sale of a Portion of Shares Not Fully Paid
- d. Sale of All of Shares Not Fully Paid
- e. Sale of Fully Paid Shares
- f. Requisites of a Valid Transfer

Claude, the registered stockholder of 1,000 shares in ABC Corp., pledged the shares to Conrad by endorsement in blank of the covering stock certificates and, execution of a Deed of Assignment of Shares of Stock, intended as collateral for a loan of P1 M that was also supported by a separate promissory note.

A. Under these facts, is there a valid pledge of the shares of stock to Conrad?

- a. No, because shares of stocks are intangible personal properties whose possession cannot be delivered and, hence, cannot be the subject of a pledge;
- b. No, because the pledge of shares of stock requires double registration with the Register of Deeds of the principal place of business of the corporation and of the residence of the pledgor;
- c. Yes, because endorsement and delivery of the certificates of stock is equivalent to the transfer of possession of the covered shares to the pledge.
- d. Yes, because the execution of the Deed of Assignment of Shares of Stock is equivalent to a lawful pledge of the shares of stock.

Suggested Answer:

d. Yes, because the execution of the Deed of Assignment of Shares of Stock is equivalent to a lawful pledge of the shares of stock. (BAR 2013)

NB It is submitted that c is also a correct answer.

- B. After Claude defaulted on the loan, Conrad sought to have the shares registered in his name in the books of the corporation. If you are the Corporate Secretary of ABC Corporation, would you register the shares in the name of Conrad without any written instruction from Claude?
 - a. Yes, since the endorsement and delivery of the certificates of stock executed by Claude constitute the legal authority to cancel the shares in his name and to place them in Conrad's name;
 - b. Yes, since the execution of the Deed of Assignment by Claude would constitute the legal authority to cancel the shares in his name and place them in Conrad's name;
 - No, because corporate officers can only take direct instructions from the registered owners on the proper disposition of shares registered in their names;

d. No, because the corporation has a primary lien on the shares covering the unpaid subscription.

Suggested Answer:

None of the answers is correct. The pledge must be foreclosed. Conrad cannot just appropriate the shares of stock. (BAR 2013)

g. Involuntary Dealings with Shares

J. Dissolution and Liquidation

AAA Corporation is a bank. The operations of AAA Corporation as a bank were not doing well. So, to avert any bank run, AAA Corporation, with the approval of the Monetary Board, sold all its assets and liabilities to BBB Banking Corporation which includes all deposits accounts. In effect then, BBB Corporation will service all deposits of AAA Corporation.

A. Will the sale of all assets and liabilities of AAA Corporation to BBB Banking Corporation automatically dissolve or terminate the corporate existence of AAA Corporation? Explain your answer.

B. What are the legal requirements in order that a corporation may be dissolved?

Suggested Answer:

A. No, the sale of all the assets and liabilities of AAA Corporation to BBB Banking Corporation will not result in the automatic dissolution or termination of the existence of the former. A decision to dissolve AAA Corporation or to terminate its corporate existence would require a separate approval by a majority of the Board of Directors of AAA Corporation and its stockholders holding at least 2/3 of the total outstanding capital stock, as well as the separate approval by the Monetary Board.

B. A corporation may be dissolved voluntarily under Section 118 (where no creditors are affected) or under Section 119 (where creditors are affected) or by shortening of the corporate term under Section 120, or involuntarily by the SEC under Section 122, all of the Corporation Code. Dissolution under Sections 118, 119, and 120 require the same corporate approvals stated in (a) above.

NB We have to add that the the voluntary dissolution must be approved by the board of directors by at least majority vote and the by the stockholders representing at least 2/3s of the outstanding capital stock in a meeting duly called for that purpose with proper notice to all stockholders. In case of banks as in this case, the favorable endorsement of the BSP must be obtained and that the dissolution is effective upon approval by the SEC.

The SEC has the authority under Section 6 of PD 902-A to revoke the certificate of registration of a corporation upon any grounds provided by law, including the aforementioned Section 6-A. (BAR 2012)

1. Modes of Dissolution

- 1. Voluntary
 - i. Where No Creditors Are Affected
 - ii. Where Creditors Are Affected
 - iii. By Shortening of Corporate Term
- 2. Involuntary
 - i.By Expiration of Corporate Term

The term of GGG Corporation in accordance with its Articles of Incorporation ended last January 30, 2012. The term was not extended. What will happen to the corporation?

- a. The corporation is dissolved ipso facto;
- b. There is a need to pass a board resolution to formally dissolve the corporation;
- c. The Board of Directors must pass a resolution for the corporation to formally go into liquidation;
- d. The stockholders must pass a resolution to dissolve the corporation.

Suggested Answer:

- a. The corporation is dissolved ipso facto. (BAR 2012)
 - ii. Failure to Organize and Commence Business Within 2 Years from Incorporation
 - iii. Legislative Dissolution
 - iv. Dissolution by the SEC on Grounds under Existing Laws
- 2. Methods of Liquidation
 - a. By the Corporation Itself
 - a. Conveyance to a Trustee within a Three-Year Period
 - b. By Management Committee or Rehabilitation Receiver
 - c. Liquidation after Three Years

Bam filed an action to enjoin SN Company's Board of Directors from selling a parcel of land registered in the corporation's name, to compel the corporation to recognize Bam as a stockholder with 50 shares, to allow him to inspect the corporate books, and to claim damages against the corporation and its officers. Subsequently, the corporation and the individual defendants moved to dismiss the complaint since the corporation's certificate of registration was revoked by the SEC during the pendency of Barn's case on the ground of non-compliance

with reportorial requirements. The special commercial court granted the motion and reasoned that only an action for liquidation of assets can be maintained when a corporation has been dissolved and Bam cannot seek reliefs which in effect lead to the continuation of the corporation's business. The court also ruled that it lost jurisdiction over the intra-corporate controversy upon the dissolution of the corporation.

Was the court correct?

Suggested Answer:

The court is not correct. An action to be recognized as a stockholder and to inspect corporate documents is an intra-corporate dispute which does not constitute a continuation of business. The dissolution of the corporation simply prohibits it from continuing its business. Moreover, under Section 145 of the Corporation Code, no right or remedy in favor of or against any corporation, its stockholders, members, directors and officers shall be removed or impaired by the subsequent dissolution of the corporation. The dissolution does not automatically convert the parties into strangers or change their intra corporate relationship. Neither does it terminate existing causes of action which arose because of the corporate ties of the parties. The cause of action involving an intracorporate controversy remains and must be filed as an intracorporate dispute despite the subsequent dissolution of the corporation (Aguirre v. FQB +7, Inc. GR no. 170770, Jan. 9, 2013).

Four years later, SN Company files an action against Bam to recover corporate assets allegedly held by the latter for liquidation. Will this action prosper? (2015)

Suggested Answer:

The action cannot prosper because the corporation has no more legal capacity to sue after three years from its dissolution (Alabang Development Corporation v. Alabang Hills Village Association, GR no. 187456, June 2, 2014).

K. Other Corporations

- 1. Close Corporations
 - a. Characteristics of a Close Corporation
- b. Validity of Restrictions on Transfer of Shares
- c. Issuance or Transfer of Stock in Breach of Qualifying Conditions
- d. When Board Meeting is Unnecessary or Improperly Held
- e. Pre-Emptive Right
- f. Amendment of Articles of Incorporation
- g. Deadlocks
- 2. Non-Stock Corporations

The number of the Board of Trustees of a non-stock, non-profit education institution be—

- a. 5 only;
- b. Any number for as long as it is not less than 5 and no more than 11;
- c. Any number in multiples of 5, for as long as it is not less than 5 and no more than 15:
- d. Not less than 5 nor more than 10 in multiples of 5.

Suggested Answer:

c. Any number in multiples of 5, for as long as it is not less than 5 and no more than 15. (BAR 2012)

- 1. Definition
- 2. Purposes
- 3. Treatment of Profits

d. Distribution of Assets upon Dissolution

3. Religious Corporations - Exclude

Father X, an American priest who came from New York, registered the Diocese of Bacolod of the Roman Catholic Church which was incorporated as a corporation sole. There were years when the head of the Diocese was a Filipino, but there were more years when the heads were foreigners. Today, the head is an American again. Y donated a piece of land located in Bacolod City for use as a school. Which statement is most accurate?

- a. The Register of Deed of Bacolod City can refuse to register and transfer the title because the present head of the corporation sole is not a Filipino;
- b. The nationality of a corporation sole depends upon the nationality of the head at any given time;
- c. A corporation sole, regardless of the nationality of the head, can acquire real property either by sale or donation;
- d. A corporation sole is not legally allowed to own real property.

Suggested Answer:

c. A corporation sole, regardless of the nationality of the head, can acquire real property either by sale or donation. (BAR 2012)

4. Foreign Corporations

- a. Bases of Authority over Foreign Corporations
- i. Consent
- ii. Doctrine of "Doing Business" (related to definition under the Foreign Investments Act, R.A. No. 7042)

When is a foreign corporation deemed to be "doing business in the Philippines?"

A foreign corporation is deemed to be "doing business in the Philippines" if it is continuing the body or substance of the business or enterprise for which it was organized.

It is the intention of an entity to continue the body of its business in the country. The grant and extension of 90day credit terms by a foreign corporation to a domestic corporation for every purchase shows an intention to continue transacting with the latter (BAR 1998)

Gawsengsit Corp. is a corporation incorporated in Singapore. It invested in Bumblebee Corp., a Philippine corporation, by acquiring 30% of its shares. As a result, Gawsengsit Corp. nominated 30% of the directors of the Bumblebee Corp., all of whom are Singaporeans and officers of Gawsensit Corp.

Choose the correct statement relating to Gawsengsit Corp.

- a. Gawsengsit Corp. is doing business in the Philippines and requires a license from the SEC;
- b. Gawsengsit Corp. is not doing business in the Philippines by its mere investment in a Philippine corporation and does not need a license from the SEC:
- c. Gawsengsit Corp. has to appoint a resident agent in the Philippines;
- d. Gawsengsit Corp. cannot elect directors in Bumblebee Corp.;
- e. All of the above choices are incorrect.

Suggested Answer:

b. Gawsengsit Corp. is not doing business in the Philippines by its mere investment in a Philippine corporation and does not need a license from the SEC. (BAR 2013)

b. Necessity of a License to Do Business

- i. Requisites for Issuance of a License
- ii. Resident Agent

AAA Corporation is a foreign corporation that wants to operate a representative office in the Philippines. As required by the Corporation Code, there is a need to appoint a Resident Agent as a condition precedent to the issuance of a license to transact business in the Philippines. After 2 years, AAA Corporation removed its Resident Agent and did not appoint anyone anymore. Which statement is the most accurate?

- a. This can be a ground for revocation or suspension of its license to do business:
- b. There is no more effect in the license because anyway at the time of registration, a resident agent was appointed;
- c. This can be a ground for suspension only;

d. This will result in automatic revocation of its license to do business in the Phiippines.

Suggested Answer:

a. This can be a ground for revocation or suspension of its license to do business. (BAR 2012)

c. Personality to Sue

d. Suability of Foreign Corporations

South China Airlines is a foreign airline company. South China Airlines tickets are sold in the Philippines though PAL as their general agent. South China Airlines is not registered to do business as such with the Philippine SEC. which statement is most accurate?

- a. Although unlicensed to do business in the Philippines, South China Airlines can sue before the Philippine Courts and can also be sued;
- b. South China Airlines can sue but cannot be sued;
- c. South China Airlines cannot sue and cannot be sued also:
- d. South China Airlines can be sued in the Philippine Courts but it cannot sue.

Suggested Answer:

d. South China Airlines can be sued in the Philippine Courts but it cannot sue. (BAR 2012)

A foreign company has been exporting goods to a Philippine company for several years now. When the Philippine company failed to pay the latest exportation, the foreign company sued to collect in the Philippines. The Philippine company interposed the defense that the foreign company was doing business in the Philippines without a license; hence, could not sue before a Philippine court. Is this defense tenable? Explain your answer. (2015)

Suggested Answer:

The defense is not tenable. The mere act of exporting from one's own country, without doing any specific commercial act within the territory of the importing country can not be deemed as doing business in the importing country. Thus, the foreign company may sue in the Philippines despite lack of license to do business in the Philippines (Van Zuiden Bros Ltd. v. GTVL Manufacturing Industries 523 SCRA 233).

After disposing of his last opponent in only two rounds in Las Vegas, the renowned boxer Sonny Bachao arrived at the NAIA met by thousands of heroworshipping fans and hundreds of media photographers. The following day, a colored photograph of Sonny wearing a black polo short embroidered with the 2inch Lacoste crocodile logo appeared on the front page of every Philippine newspaper.

Lacoste International, the French firm that manufactures Lacoste apparel and owns the Lacoste trademark, decided to cash in on the universal popularity of the boxing icon. It reprinted the photographs, with the permission of the newspaper publishers, and went on a world-wide blitz of print commercials in which Sonny is shown wearing a Lacoste shirt alongside the phrase "Sonny Bachao just loves Lacoste".

When Sonny sees the Lacoste advertisements, he hires you as a lawyer and asks you to sue Lacoste International before a Philippine court:

- a. XXX
- b. XXX
- c. XXX
- d. Can Lacoste International validly invoke the defense that it is not a Philippine company and, therefore, Philippine courts have no jurisdiction? Explain.

Suggested Answer:

No. Philippine courts have jurisdiction over it, if it is doing business in the Philippines. Moreover, under Section 133 of the Corporation Code, while a foreign corporation doing business in the Philippines without license to do business, cannot sue or intervene in any action, it may be sued or proceeded against before our courts or administrative tribunal. (BAR 2009)

- e. Instances When Unlicensed Foreign Corporations May Be Allowed to Sue Isolated Transactions
- f. Grounds for Revocation of License

L. Mergers and Consolidations

XXX Bank Corporation and ZZZ Corporation were merged into XX ZZ Bank Corporation. So as not to create any unnecessary conflict, all the former directors of both banks wanted to be appointed/elected as members of the Board of Directors of the merged bank. Each bank used to have 11 members of the board. The maximum number of directors of the merged bank is—

- a. 15;
- b. 22;
- c. 21;
- d. 11.

Suggested Answer:

d. 21. (BAR 2012)

- 1. Definition and Concept
- 2. Constituent vs. Consolidated Corporation

- 3. Plan of Merger or Consolidation
- 4. Articles of Merger or Consolidation
- 5. Procedure
- 6. Effectivity

In 2015, Total Bank (Total) proposed to sell to Royal Bank (Royal) its banking business for P 10 billion consisting of specified assets and liabilities. The parties reached an eventual agreement, which they termed as "Purchase and Assumption (P & A) Agreement," in which Royal would acquire Total's specified assets and liabilities, excluding contingent claims, with the further stipulation that it should be approved by the Bangko Sentral ng Pilipinas (BSP). BSP imposed the condition that Total should place in escrow PI billion to cover for contingent claims against it. Total complied. After securing the approval of the BSP, the two banks signed the agreement. BSP thereafter issued a circular advising all bank and non-bank intermediaries that effective January 1, 2016, "the banking activities of Total Bank and Royal Bank have been consolidated and the latter has carried out their operations since then."

- [a] Was there a merger and consolidation of the two banks in point of the Corporation Code? Explain.
- [b] What is meant by a de facto merger? Discuss. (2016 Bar)

Suggested Answer:

- (A) No, there was no merger or consolidation of the two banks from the viewpoint of the Coporation Code. In Bank of Commerce v. Radio Philippine Network Inc (G.R. No. 195615, April 21, 2014), the Court ruled that there can no merger if the requirements and procedure for merger were not observed and no certificate of merger was issued by the SEC
- (B) A de facto merger is one where one corporation acquires all or substantially all of the properties of another corporation in exchange of shares of stock of the acquiring corporation. The acquiring corporation would end up with the business enterprise of the target corporation; whereas, the target corporation would end up with basically its only remaining assets being the shares of stock of the acquiring corporation
- XXX Corporate and YYY Corporation have agreed to be merged into one corporation. To facilitate the merger, both corporations agreed that the merger be made effective on May 31, 2012. The SEC approved the Articles of Merger on June 30, 2012. Which statement is most accurate?

The effective date of merger is May 31, 2012, the date stipulated by the parties as the effective date:

The effective date of the merger is always the date of the approval of the Articles of Merger by the SEC;

The effective date of the merger would be the date approved by the Board of Directors and the stockholders:

The stockholders and the Board of Directors can set the effective date of the merger anytime after the approval of the SEC.

Suggested Answer:

b. The effective date of the merger is always the date of the approval of the Articles of Merger by the SEC. (BAR 2012)

- 7. Limitations
- 8. Effects

**JURISDICTION

Intra-corporate Controversies

Atlantis Realty Corporation (ARC), a local firm engaged in real estate development, plans to sell one of its prime assets—a 3-hectare land valued at about P100 M. for this purpose, the board of directors of ARC unanimously passed a resolution approving the sale of the property for P75 M to Shangrila Real Estate Ventures (SREV), a rival realty firm. The resolution also called for a special stockholders meeting at which the proposed sale would be up for ratification.

Atty. Edric, a stockholder who owns only 1 share in ARC, wants to stop the sale. He then commences a derivative suit for and in behalf of the corporation from approving the sale.

If such a suit is commenced, would it constitute an intra-corporate dispute? If so, why and where would such a suit be filed? If not, why not?

Suggested Answer:

Yes, such suit would constitute an intra-corporate dispute as it is a suit initiated by a stockholder against other stockholders who are officers and directors of the same corporation. Such suit should be filed in the RTC designated by the Supreme Court as a corporate or commercial court.

DC is a unit owner of Medici Condominium located in Pasig City. On September 7, 2011, Medici Condominium Corp. (Medici) demanded from DC payment for alleged unpaid association dues and assessments amounting to P195,000. DC disputed the claim, saying that he paid all dues as shown by the fact that he was previously elected as Director and President of Medici. Medici, on the other hand, claimed that DC's obligation was a Construction Corporation. Consequently, DC was prevented from exercising his right to vote and be voted for during the 2011 election of Medici's Board of Directors. This prompted DC to file a complaint for damages before the Special Commercial Court of Pasig City. Medici filed a motion to dismiss on the ground that the court has no jurisdiction over the

intracorporate dispute which the HLURB has exclusive jurisdiction over. Is Medici correct?

Suggested Answer:

No. Medici is not correct. A controversy between the condominium corporation and its members-unit owners for alleged unpaid association dues and assessments and the prevention of DC from exercising his right to vote and be voted for during the 2011 election of the Medici's Board of Directors, partakes of the nature of an intracorporate dispute which does not fall within the jurisdiction of the HLURB despite its expansive jurisdiction. It is considered as an intra-corporate controversy falling within the jurisdiction of the Regional Trial Court designated as special commercial court. (BAR 2014)

VII. Securities Regulation Code (R.A. No. 8799)

ABC Corp. is engaged in the pawnshop business involving cellphones, laptops and other gadgets of value. In order to expand its business and attract investors, it offered to any person who invests at least PI 00,000.00 a "Promissory Note" where it obligated itself to pay the holder a 50% return on investment within one month. Due to the attractive offer, many individuals invested in the company but not one of them was able to realize any profit after one month.

Has ABC Corp. violated any law with its scheme? Explain. (2016 Bar)

Suggested Answer:

Yes, it did. ABC Corporation violated the provisions of the Securities Regulation Code that prohibits the sale of securities to the public, like promissory notes, without a registration statement filed and approved by the SEC

Why is the Securities Regulation Code called a "truth in securities law"? (2015)

Suggested Answer:

The Securities Regulation Code is called a "truth in securities law" because it requires the issuer to make full and fair disclosure of information about securities being sold or offered to be sold within the Philippines and penalizes manipulative and fraudulent acts, devices and schemes.

TRUE or FALSE. The *Howey Test* that there is an investment contract when a person invests money in a common enterprise and is led to expect profits primarily from the efforts of others.

Suggested Answer:

True.

What procedure must be followed under the d to authorize the sale or offer for sale or distribution of an investment contract?

Before the investment contract is sold or offered for sale or distribution to the public in the Philippines, it should be registered with the SEC in accordance with Section 8 of the SRC.

What are the legal consequences of failure to follow this procedure?

Suggested Answer:

The failure to follow this procedure has criminal consequences (i.e., upon conviction, a fine P50, 000 to P5 M and/or imprisonment of 7-12 years). It carries also civil liabilities in that the purchaser can recover from the seller (i) the consideration paid with interest thereon, less the amount of any income received on the purchased securities, upon the tender of such securities, or (ii) damages if the purchaser no longer owns such securities. Furthermore, the SEC may issue a cease and desist order. (BAR 2010)

Andante Realty, a marketing company that promotes and facilitates sales of real property through leverage marketing, solicits investors who are required to be a Business Center Owner (BCO) by paying an enrollment fee of \$250. The BCO is then entitled to recruit two other investors who pay \$250 each. The BCO receives \$90 from the \$250 paid by each of his recruits and is credited a certain amount for payments made by investors through the initial efforts of his Business Center. Once the accumulated amount reaches \$5,000, the same is used as down payment for the real property chosen by BCO.

Does the multi-level marketing scheme constitute an "investment contract" under the SRC? Define an "investment contract".

Suggested Answer:

Yes. The multi-level marketing scheme constitutes an "investment contract" under the SRC. An "investment contract" is a contract, transaction or scheme:

Involving an investment of money,

In a common enterprise,

With expectation of profits,

Primarily from the efforts of others. (BAR 2010)

Philippine Palaces Realty (PPR) had been representing itself as a registered broker of securities, duly authorized by the SEC. On October 6, 1996, PPR sold to spouses Leon and Carina one timeshare of Palacio del Boracay for US\$7,500. However its Registration Statement became effective only on February 11, 1998 after the SEC issued a resolution declaring that PPR was authorized to sell securities, including timeshares.

On March 30, 1998, Leon and Carina wrote PPR rescinding their purchase agreement and demanding the refund of the amount they paid, because the Palacio del Boracay timeshare was sold to them by PPR without the requisite

license or authority from the SEC. PPR contended that the grant of the SEC authority had the effect of ratifying the purchase agreement (with Leon and Carina) of October 6, 1996.

Is the contention of PPR correct? Explain.

Suggested Answer:

The contention of PPR is not correct. It is settled that no securities shall be sold or offered for sale or distribution in the Philippines without a registration duly filed and approved by the Commission. Corporate registration is one of the requirements under Section 8 of BP Blg. 178. (BAR 2009)

A. State Policy, Purpose

B. Securities Required to Be Registered

1. Securities

"Securities" issued to the public are required by law to be registered with—

- a. The Banko Sentral ng Pilipinas;
- b. The Philippine Stock Exchange;
- c. The Securities and Echange Commission;
- d. The Securities and Exchange Commission and the Philippine Stock Exchange.

Suggested Answer:

c. The Securities and Echange Commission. (BAR 2012)

What are the so-called exempt securities under the SRC?

Suggested Answer:

Under Sec. 9 of the SRC, the so-called exempt securities are:

- a. Those issued or guaranteed by the government of the Philippines or any of its political subdivisions or agencies;
- b. Those issued or guaranteed by the government of any foreign country with which the Philippines has diplomatic relations, or any other state on the basis of reciprocity, although the SEC may require compliance with the form and content of disclosures;
- c. Those issued by the receiver or by the trustee in a bankruptcy duly approved by the proper adjudicatory board;
- d. Those involving the sale or transfer which is by law, under the regulation of the OIC, HLURB, BIR; and
- e. Those issued by banks, except its own shares. (BAR 2009)

Exempt Transactions

Able Corporation sold securities to 21 non-qualified buyers during a 15-month period, without registering the securities with the Securities and Exchange Commission. Did Able Corporation violate the Securities Regulation Code? Explain. (2015)

Suggested Answer:

Yes because under the SRC securities shall not be sold or offered to be sold to the public within the Philippines unless the securities are registered with and approved by the Securities and Exchange Commission. Public means 20 or more inventors. The fact that the securities were sold during a 15 month period is immaterial. However, the sale of securities to less than 20 investors if done during a 12 month period is an exempt transaction under the Securities Regulation Code.

Securities issued by the Philippine government are "exempt securities" and, therefore, need not be registered with the Securities and Exchange Commission prior to their sale or offering to the public in the Philippines. What is the rationale behind this exemption? (2015)

Suggested Answer:

The rationale for the exemption is that the public is amply protected even without the registration of the securities to be issued by the government since the government is presumed to be always solvent.

C. Registration

Philippine Chromite, Inc., after registration of its securities, sold P10 M worth of common stocks to the public at P.01 per share. In its registration statement, it alleged that it holds a perfected mining claim on 100 hectares of chromite land in Botolan, Zamabales. X, a Botolan resident, bought P50,000 worth of stocks of the corporation from the stock exchange. After its public offering, the value of the stock dropped to half its price. X made some investigations and discovered that the mining claims of the corporation had not been perfected at the time of the issuance of its securities. The stock, however, rallied and after 2 years, commanded a price of 1 ½centavo per share. On its third year, the company collapsed and its stocks became totally valueles s. What is the remedy of X?

Suggested Answer:

The remedy of X for damages is lost by prescription. Any suit therefore must be filed within 2 years after the discovery of the facts constituting the cause of action (but not beyond 5 years after such cause of action accrued). 2 years having already elapsed since the time that X had discovered the misrepresentation in the registration statement of the corporation, the latter's civil liability has prescribed. X, however, is not prevented from invoking SEC's regulatory powers against the corporation.

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Under the SRC, what is the Margin Trading Rule?

Suggested Answer:

Under the Margin Trading Rule, no registered broker or dealer, or member of an exchange shall extend credit on any security an amount greater than whichever is higher of:

- a. 65% of the current market price of the security;
- b. 100% of the lowest market price of the security during the preceding 36 calendar months, but not more than 75% of the current market price.

The purpose of the Margin Trading Rule is to prevent excessive use of credit for the purchase of securities it is a counter to broker's desire to generate more sales by encouraging clients to buy securities on credit. (BAR 2009)

- D. Prohibitions on Fraud, Manipulation and Insider Trading
 - 1. Manipulation of Security Prices
 - 2. Short Sales
 - 3. Fraudulent Transactions
 - 4. Insider Trading

What is insider trading? (2015)

Suggested Answer:

Insider trading is the buying or selling by securities by an insider while in the possession of material non-public information.

X, who is the Executive VP of ABC Corporation, a listed company, can be held liable or guilty of insider trading if, he—

- a. Bought shares of ABC Corporation when it was planning to acquire another company to improve its asset base, the news of which increased the price of the shares in the Stock Exchange.
- b. Bought shares of XYC Corporation, a sister company of ABC Corporation when he learned that XYC Corporation was about to also list its share in the Philippine Stock Exchange;
- c. Bought shares of ZZZ Corporation when he learned that ABC Corporation would acquire ZZZ Corporation;
- d. All of the above.

Suggested Answer:

d. All of the above. (BAR 2012)

You are a member of the legal staff of a law firm doing corporate and securities work for Coco Products Inc., a company with unique products derived from coconuts and whose shares are traded in the Philippine Stock Exchange. A partner in the law firm, Atty. Buenexito, to whom you report, is the Corporate Secretary of Coco Products. You have long been investing in Coco Products stocks even before you became a lawyer.

While working with Atty. Buenixito on another file, he accidentally gave you the Coco products file containing the company's planned corporate financial rehabilitation. While you knew you had the wrong file, your curiosity prevailed and you browsed through the file before returning it. Thus, you learned that a petition for financial rehabilitation is imminent, as the company could no longer meet its obligations as they fell due.

Soon after, your mother is rushed to the hospital for an emergency operation, and you have to raise money for her hospital bills. An immediate option for you is to sell your Coco Products shares. The sale would be very timely because the price of the company's stocks are still high.

Would you sell the shares to raise the needed funds for your mother's hospitalization? Take into account legal and ethical considerations.

Suggested Answer:

The sale of the shares does not constitute insider trading. Although Atty. Buenixto, as corporate secretary of Coco products, Inc. was an insider, I did not obtain the information regarding the planned corporate rehabilitation by a communication from him. He just accidentally gave the wrong file.

It would be unethical to sell the shares. Rule 1.01 of the Code of Professional Responsibility provides, "A lawyer shall not engage in unlawful, dishonest, immoral or deceitful conduct."

A lawyer should not only refrain from performing unlawful acts. He should also desist from engaging in unfair deceitful conduct to conceal from the buyer of the shares the planned corporate rehabilitation. (BAR 2013)

E. Protection of Investors

1. Tender Offer Rule

C Corp. is the direct holder of 10% of the shareholdings in U Corp., a nonlisted (not public) firm, which in turn owns 62% of the shareholdings in H Corp., a publicly listed company. The other principal stockholder in H Corp. is C Corp. which owns 18% of its shares. Meanwhile, the majority stocks in U Corp. are owned by B Corp. and V Corp. at 22% and 30%, respectively. B Corp. and V Corp. later sold their respective shares in U Corp. to C Corp., thereby resulting in the increase of C Corp.'s interest in U Corp., whether direct or indirect, to more than 50%.

[a] Explain the Tender Offer Rule under the Securities Regulation Code.

[b] Does the Tender Offer Rule apply in this case where there has been an indirect acquisition of the shareholdings in H Corp. by C Corp.? Discuss. (2016 Bar)

Suggested Answer:

- (A) A Tender Offer Rule means a publicly announced intention by a person, acting alone or in concert with other persons, to acquire the outstanding equity shares of a public company or outstanding equity securities of an associate or related company of such public company which controls said public company (Section 19.1.8 of the SRC Implementing Rules and Regulations)
- (B) Yes, the mandatory Tender Offer Rule is still applicable even if the acquisition, direct or indirect, is less than 35% when the purchase would result in direct or indirect ownership of over 50% of the total outstanding equity shares of a public company (Cemco Holdings, Inc. v. National Life Insurance Co. of the Philippines, Inc., G.R. No. 171815, August 7, 2007)

Union Mines, Inc. has a total asset of P60 M with 210 stockholders holding at least 100 shares each.

The company has two principal stockholders, ABC which owns 60% of the shares of stock, and XYZ which owns 17%.

ABC in turn is owned to the extent of 21.31% by Acme, Inc.; 29.69% by Golden Boy, Inc; 9%by XYZ; and the rest by individual stockholders.

None of the parties is a publicly-listed company.

XYZ now proposes to buy Acme's and Golden Boy's shares in ABC, which would give it direct control of ABC and indirect control of Union Mines.

Is the proposed acquisition by XYZ subject to the mandatory tender offer and when is it mandatory?

Suggested Answer:

Yes, the proposed acquisition is subject to mandatory tender offer rule. A tender offer is a publicly announced intention by a person (acting alone or in concert with other persons) to acquire shares of a public company. A tender offer is meant to protect minor stockholders against any scheme that dilutes the share value of their investments. It gives them the chance to exit the company under the same terms offered to the majority stockholders.

Under the SRC and its implementing rules, a mandatory tender offer is required:

When at least 35% of the outstanding shares of a public company is to be acquired in one transaction or a series of transaction during a 12-month period, or

Even if any acquisition is less than 35% threshold but the result thereof is the ownership of more than 51% of the total outstanding shares of a public company. The mandatory offer rule also applies to share acquisition meeting the threshold, which is done at the level of the holding or parent corporation controlling a public company

In this case, Union Mines is clearly a public company, since it has a total asset of P60 M with 210 stockholders holding at least 100 shares each. A public company is defined as a corporation listed on the stock exchange, or a corporation with assets exceeding P50 M and with 200 or more stockholders at least 200 of them holding not less than 100 share of such corporation.

XYZ's acquisition of shares of Acme, Inc. and Golden Boy, Inc., taken separately, does not reach 35% threshold. If taken collectively, the two acquisitions total only 50%. However, when the acquisitions are added to XYZ's existing shares in Union Mines, they meet the more-than-51% threshold for mandatory tender offer. (BAR 2010)

The purpose of the "Tender Offer" Rule is to-

- a. Ensure an even playing field for all shareholders of a company in term of opportunity to sell their shareholdings;
- b. Ensure that minority shareholders in a publicly listed company are protected in the sense that they will equally have the same opportunity as the majority shareholders in terms selling their shares:
- c. Ensure that the shareholders who would also want to sell their

shareholdings will have the opportunity for a better price;

d. All of the above.

Suggested Answer:

d. All of the above. (BAR 2012)

- 2. Rules on Proxy Solicitation
- 3. Disclosure Rule

F. Civil Liability

Mr. and Mrs. Reyes invested their hard-earned savings in securities issued by LEAD Bank. After discovering that the securities sold to them were not registered with the SEC in violation of the Securities Regulation Code, the spouses Reyes filed a complaint for nullity of contract and for recovery of a sum of money with the RTC. LEAD Bank moved to dismiss the case on the ground that it is the SEC that has primary jurisdiction over actions involving violations of the Securities Regulation Code. If you were the judge, how would you rule on the motion to dismiss? (2015)

Suggested Answer:

The motion should be denied. Civil suits falling under the SRC (like liability for selling unregistered securities) are under the exclusive original jurisdiction of the RTC and hence, need not be first filed before the SEC unlike criminal cases, wherein the latter body exercises primary jurisdiction (*Pua vs Citibank, GR no. 1800*64, *September 16, 2013*).

Jurisdiction

What is the original and exclusive jurisdiction of the SEC?

Suggested Answer:

The SEC has original and exclusive jurisdiction over case involving:

- a. Devices or schemes amounting to fraud and misrepresentation;
- b. Controversies arising out of intra-corporate or partnership relations;
- c. Controversies in the election or appointment of directors, officers, etc.;
- d. Petitions to be declared in the state of suspension of payment. (BAR 1996)

NB The jurisdiction of the SEC on these items has been transferred to the RTC designated as special commercial courts by the SC. The SEC retains administrative and regulatory jurisdiction over corporations and and partnerships registered with it.

VIII. Banking Laws

Company X issued a Bank A Check No. 12345 in the amount of P500,000.00 payable to the Bureau of Internal Revenue (BIR) for the company's taxes for the third quarter of 1997. The check was deposited with Bank B, the collecting bank with which the BIR has an account. The check was subsequently cleared and the amount of P500,000.00 was deducted from the company's balance. Thereafter, Company X was notified by the BIR of its non-payment of its unpaid taxes despite the P500,000.00 debit from its account. This prompted the company to seek assistance from the proper authorities to investigate on the matter.

The results of the investigation disclosed that unknown then to Company X, its chief accountant Bonifacio Santos is part of a syndicate that devised a scheme to syphon its funds. It was discovered that though deposited, the check was never paid to the BIR but was passed on by Santos to Winston Reyes, Bank B's branch manager and Santos' co-conspirator. Instead of bringing the check to the clearing house, Reyes replaced Check No. 12345 with a worthless check bearing the same amount, and tampered documents to cover his tracks. No amount was then credited to the BIR. Meanwhile, Check No. 12345 was subsequently cleared and the amount therein credited into the accounts of fictitious persons, to be later withdrawn by Santos and Reyes.

Company X then sued Bank B for the amount of P500, 000.00 representing the amount deducted from its account. Bank B interposed the defense that Company X was guilty of contributory negligence since its confidential employee Santos was an integral part of the scheme to divert the proceeds of Check No. 12345. Is Company X entitled to reimbursement from Bank B, the collecting bank? Explain. (2016 Bar)

Suggested Answer:

Yes. Company X is entitled to reimbursement from the collecting bank. In a similar case, the Supreme Court ruled that the drawer could recover the amount deducted from its account because it failed to ensure that the check be paid to the designated payee, while the collecting bank share ½ of the loss because its branch manager conspired in the fraud (Philippine Commercial International Bank v. Court of Appeals, G.R. No. 121413, January 29, 2001)

B Bank, a large universal bank, regularly extends revolving credit lines to business establishments under what it terms as socially responsible banking and private business partnership relations. All loans that are extended to clients have a common "Escalation Clause," to wit: "B Bank hereby reserves its right to make successive increases in interest rates in accordance with the bank's adopted policies as approved by the Monetary Board; Provided that each successive increase shall be with the written assent of the depositor."

[a] X, a regular client of the bank, contends that the "Escalation Clause" is unfair, unconscionable and contrary to law, morals, public policy and customs. Rule on the issue and explain.

[b] Suppose that the "Escalation Clause" instead reads: "B Bank hereby reserves the right to make reasonable increases in interest rates in accordance with bank policies as approved by the Monetary Board; Provided, there shall be corresponding reasonable decreases in interest rates as approved by the Monetary Board." Would this be valid? Explain. (2016 Bar)

Suggested Answer:

- (A) The "escalation clause" is valid because each successive increase shall be with the written assent of the depositor. This stipulation does not violate the principle of mutuality of contracts. The stipulation would have been void if the supposed consent is given prior to the increase in interest rate.
- (B) The escalation clause with the de-escalation clause is valid provided that the client's consent is still secured prior to any increase in interest rate; otherwise, the escalation clause is void

A. The New Central Bank Act (R.A. No. 7653)

- 1. State Policies
- 2. Creation of the Bangko Sentral ng Pilipinas (BSP)

Why is the Bangko Sentral ng Pilipinas considered a lender of last resort? (2015)

Suggested Answer:

It is considered the lender of last resort because it lends to banks and similar institutions under financial distress when they have no other means to raise funds.

The government agency granted with the power of supervision and examination over banks and nonbank financial institutions performing quasi-banking functions, to ensure that the conduct of its business is on a sound financial basis that will provide continued solvency and liquidity is—

- a. The Philippine Deposit Insurance Corporation;
- b. The Bangko Sentral ng Pilipinas;
- c. The Anti-Money Laundering Council;
- d. The Securities and Exchange Commission.

Suggested Answer:

- b. The Bangko Sentral ng Pilipinas. (BAR 2012)
 - 3. Responsibility and Primary Objective
- 4. Monetary Board—Powers and Functions
- 5. How the BSP Handles Banks in Distress
 Conservatorship

Closure

Maharlikang Pilipino Banking Corporation (MPBC) operates several branches of Maharlikang Pilipino Rural Bank in Eastern Visayas. Almost all the branch managers are close relatives of the members of the Board of Directors of the corporation. Many undeserving relatives of the branch managers were granted loans. In time, the branches could not settle their obligations to depositors and creditors.

Receiving reports of these irregularities, the Supervising and Examining Department (SED) of the Monetary Board prepared a detailed report (SED Report) specifying the facts and the chronology of events relative to the problems that beset MPBC rural bank branches. The report concluded that the bank branches were unable to pay their liabilities as they fell due, and could not possibly continue in business without incurring substantial losses to its depositors and creditors.

May the Monetary Board order the closure of the MPBC rural banks relying only on the SED Repost, without need of an examination? Explain.

Suggested Answer:

Yes. Upon receipt of the report of the SED, the Monetary Board is authorized to take any of the actions enumerated under Sec. 30, RA No. 7653, otherwise known as the New Central Bank Act, leading to the receivership and liquidation of a bank or quasibank. There is no requirement that an examination be first conducted before a banking institution may be placed under receivership. (BAR 2009)

c. Receivership

A bank can be placed under receivership when, if allowed to continue in business, its depositors or creditors would incur

- a. Probable losses
- b. Inevitable losses
- c. Possible losses
- d. A slight chance of losses

Suggested Answer:

a. Probable losses (BAR 2011)

TRUE OR FALSE. A bank under a receivership can still grant new loans and accept new deposits.

Suggested Answer:

False. During the receivership, the assets and properties of the corporation are being gathered for conversion into cash in preparation for distribution to creditors. Granting new loans and accepting new deposits would constitute doing business for the bank in

the ordinary course of business which is contrary to the purpose and nature of a receivership proceeding. (BAR 2009)

d. Liquidation

e. Remedy

Maharlikang Pilipino Banking Corporation (MPBC) operates several branches of Maharlikang Pilipino Rural Bank in Eastern Visayas. Almost all the branch managers are close relatives of the members of the Board of Directors of the corporation. Many undeserving relatives of the branch managers were granted loans. In time, the branches could not settle their obligations to depositors and creditors.

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If the MPBC hires you as a lawyer because the Monetary Board has forbidden it from carrying on its business due to its imminent insolvency, what action will you institute to question the Monetary Board's order? Explain.

Suggested Answer:

The order of the Monetary Board may be questioned on a petition for certiorari on the ground that the action taken was in excess of jurisdiction or with grave abuse of discretion amounting to lack or excess of jurisdiction. The petition of certiorari may only be filed by the stockholders of record representing the majority of the capital stock within 10 days from receipt by the board of directors of the MPBC of the order directing receivership, liquidation or conservatorship. (BAR 2009)

6. How the BSP Handles Exchange Crisis a. Legal Tender Power

Rate of Exchange

Uniform Currency Act (Republic Act 529)

B. Law on Secrecy of Bank Deposits (R.A. No. 1405, as amended)

A. Purpose

B. Prohibited Acts

Raymond invested his money in securities issued by the Philippine government, through his bank. Subsequently, the Bureau of Internal Revenue asked his bank to disclose his investments. His bank refused the request for disclosure on the ground that the investments are confidential under the Secrecy of Bank Deposits Law (Republic Act No. 1405, as amended). Is the bank's refusal justified? Defend your answer. (2015)

Suggested Answer:

It is justified. Under *RA 1405*, investment in bonds issued by the Philippine government are also absolutely confidential and may not be examined, inquired or looked into by any person, government official, bureau or office save for the exceptions provided by law. None of the exceptions apply in the present case.

B. First Bank received an order of garnishment over a client's peso and dollar deposits in First Bank. Should First Bank comply with that order? Explain. (2015)

Suggested Answer:

First Bank should comply with the order of garnishment over a client's peso deposits because there is nothing in RA 1405 that places bank deposits beyond the reach of judgment creditor. And the disclosure of information on bank deposits pursuant to the writ of garnishment is only incidental to the execution process (PCIB v. CA, 193 SCRA 452). The dollar deposits, however, are exempt from garnishment or court order under the Foreign Currency Act (RA 6426). Thus, the bank should not comply with this part of the garnishment.

From his first term in 2007, Congressman Abner has been endorsing his pork barrel allocations to Twin Rivers in exchange for a commission of 40% of the face value of the allocation. Twin Rivers is a nongovernmental organization whose supporting papers, after audit, were found by the COA to be fictitious. Other than to prepare and submit falsified papers to support the encashment of the pork barrel checks, Twin Rivers does not appear to have done anything on the endorsed projects and Congressman Abner likewise does not appear to have bothered to monitor the progress of the progress of the projects he endorsed. The congressman converted most of the commissions he generated into US dollars, and deposited these in a foreign currency account with Banco de Plata (BDP)

Based on amply-supported tips given by a congressman from another political party, the AMLC sent BDP an order: (1) to confirm Cong. Abner's deposits with the bank and to provide details of these deposits; and (2) to hold all withdrawals and other transactions involving the congressman's bank accounts.

As counsel for BDP, would you advise the bank to comply with the order?

Suggested Answer:

I shall advise BDP not to comply with the order of the AMLC. It cannot inquire into the deposits of Congressman Abner, regardless of currency, without a bank inquiry order from a competent court, because crimes involved are not kidnapping for ransom, violations of the Dangerous Drugs act, hijacking and other violations of R.A. No. 6235, destructive arson, murder, and terrorism and conspiracy to commit terrorism.

The AMLC cannot order BDP to hold all withdrawals and other transactions involving the accounts of Congressman Abner. It is the Court of Appeals which has the power to issue a freeze order over that accounts upon petition of the AMLC. (BAR 2013)

GP is a suspected jueteng lord who is rumored to be enjoying police and military protection. The envy of many drug lords who had not escaped the dragnet of the law, GP was summoned to a hearing of the Committee on Racketeering and Other Syndicated Crimes of the House of Representatives, which was conducting a congressional investigation "in aid of legislation" on the involvement of police and military personnel, and possibly even of local government officials, in the illegal activities of suspected gambling and drug lords. Subpoenaed to attend the investigation were officers of certain identified banks with a directive to them to bring the records and documents of bank deposits of individuals mentioned in the subpoenas, among them GP. GP and the banks opposed the production of the banks records of deposits on the ground that no such inquiry is allowed under the Law on Secrecy of Bank Deposits. (RA 1405). Is the opposition of GP and the bank valid? Explain.

Suggested Answer:

Yes. The opposition is valid. GP is not a public official. The investigation does not involve one of the exceptions to the prohibition against disclosure of any information concerning bank deposits under the Law on Secrecy of Bank Deposits. The Committee conducting the investigation is not a competent court authorized under the law to issue a subpoena for the production of the bank record involving such disclosure. (BAR 2000)

TRUE OR FALSE. If the Ombudsman is convinced that there is a violation of law after investigating a complaint alleging illicit bank deposits of public officer, the Ombudsman may order the bank concerned to allow in camera inspection of bank records and documents.

Suggested Answer:

False. The Bank Secrecy Law prohibits the inspection of a bank account unless the permission of the account holder is obtained, or upon lawful order of the court or when the deposit is the subject matter of litigation. Investigation by the Ombudsman is not considered as a pending litigation to allow the examination of the bank records and documents. (BAR 2009)

Deposits Covered

X, a government official, has a number of bank accounts in T Bank containing millions of pesos. He also opened several trust accounts in the same bank which specifically covered the placement and/or investment of funds. X was later charged with graft and corruption before the Sandiganbayan (SB) by the Ombudsman. The Special Prosecutor filed a motion praying for a court order authorizing it to look into the savings and trust accounts of X in T Bank. X opposed the motion arguing that the trust accounts are not "deposits" under the Law on Secrecy of Bank Deposits (Rep. Act No. 1405). Is the contention of X correct? Explain. (2016 Bar)

Suggested Answer:

No, X is not correct.

Deposits in the context of the Secrecy of Philippine currency deposits include deposits of whatever nature and kind. They include funds deposited in the bank giving rise to creditor-debtor relationship, as well as funds invested in the bank like trust accounts (Ejercito v. Sandiganbayan, G.R. Nos. 157294-95, November 30, 2006)

Exceptions

The Bank Secrecy Law (RA 1405) prohibits disclosing any information about deposit records of an individual without court order except—

- a. In an examination to determine gross estate of a decedent;
- b. In an investigation for violation of Anti-Graft and Corrupt Practices;
- c. In an investigation by the Ombudsman;
- d. In an impeachment proceeding.

Suggested Answer:

a. In an examination to determine gross estate of a decedent. (BAR 2012)

X is being charged for violation of Anti-Graft and Corrupt Practices because he is suspected of having accumulated unexplained wealth. X maintains deposit accounts with ABC Bank. The Ombudsman filed criminal cases against X before the Sandiganbayan. Can the court issue subpoena against ABC Bank to produce all documents pertaining to all the deposit accounts of X?

- a. Yes, because there is already a pending case and provided the subpoena must be specific as to which account:
- b. Yes, it is enough that the specific bank is identified;
- c. No, because the issuance of the subpoena has no real legal basis;
- d. Even without a subpoena, information about the deposit accounts of X can be submitted to the Sandiganbayan because it will be used in a pending case.

Suggested Answer:

a. Yes, because there is already a pending case and provided the subpoena must be specific as to which account. (BAR 2012)

5. Garnishment of Deposits, including Foreign Deposits

Foreign Currency Deposit Act

Which of the following is an exception to the secrecy of bank deposits which are in the Philippine Pesos, but NOT an exception to the secrecy of foreign currency deposits?

- c. Upon BSP inquiry into or examination of deposits or investments with any bank, when the inquiry or examination is made in the course of the BSP's periodic special examination of said bank to ensure compliance with the AMLA:
- d. Upon PDIC and BSP inquiry into examination of deposit accounts in case there is a finding of unsafe or unsound banking practice;
- e. Upon inquiry in cases of impeachment;
- f. Upon inquiry by the Commissioner of Internal Revenue in the event a taxpayer files an application to compromise his tax liabilities on the ground of financial incapacity.

Suggested Answer:

C. Upon inquiry in cases of impeachment. (BAR 2012)

NB. a is also a correct answer because the law that gave BSP such authority has been repealed under Section 135 of RA 7653, the Central Bank Act. Pls see previous answers

X, a private individual, maintains a dollar deposit with ABC Bank. X is suspected to be the leader of a Kidnap for Ransom Gang and he is suspected of depositing all ransom money in said deposit account which are all in US Dollars. The police want to open said account to know if there are really deposits in big amounts. Which statement is most accurate?

- a. The same rules under the Secrecy of Bank Deposit Act will apply;
- b. An approval from the Monetary Board is necessary to open the account;
- c. Because the deposit is in US Dollars, it is covered by the Foreign Currency Deposit Act which allows disclosure only upon the written permission of the depositor;
- d. Approval from the court is necessary to order disclosure of the account.

Suggested Answer:

a. The same rules under the Secrecy of Bank Deposit Act will apply. (BAR 2012)

C. General Banking Law of 2000 (R.A. No. 8791)

1. Definition and Classification of Banks

Briefly describe the following types of banks:

a. Universal bank

Suggested Answer:

A universal bank is a commercial bank with 2 additional powers, namely:

- a. The power of an investment house; and
- b. The power to invest in non-allied enterprises.

b. Commercial bank

Suggested Answer:

A commercial bank is a bank that can:

- a. Accept drafts;
- b. Issue letters of credit;
- c. Discount and negotiate promissory note, bills of exchange, and other evidence of debt:
- d. Accept or create demand deposits;
- e. Receive other types of deposits, as well as deposit substitutes;
- f. Buy and sell foreign exchange, as well as gold or silver bullion;
- g. Acquire marketable bonds and other debts securities; and
- h. Extend credit, subject to such rules promulgated by the Monetary Board.

c. Thrift bank

Suggested Answer:

A thrift bank is one established as a savings and mortgage bank, a stock savings and loan association, or a private development bank, for the purpose of:

- a. Accumulating the savings of depositors and investing them in outlets determined by the Monetary Board as necessary in the furtherance of national economic objectives;
- b. Providing short-term working capital, medium and long-term financing, to business engaged in agriculture, services, industry and housing; and
- c. Providing diversified financial and allied services for its chosen market and constituencies especially for small and medium enterprises and individuals.

d. Rural bank

Suggested Answer:

A rural bank is one established to provide credit facilities to farmers and merchants or their cooperatives and, in general, to the people of the rural communities.

e. Cooperative bank

Suggested Answer:

A cooperative bank is organized under the Cooperative Code to provide financial and credit services to cooperatives. It may perform any or all the services offered by a rural

bank, including the operation of a Foreign Currency Deposit Unit subject to certain conditions. (BAR 2010)

May a publicly listed universal bank own 100% of the voting stocks in another universal bank and in a commercial bank?

- a. Yes, if with the permission of the Bangko Sentral ng Pilipinas.
- b. No, since it has no power to invest in equities.
- c. Yes, as there is no prohibition on it.
- d. No, since under the law, the 100% ownership on voting stocks must be in either bank only.

Suggested Answer:

d. No, since under the law, the 100% ownership on voting stocks must be in either bank only. (BAR 2011)

2. Distinction of Banks from Quasi-Banks and Trust Entities

XYZ Corporation is engaged in lending funds to small vendors in various public markets. To fund the lending, XYZ Corporation raised funds through borrowings from friends and investors. Which statement is most accurate?

- a. XYZ Corporation is a bank;
- b. XYZ Corporation is a quasi-bank;
- c. XYZ Corporation is an Investment Company;
- d. XYZ is none of the above.

Answer:

b. XYZ Corporation is a quasi-bank. (BAR 2012)

NB As an alternative answer, it is (d) because it is not clear that the funds were obtained from the public.

- 3. Bank Powers and Liabilities
 - a. Corporate Powers
 - b. Banking and Incidental Powers

A commercial bank wants to acquire shares in a cement manufacturing company. Do you think it can do that? Why or why not? (2015)

Answer:

A commercial bank cannot acquire shares in a cement manufacturing company because a commercial bank can only invest in the equity of allied undertakings, meaning, undertakings related to banking (Section 30 of RA 8791).

How do you characterize the legal relationship between a commercial bank and its safety deposit box client?

The relationship between a commercial bank and its safety deposit box client is that of a bailee and bailor, the bailment being for hire and mutual benefit.

Alternative Answer:

The legal relationship of the bank and its safety deposit box client is that of a lessor and lessee. (BAR 2010)

Is a stipulation in the contract for the use of a safety deposit box relieving the bank of liability in connection with the use thereof valid?

Suggested Answer:

The stipulation relieving the bank of liability in connection with the use of the safety deposit box is void as it is against law and public policy. (BAR 2010)

XXX Bank Corporation and ZZZ Corporation were merged into XX ZZ Bank Corporation. So as not to create any unnecessary conflict, all the former directors of both banks wanted to be appointed/elected as members of the Board of Directors of the merged bank. Each bank used to have 11 members of the board. The maximum number of directors of the merged bank is—

- a. 15;
- b. 22;
- c. 21;
- d. 11.

Suggested Answer:

c) 21. (BAR 2012)

- 4. Diligence Required of Banks Relevant Jurisprudence
- 5. Nature of Bank Funds and Bank Deposits

Differentiate "bank deposits" from bank substitutes".

Suggested Answer:

Bank deposits are funds obtained by a bank from the public which are relent by such bank to its own borrowers. Deposit substitutes are alternative forms of obtaining funds from the public, other than deposits, through the issuance, endorsement, or acceptance of debt instruments for the own account of the borrower, for the purpose of relending or purchasing of receivables and other obligations. These instruments may include, but need not be limited to, bankers acceptances, promissory notes, participations, certificates of assignment and similar instruments with recourse, and repurchase agreements. (BAR 2010)

Why are banks required to maintain reserves against their deposits and deposit substitutes? State one of three purposes for these reserves.

Any one of the following 4 purposes for requiring banks to maintain reserves against their deposits and deposit substitutes will suffice:

- 1. One of the purposes of the requirement to maintain bank reserves is to control the volume of money created by the credit operations of the banking system;
- 2. It is to enable the banks to answer any withdrawal;
- 3. To help Government to finance its operation;
- 4. To help Government control money supply. (BAR 2010)

6. Stipulation on Interests

A court found the interest charged by a bank as excessive and unconscionable and struck down the contractual stipulation on interest. If you were the judge, what would you impose as the applicable interest rate? State your legal basis. (2015)

Suggested Answer:

I will impose legal rate of interest which is currently set at 6% per annum.

7. Grant of Loans and Security Requirements

ABC Commercial Bank extends a loan to A, one of its stockholders. As security for the repayment of the loan, A pledges his ABC Commercial Bank shares of stocks. Is the loan valid? Why?

Suggested Answer:

The loan is invalid, contrary to Sec. 24 of the General Banking Act, which provides that no commercial bank shall make any loan on the security of shares of its own capital stock, unless such security is necessary to prevent loss upon a debt previously contracted in good faith. (BAR 1984)

NB Under the new General Banking law (RA 8791), banks are now allowed to grant loans against the security of its own shares as long as this is done with prior BSP approval but in case of foreclosure, the foreclosed shares must be disposed of within 6 months from acquisition.

As an alternative answer, the loan is valid even without BSP approval but the pledge or chattel mortgage on the shares is void.

X maintains a savings deposit in the amount of P1 M with ABC Bank Corporation. X also has obtained a loan from ABC Bank Corporation in the amount of P1 M. in case of default:

- a. ABC Bank can set-off the loan from the savings account being maintained by X with ABC Bank;
- b. Set-off is not possible because legal compensation is not allowed in banking transaction;

- c. Deposit accounts are usually earmarked for specific purpose hence offsetting is not legally possible;
- d. Off-setting is not possible because the obligation of X is a "simple loan".

a. ABC Bank can set-off the loan from the savings account being maintained by X with ABC Bank. (BAR 2012)

What is the single borrower's limit? (2015)

Suggested Answer:

Under the single borrower's limit, the total amount of loans, credit accommodations and guarantee that the bank may extend to any person shall not exceed 25% of the bank's net worth. While the law sets the ceiling at 20% of the bank's networth, it also empowers the BSP to modify the ceiling. The current SBL as set by BSP is 25% of the Bank's net worth.

1. Ratio of Net Worth to Total Risk Assets

A bank may acquire real property

- a. By purchase at a public sale of properties levied to satisfy tax delinquencies;
- b. By purchase from a real estate corporation in the ordinary course of the bank's business;
- c. Through dacion en pago in satisfaction of a debt in favor of a bank;
- d. In exchange for the purchase of shares of stocks of the bank;
- e. All of the above:
- f. None of the above.

Suggested Answer:

- b. By purchase from a real estate corporation in the ordinary course of the bank's business:
- c. Through dacion en pago in satisfaction of a debt in favor of a bank;
- d. In exchange for the purchase of shares of stocks of the bank; (BAR 2013)

NB As an alternative answer, only b and c on the assumption that for letter c, the debt is made in the ordinary course of of business. Letter d is not covered by the statutory provision allowing banks to acquire real property.

2. Single Borrower's Limit

3. Restrictions on Bank Exposure to DOSRI (Directors, Officers, Stockholders and their Related Interests)

Samito is the President and a Director of Lucky Bank (Lucky), a commercial bank holding its main office in Makati. His brother, Othello, owned a big fishing business based in Malabon. Othello applied for a loan of PSO Million with Lucky.

Othello followed the ordinary banking procedures in all the stages of the processing of his application. When required, he made the necessary arrangements to guarantee the loan. Thus, in addition to the real estate mortgage, Othello executed a joint and solidary suretyship, issued postdated checks, and submitted all other requirements prescribed by Lucky.

When the loan application was about to be approved and the proceeds released, BG Company, a keen competitor of Othello in the fishing industry, wrote to the Board of Directors and the management of Lucky questioning the loan on the ground of conflict of interest due to Samito and Othello being brothers, citing the legal restriction against bank exposure of directors, officers, stockholders or their related interests (DOSRI). (2017 BAR)

(a) What are the three restrictions imposed by law on DOSRI transactions? (4%)

Suggested Answer:

- (a) The restrictions are as follows:
- (I) The Transanctions must be approved by at least majority of the entire board excluding the director concerned;
- (II) The required approval shall be entered upon the records he bank and copy of such entry shall be submitted to the BSP;
- (III) Unless the loan is non-risk, the loan must not exceed the book value of the paid up shares of the borrowing DOSRI and the amount of unencumbered deposits. (Section 36 of RA 8791).
- (b) Is BG Company's opposition based on conflict of interest and violation of the restrictions on DOSRI transactions legally and factually correct? Explain your answer. (4%)

Suggested Answer:

(b) BG Company's opposition based on conflict of interest and violation of the restrictions on DOSRI transactions are not legally and factually correct. The "related interest" referred to under DOSRI extends only to the spouse of any Director, Officer or Stockholder, his ascendants and descendants up to the first degree of affinity or consanguinity. The Brothers are second degree relatives and as such, cannot be considered DOSRI accounts.

NOTE: It is recommended that the examinees be given outright credit for this question regardless of the answer because the question is answerable based on the Manual of Banking regulations, which are not included in the syllabus.

All senior officers of ABC Bank are entitled to obtain a housing loan. X is an Executive VP for Operations of ABC Bank. She obtained a housing loan with the ABC Bank. Which statement is most accurate?

a. The housing loan of X required a guarantor from somebody who is not

- connected with the bank;
- b. The housing loan of X requires the approval of the Board of Directors of the bank;
- c. The housing loan of X, being a benefit for employees does not require (a) but will require (b);
- d. The housing loan of X, being a benefit for employees, will not require (a) and (b).

d. The housing loan of X, being a benefit for employees, will not require (a) and (b). (BAR 2012)

A. Ownership of Banks

IX. Intellectual Property Code (Exclude Implementing Rules & Regulations)

- A. Intellectual Property Rights in General
- 1. Intellectual Property Rights
- 2. Differences between Copyrights, Trademarks and Patent

Differentiate trademark, copyright and patent from each other. (2015)

Suggested Answer:

As to definition:

- 1. Trademark is any visible sign capable of distinguishing goods
- Copyright is an incorporeal right granted by statute to the author or creator of original literary and artistic works whereby he is invested for a limited period of time with the right carry out, authorize and prevent the reproduction, distribution, transformation, rental, public performance and other forms of communication of his work to the public.
- 3. Patent is any technical solution of any problem in any field of human activity which is new, requires an inventive step and industrially applicable.

As to object

- 1. The object of trademark are goods
- 2. The object of copyright are original literary and artistic works
- 3. The object of patent is invention

As to term

- 1. The term of trademark is ten years
- 2. The term of copyright is generally 50 years
- 3. The term of patent is 20 years from application

As to how acquired

1. Trademark is acquired through registration and use

- 2. Copyright is acquired from the moment of creation
- 3. Patent is acquired through application with the IPO

Can an article of commerce serve as a trademark and at the same time enjoy patent and copyright protection? Explain and give an example.

Suggested Answer:

A stamped or marked container of goods can be registered as a trademark. An original ornamental design or model for articles of manufacturer can be copyrighted. An ornamental design cannot be patented, because aesthetic creations cannot be patented. However, it can be registered as an industrial design. Thus, a container of goods which has an original ornamental design can be registered as a trademark, can be copyrighted, and can be registered as an industrial design. (BAR 2010)

3. Technology Transfer Arrangements

Enumerate 3 stipulations that are prohibited in technology transfer agreements.

Answer:

The following stipulations are prohibited in technology transfer agreements:

- 1. Those that contain restrictions regarding the volume and structure of production;
- 2. Those that prohibit the use of competitive technologies in no-exclusive agreement; and
- 3. Those that establish a full or partial purchase option in favor of the licensor. (BAR 2010)

What contractual stipulations are required in all technology transfer agreements?

Answer:

The following stipulations are required in all technology transfer agreements:

- i. The laws of the Philippines shall govern its interpretation and in the event of litigation, the venue shall be the proper court in the place where the licensee has its principal place of business;
- ii. Continued access to improvements in techniques and processes related to the technology shall be made available during the period of the technology transfer arrangement;
- iii. In case it shall provide for arbitration, the Procedure of Arbitration of the Arbitration Law of the Philippines or the Arbitration Rules of the International Chamber of Commerce (ICC) shall apply and the venue of arbitration shall be the Philippines or any neutral country;
- iv. The Philippine taxes on all payments relating to the technology transfer agreement shall be borne by the licensor. (BAR 2010)

B. Patents

1. Patentable Inventions

Dr. Nobel discovered a new method of treating Alzheimer's involving a special method of diagnosing the disease, treating it with a new medicine that has been discovered after long experimentation and field testing, and novel mental isometric exercises. He comes to you for advice on how he can have his discoveries protected. Can he legally protect his new method of diagnosis, the new medicine, and the new method of treatment? If no, why? If yes, how?

Suggested Answer:

Dr. Nobel can be protected by a patent for the new medicine as it falls within the scope of Section 21 of the Intellectual Property Code. But no protection can be legally extended to him for the method of diagnosis and method of treatment which are expressly non-patentable. (BAR 2010)

- 2. Non-Patentable Inventions
- 3. Ownership of a Patent

X works as a research computer engineer with the Institute of Computer Technology, a government agency. When not busy with his work, but during office hours, he developed a software program for law firms that will allow efficient monitoring of the cases, which software program is not at all related to his work. Assuming the program is patentable, who has the right over the patent?

- A. X;
- B. Institute of Computer Technology;
- C. Neither X nor the Institute Computer Technology can claim patent right over the invention;
- D. X and the employer of X will jointly have the rights over the patent.

Suggested Answer:

A. X. (BAR 2012)

- a. Right to a Patent
- b. First-to-File Rule
- c. Inventions Created Pursuant to a Commission
- d. Right of Priority
- 4. Grounds for Cancellation of a Patent
- 5. Remedy of the True and Actual Inventor
- 6. Rights Conferred by a Patent

For years, Y has been engaged in the parallel importation of famous brands, including shoes carrying the foreign brand MAGIC. Exclusive distributor X demands that Y cease importation because of his appointment as exclusive distributor of MAGIC shoes in the Philippines.

Y countered that the trademark MAGIC is not registered with the Intellectual Property Office as a trademark and therefore no one has the right to prevent its parallel importation.

Who is correct? Why?

Suggested Answer:

X is correct. His rights under his exclusive distributorship agreement are property rights entitled to protection. The importation and sale by Y of MAGIC shoes constitutes unfair competition. Registration of the trademark is not necessary in case of an action for unfair competition.

Suppose the shoes are covered by a Philippine patent issued to the brand owner, what would your answer be? Explain.

Suggested Answer:

A patent for a product confers upon its owner the exclusive right of importing the product. The importation of a patented product without authorization of the owner of a patent constitutes infringement of the patent. X can prevent the parallel importation of such shoes by Y without its authorization. (BAR 2010)

7. Limitations of Patent Rights a. Prior User

X invented a device which, through the use of noise, can recharge a cellphone battery. He applied for and was granted a patent on his device, effective within the Philippines. As it turns out, a year before the grant of X's patent, Y, also an inventor, invented a similar device which he used in his cellphone business in Manila. But X files an injunctive suit against Y to stop him from using the device on the ground of patent infringement. Will the suit prosper?

- a. No, since the correct remedy for X is a civil action for damages.
- b. No, since Y is a prior user in good faith.
- c. Yes, since X is the first to register his device for patent registration.
- d. Yes, since Y unwittingly used X's patented invention.

Suggested Answer:

b. No, since Y is a prior user in good faith. (BAR 2011)

b. Use by the Government

8. Patent Infringement

What is the doctrine of equivalents? (2015)

Suggested Answer:

Under the doctrine of equivalents, infringement of patent occurs when a device appropriates a prior invention by incorporating its innovative concept and albeit with some modifications and change performs the same function in substantially the same way to achieve the same result (Godines v. CA, 226 SCRA 338).

What is the distinction between trademark infringement and unfair competition? (2015)

Suggested Answer:

The distinctions between infringement and unfair competition are the following:

- a. Infringement of trademark is the unauthorized use of a trademark, whereas unfair competition is the passing off of one's goods as those of another.
- b. In infringement of trademark fraudulent intent is unnecessary whereas in unfair competition fraudulent intent is essential.
- c. In infringement of trademark the prior registration of the trademark is a prerequisite to the action, whereas in unfair competition registration is not necessary (Del Monte Corp. vs. CA, G.R. No. L-78325, January 25, 1990).

a. Tests in Patent Infringement

i. Literal Infringement

ii. Doctrine of Equivalents

b. Defenses in Action for Infringement

9. Licensing

a. Voluntary

b. Compulsory

Super Biology Corporation (Super Biology) invented and patented a miracle medicine for the cure of AIDS. Being the sole manufacturer, Super Biology sold the medicine at an exorbitant price. Because of the sudden prevalence of AIDS cases in Metro Manila and other urban areas, the Department of Health (DOH) asked Super Biology for a license to produce and sell the AIDS medicine to the public at a substantially lower price. Super Biology, cited the huge costs and expenses incurred for research and development, refuses.

Assuming you are asked your opinion as the, legal consultant of DOH, discuss how you will resolve the matter. (4%) (2017 BAR)

Suggested Answer:

DOH may file a petition for compulsory license with the Director of Legal Affairs of the Intellectual Property Office to exploit the patented medicine even without the agreement of the patent owner on the ground of public interest, in particular, health (Section 193 of RA 8293, as ended). Once granted, the DOH may then produce and sell the AIDS medicines for a cheaper price subject to payment of reasonable royalties super Biology.

Compulsory Licensing of Inventions which are duly patented may be dispensed with or will be allowed exploitation even without agreement of the patent owner under certain circumstances, like national emergency, for reason of public interest, like national security, etc. The person who can grant such authority is—

- a. The Director General of the Intellectual Property Office;
- b. The Director of Legal Affairs of the Intellectual Property Office;
- c. The owner of the Patent right;
- d. Any agent of the owner of the Patent right.

Suggested Answer:

b) The Director of Legal Affairs of the Intellectual Property Office. (BAR 2012)

10. Assignment and Transmission of Rights

C. Trademarks

Can an article of commerce serve as a trademark and at the same time enjoy patent and copyright protection? Explain and give an example.

Suggested Answer:

A stamped or marked container of goods can be registered as a trademark. An original ornamental design or model for articles of manufacturer can be copyrighted. An ornamental design cannot be patented, because aesthetic creations cannot be patented. However, it can be registered as an industrial design. Thus, a container of goods which has an original ornamental design can be registered as a trademark, can be copyrighted, and can be registered as an industrial design. (BAR 2010)

- 1. Definition of Marks, Collective Marks, Trade Names
- 2. Acquisition of Ownership of Mark
- 3. Acquisition of Ownership of Trade Name

"Eagleson Refillers, Co.," a firm that sells water to the public, opposes the trade name application of "Eagleson Laundry, Co.," on the ground that such trade name tends to deceive trade circles or confuse the public with respect to the water firm's registered trade name. Will the opposition prosper?

- A. Yes, since such use is likely to deceive or confuse the public.
- B. Yes, since both companies use water in conducting their business.
- C. No, since the companies are not engaged in the same line of business.
- D. No, since the root word "Eagle" is a generic name not subject to registration.

Suggested Answer:

C. No, since the companies are not engaged in the same line of business. (BAR 2011)

4. Non-Registrable Marks

Jinggy went to Kluwer University (KU) in Germany for his doctorate degree (Ph.D.). He completed his degree with the highest honors in the shortest time. When he came back, he decided to set-up his own graduate school in his hometown in Zamboanga. After seeking free legal advice from his high-flying lawyer-friends, he learned that the Philippines follows the territoriality principle in trademark law, i.e., trademark rights are acquired through valid registration in accordance with the law. Forthwith, Jinggy named his school the Kluwer Graduate School of Business of Mindanao and immediately secured registration with the Bureau of Trademarks. KU did not like the unauthorized use of its name by its top alumnus no less. KU sought your help. What advice can you give KU?

Suggested Answer:

I will advice KU to seek for the cancellation of the Kluwer Graduate School of Business of Mindanao with the Bureau of Trademarks. Jinggy's registration of the mark "Kluwer" should not have been allowed because the law prohibits the registration of the mark "which may disparage or falsely suggests a connection with persons, living or dead, institutions, beliefs". Moreover, the Philippines is a signatory to the Paris Convention for the Protection of Intellectual Property (Paris Convention), it is obligated to assure nationals of countries of the Paris Convention that they are afforded an effective protection against violation of their intellectual property rights in the Philippines. Thus, under the Philippine law, a trade name of a national of a State that is a party to the Paris Convention, whether or not the trade name forms part of a trademark, is protected "without the obligation of filing or registration". (BAR 2014)

2. Prior Use of Mark as a Requirement

CHEN, Inc., a Taiwanese company, is a manufacturer of tires with the mark Light Year. From 2009 to 2014, Clark Enterprises, a Philippine- registered corporation, imported tires from CHEN, Inc. under several sales contracts and sold them herein the Philippines. In 2015, CHEN, Inc. filed a trademark application with the Intellectual Property Office (IPO) for the mark Light Year to be used for tires. The IPO issued CHEN, Inc. a certificate of registration (COR) for said mark. Clark Enterprises sought the cancellation of the COR and claimed it had a better right to register the mark Light Year. CHEN, Inc. asserted that it was the owner of the mark and Clark Enterprises was a mere distributor. Clark Enterprises argued that there was no evidence on record that the tires it imported from CHEN, Inc. bore the mark Light Year and Clark Enterprises was able to prove that it was the first to use the mark here in the Philippines. Decide the case. (2015)

Suggested Answer:

While RA 8293 removed the previous requirement of proof of actual use prior to the filing of an application for registration of a mark, proof of prior and continuous use is

necessary to establish ownership of trademark. Such ownership of the trademark confers the right to register the trademark. Since Chen owns the trademark as evidenced by its actual and continuous use prior to the Clark Enterprises, then it is the one entitled to the registration of the trademark. The fact that Clark was the first one to use the mark here in the Philippines will not matter. Chen's prior actual use of the trademark even in another country bars Clark from applying for the registration of the same trademark. Also, a mere distributor does not own the trademark to the goods he distributes and his right over the trademark can not prevail over the owner (E.Y Industrial Sales v. Shien Dar Electricity and Machinery, GR no. 184850, Oct. 20, 2010; Ecole de Cuisine Manille v. Renaud Cointreau, GR 185830, June 5, 2013).

3. Tests to Determine Confusing Similarity between Marks

a. Dominancy Test

X's "MINI-ME" burgers are bestsellers in the country. Its "MINI-ME" logo, which bears the color blue, is a registered mark and has been so since the year 2010. Y, a competitor of X, has her own burger which she named "ME-TOO" and her logo thereon is printed in bluish-green. When X sued Y for trademark infringement, the trial court ruled in favor of the plaintiff by applying the Holistic Test. The court held that Y infringed on X's mark since the dissimilarities between the two marks are too trifling and frivolous such that Y's "ME-TOO," when compared to X's "MINI-ME," will likely cause confusion among consumers.

Is the application of the Holistic Test correct? (2016 Bar)

Suggested Answer:

No, the application of the Holistic Test is not correct.

Considering the factors considered by the Court, it is more proper to apply the Dominancy test. Under this test, the focus is on the dominant features of the competing trademarks. Accordingly, MINI-ME trademark is confusingly similar with ME-TOO mark (McDonald's Corporation v. LC Big Mak Burger, Inc., G.R. No. 43993, August 18, 2004)

The "test of dominancy" in the Law on Trademarks, is a way to determine whether there exists an infringement of a trademark by—

- a. Determining if the use of the mark has been dominant in the market;
- b. Focusing on the similarity of the prevalent features of the competing marks which might create confusion;
- c. Looking at the mark whether they are similar in size, form or color;
- d. Looking at the mark whether there is one specific feature that is dominant.

Suggested Answer:

b. Focusing on the similarity of the prevalent features of the competing marks which might create confusion. (BAR 2012)

Skechers Corporation sued Inter-Pacific for trademark infringement claiming that Inter-Pacific used Skechers' registered "S" logo mark on Inter-Pacific's shoe products without its consent. Skechers has registered the trademark "SKECHERS" and the trademark "S" (with an oval design) with the Intellectual Property Office (IPO).

In its complaint, Skechers points out the following similarities: the color scheme of the blue, white and gray utilized by Skechers. Even the design and "wave-like" pattern of the mid-sole and outer sole of Inter-Pacific's shoes are very similar to Skechers' shoes, if not exact patterns thereof. On the side of Inter-Pacific's shoes, near the upper part, appears the stylized "S" placed in the exact location as that of the stylized "S" the Skechers shoes. On top of the "tongue" of both shoes, appears the stylized "S" in practically the saem location and size.

In its defense, Inter-Pacific claims that under the Holistic Test, the following dissimilarities are present: the mark "S" found in Strong shoes is not enclosed in an "oval design"; the word "Strong" is conspicuously placed at the backside and insoles; the hang tags labels attached to the shoes bear the word "Strong" for Inter-Pacific and Skeckers U.S.A." for Skechers; and, Strong shoes modestly priced compared to the cost of Skechers shoes.

Under the foregoing circumstances, which is the proper test to be applied—Holistic or Dominancy Test? Decide.

Suggested Answer:

The proper test to be applied is the dominancy test. Applying the dominancy test, there is a confusing similarity "Skechers" rubber shoes and "Strong" rubber shoes. The use of the stylized "S" by Inter-Pacific in its Strong Shoes infringes on the trademark "Skechers" already registered by Skechers U.S.A. with the IPO. While it is undisputed that Skechers U.S.A. stylized "S" is within an oval design, the dominant feature of the trademark is stylized "S" as it is precisely the stylized "S" which catches the eye of the purchaser. (BAR 2014)

b. Holistic Test

Confusion of Goods and Confusion of Services

- 4. Well-Known Marks
- 5. Rights Conferred by Registration

ABC Appliances Corporation (ABC) is a domestic corporation engaged in the production and sale of televisions and other appliances. YYY Engineers, a Taiwanese company, is the manufacturer of televisions and other appliances from whom ABC actually purchases appliances. From 2000, when ABC started doing business with YYY, it has been using the mark "TTubes" in the Philippines for the television units that were bought from YYY. In 2015, YYY filed a trademark

application for "TTubes." Later, ABC also filed its application. Both claim the right over the trademark "TTubes" for television products. YYY relies on the principle of "first to file" while ABC involves the "doctrine of prior use."

- [a] Does the fact that YYY filed its application ahead of ABC mean that YYY has the prior right over the trademark? Explain briefly.
- [b] Does the prior registration also mean a conclusive assumption that YYY Engineers is in fact the owner of the trademark "TTubes?" Briefly explain your answer. (2016 BAR)

Suggested Answer:

- (A) No. Since YYY is not the owner of the trademark, it has no right to apply for registration. Registration of trademark, by itself, it not a mode of acquiring ownership. It is the ownership of trademark that confers the right to register the same (Birkenstock Orthopaedia GMBH v. Philippine Shoe Expo Marketing Corporation, G.R. No. 194307, November 20, 2013)
- (B) No. Registration merely creates a prima facie presumption of the validity of the registration of the registrant's ownership of the trademark and the exclusive right to the use thereof. The presumption of ownership accorded to a registrant is rebuttable and must yield to evidence to the contrary

6. Use by Third Parties of Names, etc. Similar to Registered Mark

T is the registered trademark owner of "CROCOS" which he uses on his ready-towear clothes. Banking on the popularity of T's trademark, B came up with his own "CROCOS" mark, which he then used for his "CROCOS" burgers. T now sues B for trademark infringement but B argues that his product is a burger, hence, there is no infringement. Is B correct?

- a. No, since the owner of a well-known mark registered in the Philippines has rights that extends even to dissimilar kinds of goods.
- b. Yes, since the right of the owner of a well-known mark registered in the Philippines does not extend to goods which are not of the same kind.
- c. Yes, as B was in bad faith in coming up with his own "CROCOS" mark.
- d. No, since unlike T, he did not register his own "CROCOS" mark for his product.

Suggested Answer:

a. No, since the owner of a well-known mark registered in the Philippines has rights that extends even to dissimilar kinds of goods. (BAR 2011)

7. Infringement and Remedies

a. Trademark Infringement

In intellectual property cases, fraudulent intent is not an element of the cause of action except in cases involving:

- a. Trademark infringement
- b. Copyright infringement
- c. Patent infringement
- d. Unfair competition

a. Trademark infringement (BAR 2014)

After disposing of his last opponent in only two rounds in Las Vegas, the renowned boxer Sonny Bachao arrived at the NAIA met by thousands of heroworshipping fans and hundreds of media photographers. The following day, a colored photograph of Sonny wearing a black polo short embroidered with the 2inch Lacoste crocodile logo appeared on the front page of every Philippine newspaper.

Lacoste International, the French firm that manufactures Lacoste apparel and owns the Lacoste trademark, decided to cash in on the universal popularity of the boxing icon. It reprinted the photographs, with the permission of the newspaper publishers, and went on a world-wide blitz of print commercials in which Sonny is shown wearing a Lacoste shirt alongside the phrase "Sonny Bachao just loves Lacoste".

When Sonny sees the Lacoste advertisements, he hires you as a lawyer and asks you to sue Lacoste International before a Philippine court:

For trademark infringement in the Philippines because Lacoste International used his image without his permission

Suggested Answer:

Sonny Bachao cannot sue for infringement of trademark. The photographs showing him wearing a Lacoste shirt were not registered as a trademark. (BAR 2009)

- b. Damages
- c. Requirement of Notice

8. Unfair Competition

MS Brewery Corporation (MS) is a manufacturer and distributor of the popular beer "MS Lite." It faces stiff competition from BA Brewery Corporation (BA) whose sales of its own beer product, "BA Lighter," has soared to new heights. Meanwhile, sales of the "MS Lite" decreased considerably. The distribution and marketing personnel of MS later discovered that BA has stored thousands of empty bottles of "MS Lite" manufactured by MS in one of its warehouses. MS filed a suit for unfair competition against BA before the Regional Trial Court (RTC). Finding a connection between the dwindling sales of MS and the increased sales

of BA, the RTC ruled that BA resorted to acts of unfair competition to the detriment of MS. Is the RTC correct? Explain. (2016 Bar)

Suggested Answer:

No, the RTC is not correct.

Hoarding, or the act of accumulating empty bottles to impede circulation of the bottled product, does not amount to unfair competition. BA did not fraudulently "pass off" its product as that of MS Lite. There was no representation of misrepresentation on the part of BA that would confuse or tend to confuse its goods with those of MS Lite (Coca Cola Bottlers v. GOMEZ, G.R. No. 154491, November 14, 2008).

Ashley Manufacturing Company, a manufacturer in France of a certain brand of cigarette paper, appoints "X" Company the exclusive agent to sell its paper in the Philippines. Among its customers are well-known cigarette manufacturers in the Philippines.

9. Trade Names or Business Names
10. Collective Marks

D. Copyrights

Can an article of commerce serve as a trademark and at the same time enjoy patent and copyright protection? Explain and give an example.

Suggested Answer:

A stamped or marked container of goods can be registered as a trademark. An original ornamental design or model for articles of manufacturer can be copyrighted. An ornamental design cannot be patented, because aesthetic creations cannot be patented. However, it can be registered as an industrial design. Thus, a container of goods which has an original ornamental design can be registered as a trademark, can be copyrighted, and can be registered as an industrial design. (BAR 2010)

1. Basic Principles, Sections 172.2, 175 and 181

Jose Santos has written many poems, some of which have been published in Panorama Magazine but never registered with the Copyright Office. Among his published works was the poem entitled "In a Rose Garden."

About a year from its publication, Jose was surprised to hear over the radio a song whose lyrics were copied from his poem. It appears that music sheets of the song have been published and sold under the name of the composer, without any acknowledgment in favor of Jose.

Jose wants to know what his rights are and whether he can secure an injunction against the composer and/or the publisher, perhaps with damages. How will you advise him? Explain.

Suggested Answer:

I would tell Santos that he has a right to file injunction proceedings to restrain the composer and/or his publisher from further committing any act of infringement of his copyright. Under the present law, copyright is acquired from the moment of the creation of the work. Registration and deposit of the work are no longer necessary for its acquisition. The moment Santos wrote his poem, he acquired the right to restrain any infringement on his copyright, as well as the right to have the infringing copies and devices impounded. However, what Santos cannot demand without such registration and deposit are damages resulting from the infringement. He is therefore not entitled to such damages. (BAR 1981)

Copyrightable Worksa. Original Works

Under the Intellectual Property Code, lectures, sermons, addresses or dissertations prepared for oral delivery, whether or not reduced in writing or other material forms, are regarded as

- a. Non-original works.
- b. Original works.
- c. Derivative works.
- d. Not subject to protection.

Suggested Answer:

b. Original works. (BAR 2011)

b. Derivative Works

3. Non-Copyrightable Works

TRUE or FALSE — EXPLAIN BRIEFLY YOUR ANSWER

(d) News reports are not copyrightable. (2%) (2017 BAR)

Suggested Answer:

(d) True. Under Section 175 of the Intellectual Property de (R.A. 8293, June 6, 1997) "news of the day and other miscellaneous having the character of mere items of press information" are "unected subject matter", therefore, not copyrightable.

X, an amateur astronomer, stumbled upon what appeared to be massive volcanic eruption in Jupiter while peering at the planet through his telescope. The following week, X, without notes, presented a lecture on his findings before the Association of Astronomers of the Philippines. To his dismay, he later read an article in a science journal written by Y, a professional astronomer, repeating

exactly what X discovered without any attribution to him. Has Y infringed on X's copyright, if any?

- a. No, since X did not reduce his lecture in writing or other material form.
- b. Yes, since the lecture is considered X's original work.
- c. No, since no protection extends to any discovery, even if expressed, explained, illustrated, or embodied in a work.
- d. Yes, since Y's article failed to make any attribution to X.

Suggested Answer:

c. No, since no protection extends to any discovery, even if expressed, explained, illustrated, or embodied in a work. (BAR 2011)

X came up with a new way of presenting a telephone directory in a mobile phone, which he dubbed as the "iTel" and which uses lesser time for locating names and telephone numbers. May X have his "iTel" copyrighted in his name?

- a. No, because it is a mere system or method.
- b. Yes, because it is an original creation.
- c. Yes, because it entailed the application of X's intellect.
- d. No, because it did not entail any application of X's intellect.

Suggested Answer:

a. No, because it is a mere system or method. (BAR 2011)

TRUE OR FALSE. The *Denicola Test* in intellectual property law states that if design elements of an article reflect a merger of aesthetic and functional considerations, the artistic aspects of the work cannot be conceptually separable from the utilitarian aspects; thus, the article cannot be copyrighted.

Suggested Answer:

True. Applying the *Denicola Test* in *Brandir International, Inc. v. Cascade Pacific Lumber Co.* (834 F.2d 1142, 1988 Copr.L.Dec. P26), the United State Court of Appeals for the Second Circuit held that if there is any aesthetic element which can be separated from the utilitarian elements, then the aesthetic element may be copyrighted. (BAR 2009)

4. Rights of Copyright Owner

Apart from economic rights, the author of a copyright also has moral rights which he may transfer by way of assignment. The term of these moral rights shall last

- a. During the author's lifetime and for 50 years after his death.
- b. Forever.
- c. 50 years from the time the author created his work.
- d. During the author's lifetime.

a. During the author's lifetime and for 50 years after his death. (BAR 2011)

5. Rules on Ownership of Copyright

While vacationing in Boracay, Valentino surreptitiously took photographs of his girlfriend Monaliza in her skimpy bikini. 2 weeks later, her photograph appeared in the Internet and in a national celebrity magazine.

Monaliza found out that Valentino had sold the photograph to the magazine and, adding insult to injury, uploaded them to his personal blog on the Internet.

Monaliza filed a complaint against Valentino for damages based on, among other grounds, violation of her intellectual property rights. Does she have any cause of action? Explain.

Suggested Answer:

No. Monaliza cannot sue Valentino for violation of her intellectual property rights, because she was not the one who took the pictures. She may sue Valentino instead for violation of her right to privacy. He surreptitiously took photographs of her and then sold the photographs to a magazine and uploaded them to his personal blog in the Internet.

Valentino's friend Francesco stole the photographs and duplicated them and sold them to a magazine publication. Valentino sued Francesco for infringement and damages. Does Valentino have any cause of action? Explain.

Suggested Answer:

No. Valentino cann<mark>ot sue Francesco for infringement, because he</mark> has already sold the photographs to a magazine.

Does Monaliza have any cause of action against Franceso? Explain.

Suggested Answer:

Yes. Monaliza can also sue Francesco for violation of her right to privacy. (BAR 2010)

T, an associate attorney in XYZ Law Office, wrote a newspaper publisher a letter disputing a columnist's claim about an incident in the attorney's family. T used the law firm's letterhead and its computer in preparing the letter. T also requested the firm's messenger to deliver the letter to the publisher. Who owns the copyright to the letter?

- a. T, since he is the original creator of the contents of the letter.
- b. Both T and the publisher, one wrote the letter to the other who has possession of it.
- c. The law office since it was an employee and he wrote it on the firm's letterhead.
- d. The publisher to whom the letter was sent.

a. T, since he is the original creator of the contents of the letter. (BAR 2011)

Rudy is a fine arts student in a university. He stays in a boarding house with Bernie as his roommate. During his free time, Rudy would paint and leave his finished works lying around the boarding house. One day, Rudy saw one of his works—an abstract painting entitled Manila Traffic Jam—on display at the university cafeteria. The cafeteria operator said he purchased the painting from Bernie who represented himself as its painter and owner.

Rudy and the cafeteria operator immediately confronted Bernie. While admitting that he did not do the painting, Bernie claimed ownership of its copyright since he had already registered it in his name with the National Library as provided in the Intellectual Property Code.

Who owns the copyright to the painting? Explain.

Suggested Answer:

Rudy owns the copyright to the painting because he was the one who actually created it. His rights existed from the moment of its creation. The registration of the painting by Bernie with the National Library did not confer copyright upon him. The registration is merely for the purpose of completing the records of the National Library. (BAR 2013)

6. Limitations on Copyright

a. Doctrine of Fair Use

Virtucio was a composer of Ilocano songs who has been quite popular in the Ilocos Region. Pascuala is a professor of music in a local university with special focus on indigenous music. When she heard the musical works of Virtucio, she purchased a CD of his works. She copied the CD and sent the second copy to her Music class with instructions for the class to listen to the CD and analyze the works of Virtucio.

Did Pascuala thereby infringe Virtucio's copyright? Explain your answer. (4%) (2017 BAR)

Suggested Answer:

Pascuala did not infringe on the rights of Virtucio. The fair use of a copyrighted work for criticism, comment, news reporting, teaching including limited number of copies for classroom use, scholarship, research and similar purposes is not an infringement of copyright (Section I85 of RA 8293, as amended). In this case, Virtucio's reproduction of the limited number of CD was for classroom use and educational purposes thus negating copyright infringement.

The Fair Use Doctrine allows others to utilize copyrighted works under certain conditions. The factors to consider whether use is fair or not would be the purpose and character of the use, nature of the copyrighted work, amount and substantially of the portions used, and else?

- a. Effect of the use upon the creator of the work;
- b. Effect upon the potential market of the work;
- c. Effect of the use upon the public in general;
- d. Effect of the use upon the class in which the creator belongs.

Suggested Answer:

b. Effect upon the potential market of the work. (BAR 2012)

b. Copyright Infringement

X's painting of Madonna and Child was used by her mother to print some personalized gift wrapper. As part of her mother's efforts to raise funds for Bantay Bata, the mother of X sold the wrapper to friends. Y, an entrepreneur, liked the painting in the wrapper and made many copies and sold the same through National Bookstore. Which statement is most accurate?

- a. Y can use the painting for his use because this is not a copyrightable material:
- b. X can sue Y for infringement because artistic works are protected from the moment of creation;
- c. Works of art need to be copyrighted also to get protection under the law;
- d. Y can use the drawing even though not copyrighted because it is already a public property having been published already.

Suggested Answer:

B. X can sue Y for infringement because artistic works are protected from the moment of creation. (BAR 2012)

KK is from Bangkok, Thailand. She studies medicine in the Pontifical University of Santo Tomas (UST). She learned that the same foreign books prescribed in UST are 40-50% cheaper in Bangkok. So she ordered 50 copies of each book for herself and her classmates and sold the books at 20% less than the price in the Philippines. XX, the exclusive licensed publisher of the books in the Philippines, sued KK for copyright infringement. Decide.

Suggested Answer:

KK did not commit copyright infringement. Under the "first sale" doctrine, the owner of a particular copy or phonorecord lawfully made is entitled, without the authority of the copyright owner, to sell or otherwise dispose of the possession of that copy or phonorecord. Hence, there is no infringement by KK since the said doctrine permitted importation and resale without the publisher's further permission. (BAR 2014)

After disposing of his last opponent in only two rounds in Las Vegas, the renowned boxer Sonny Bachao arrived at the NAIA met by thousands of heroworshipping fans and hundreds of media photographers. The following day, a colored photograph of Sonny wearing a black polo short embroidered with the 2inch Lacoste crocodile logo appeared on the front page of every Philippine newspaper.

Lacoste International, the French firm that manufactures Lacoste apparel and owns the Lacoste trademark, decided to cash in on the universal popularity of the boxing icon. It reprinted the photographs, with the permission of the newspaper publishers, and went on a world-wide blitz of print commercials in which Sonny is shown wearing a Lacoste shirt alongside the phrase "Sonny Bachao just loves Lacoste".

When Sonny sees the Lacoste advertisements, he hires you as a lawyer and asks you to sue Lacoste International before a Philippine court:

A. XXX.

B. For copyright infringement because of the unauthorized use of the published photographs.

Suggested Answer:

Sonny Bachao cannot sue for infringement of copyright for the unauthorized use of the photographs showing him wearing a Lacoste shirt. The copyright to the photographs belong to the newspaper which published them inasmuch as the photographs were the result of the performance of the regular duties of the photographers. Moreover, the newspaper publishers authorized the reproduction of the photographs. (BAR 2009)

E. Rules of Procedure for Intellectual Property Rights Cases (A.M. No. 10-3-10-SC)

X. Special Laws

A. The Chattel Mortgage Law and Real Estate Mortgage Law (Excluded and made a part of Civil Law coverage)

X obtained a loan for Php50Million from SSS Bank. The collateral is his vacation house in Baguio City under a real estate mortgage. X needed more funds for his business so he again borrowed another Php10Million, this time from BBB Bank, another bank, using the same collateral. The loan secured from SSS Bank fell due and X defaulted.

- a. If SSS Bank forecloses the real estate mortgage, what rights, if any, are left with 888 Bank as mortgagee also? (2%)
- b. If the value of the Baguio property is less than the amount of loan, what would be the recourse of SSS Bank? BBB Bank? (2%)

- c. If the value of the property is more that the amount of the loan, who will benefit from the excess value of the property? (2%)
- d. If X defaulted with its loan in favor of BBB Bank but fully paid his loan with SSS Bank, can BBB Bank foreclose the real mortgage executed in its favor? (2%)
- e. Does X have any legal remedy after the foreclosure in the event that later on he has the rnoney to pay for the loan? (1%)
- f. If SSS Bank and BBB Bank abandon their rights under the real estate mortgage, is there any legal recourse available to them? (1%)

- a. BBB Banks, as a junior mortgagee, would have the right to redeem the foreclosed property, together with X, his successor in interest, any judicial or judgment creditor of X, or any other person or entity having a lien on the vacation house subsequent to the real mortgage in favor of SSS Bank(i.e. other junior mortgagees, if any). (Sec. 6, Art. 3135).
- b. In case of a deficiency, SSS Bank could file a suit to claim for the deficiency. BBB Bank could file an ordinary action to collect its loan from X. If it does so, it would be deemed to have waived its mortgage lien. If the judgment in action to collect is favorable to BBB Bank, and it becomes final and executory, BBB Bank could enforce the said judgment by execution. It could even levy execution on the same mortgaged property, but it would not have priority over the latter. (Caltex Phiippines vs. IAC, et. al., GR. No. 74730)
- c. If the value of the property is more than that the amount of loan, the excess could benefit and be claimed by BBB Bank, any judicial or judgment creditor of X, any other junior mortgagee, and X.
- d. If X defaulted in respect of his loan from BBB Bank but fully paid his loan from SSS Bank, BBB Bank could now foreclose the mortgaged property as it would be the only remaining mortgagee of the same.
- e. Yes, X could redeem the property within 1 year from the date of the registration of the sheriff's certificate of foreclosure sale.
- f. SSS Bank and BBB Bank could each file an ordinary action to collect its loan from X.

X obtained a Php10Million loan from BBB Banking Corporation. The loan is secured by Real Estate Mortgage on his vacation house in Tagaytay City. The original Deed of Real Estate Mortgage for the Php10Million was duly registered. The Deed of Real Estate Mortgage also provides that "The mortgagor also agrees that this mortgage will secure the payment of additional loans or credit accommodations that may be granted by the mortgagee ... " Subsequently, because he needed more funds, he obtained another Php5Million loan. On due dates of both loans, X failed to pay the Php5Million but fully paid the

Php10Million. BBB Banking Corporation instituted extrajudicial foreclosure proceedings.

- a. Will the extrajudicial foreclosure prosper considering that the additional Php5Million was not covered by the registration? (5%)
- b. What is the meaning of a "dragnet clause" in a Deed of Real Estate Mortgage? Under what circumstances will the "dragnet clause" be applicable? (5%)

Suggested Answer:

- a. Yes. X executed a real estate mortgage containing a "blanket mortgage clause." Mortgages given to secure future advancements are valid and legal contracts, and the amounts named as consideration in said contracts do not limit the amount for which the mortgage may stand as security if from the four corners of the instrument the intent to secure future and other indebtedness can be gathered. (Prudential Bank vs. Alviar, 464 SCRA 353, G.R. No. 150197 July 28, 2005)
- b. A "dragnet clause" is one which is specifically phrased to subsume all debts of past or future origins. Such clauses are "carefully scrutinized and strictly construed." Mortgages of this character enable the parties to provide continuous dealings, the nature or extent of which may not be known or anticipated at the time, and they avoid the expense and inconvenience of executing a new security on each new transaction. A "dragnet clause" operates as a convenience and accommodation to the borrowers as it makes available additional funds without their having to execute additional security documents, thereby saving time, travel, loan closing costs, costs of extra legal services, recording fees, et cetera. (Prudential Bank vs. Alviar, 464 SCRA 353, G.R. No. 150197 July 28, 2005)

Dragnet clause may not apply when the mortgagor takes another loan for which another security was given. It could not be inferred that such loan was made in reliance solely on the original security with the "dragnet clause," but rather, on the new security given. This is the "reliance on the security test." (Prudential Bank vs. Alviar, 464 SCRA 353, G.R. No. 150197 July 28, 2005)

On X's failure to pay his loan to ABC Bank, the latter foreclosed the Real Estate Mortgage he executed in its favor. The auction sale was set for Dec. 1, 2010 with the notices of sale published as the law required. The sale was, however, cancelled when Dec. 1, 2010 was declared a holiday and re-scheduled to Jan. 10, 2011 without republication of notice. The auction sale then proceeded on the new date. Under the circumstances, the auction sale is (BAR 2011)

a. rescissible.

- b. unenforceable.
- c. void.
- d. voidable.

X constituted a chattel mortgage on a car (valued at Php1 Million pesos) to secure a P500,000.00 loan. For the mortgage to be valid, X should have (BAR 2011)

- a. the right to mortgage the car to the extent of half its value.
- b. ownership of the car.
- c. unqualified free disposal of his car.
- d. registered the car in his name.

X, at Y's request, executed a Real Estate Mortgage (REM) on his (X's) land to secure Y's loan from Z. Z successfully foreclosed the REM when Y defaulted on the loan but half of Y's obligation remained unpaid. May Z sue X to enforce his right to the deficiency? (BAR 2011)

- a. Yes, but solidarily with Y.
- b. Yes, since X's is deemed to warrant that his land would cover the whole obligation.
- c. No, since it is the buyer at the auction sale who should answer for the deficiency.
- d. No, because X is not Z's debtor.

Which phrase best completes the statement - A chattel mortgage can be constituted to secure:

- a. obligations both past and future; (BAR 2012)
- b. obligations existing at the time the mortgage is constituted;
- c. future obligations only;
- d. past obligations only.

Which phrase best completes the statement - A chattel mortgage can cover: (BAR 2012)

- a. only property described in the deed without exception;
- b. can also cover substituted property:
- c. <u>properties described in the deed except in case of stock in trade being a</u> substitute;
- d. after acquired property.

Which phrase best completes the statement - The Deed of Chattel mortgage, if not registered with the Register of Deeds where debtor resides: (BAR 2012)

- a. is not valid, hence not binding between the mortgagor and the mortgagee;
- b. <u>is binding between the mortgagor and the mortgagee but will not affect third party;</u>
- c. to be valid between the mortgagor and the mortgagee, it must be coupled with the delivery of the subject matter of the chattel mortgage;

Which phrase best completes the statement - To bind third parties, a chattel mortgage of shares of stock must be registered: (BAR 2012)

- a. with the Register of Deeds where the debtor resides;
- b. with the Register of Deeds where the principal office of the corporation is;
- c. in the Stock and Transfer Book of the corporation with the Corporate Secretary;
- d. with the Register of Deeds where the debtor resides and the principal office of the corporation.

Which phrase best completes the statement - The affidavit of good faith in a Deed of Chattel Mortgage is: (BAR 2012)

- a. an oath where the parties swear that the mortgage is made for the purpose of securing the obligations specified and that the obligation is just and valid;
- b. an affidavit, the absence of which will vitiate the mortgage between the parties;
- c. necessary only if the chattel being mortgaged are growing crops;
- d. a certification from the mortgagor that he is the mortgagor of the chattel.

X defaulted in his loan with Y. Y instituted extra-judicial foreclosure of the property subject of a real estate mortgage that secured the loan. X has one year within which to redeem the property. After the foreclosure, X filed an action questioning the validity of the extra-judicial foreclosure sale. Which statement is most accurate? (BAR 2012)

- a. The one (1) year period within which to redeem will be interrupted by the filing of an action questioning the validity of the foreclosure.
- b. The one (1) year period will not be interrupted by the filing of the action.
- c. The one (1) year period will be extended for another year because of the filing of an action questioning the validity of the foreclosure sale.
- d. If the action which questions the validity of the foreclosure prospers, the period will be interrupted.

What is the effect if the proceeds in an extra-judicial foreclosure sale is not sufficient to pay for the obligation? (BAR 2012)

- a. the mortgagee can claim for deficiency judgment from the debtor.
- b. the mortgagee can claim for deficiency judgment from the mortgagor even though it is a third party mortgage.
- c. the mortgagee has no more recourse or claim against the debtor.
- d. the mortgagee cannot claim for deficiency judgment from the debtor because its an extrajudicial foreclosure.

X mortgaged her residential house and lot in favor of ABC Bank. X defaulted in her loan and so the bank foreclosed the real estate mortgage on the residential house. Y then bought the residential house and lot before the expiration of the redemption period. Can Y now take possession of the property? (BAR 2012)

- a. No, because it is still covered by the redemption period and the purchaser is not yet entitled as a matter of right to take possession of the property.
- b. Yes, the purchaser is now entitled to the possession of the house.
- c. No, because there is a need to talk to X to leave the house.
- d. No, because Y was not the one who foreclosed the mortgage on the property.

A. Anti-Money Laundering Act (R.A. No. 9160, as amended by R.A. No. 9194)

Prosperous Bank is a domestic bank with head office in Makati. It handles the banking requirements of thousands of clients.

The AMLC initiated a discreet investigation of the financial transactions of Lorenzo, a suspected drug trafficker based in Naga City. The intelligence group of the AMLC, in coordination with the counterpart group from the PDEA and the NBI, gathered ample evidence establishing Lorenzo's unlawful drug activities. The AMLC had probable cause that his deposits and investments in various banks, including Prosperous Bank, were related to money laundering.

Accordingly, the AMLC now transmits to Prosperous Bank a formal demand to allow its agents to examine the banking transactions of Lorenzo, but Prosperous Bank refuses the demand.

Is Prosperous Bank's refusal justified? Explain your answer. (4%) (2017 BAR)

Suggested Answer:

Prosperous Bank's refusal is not justified. Notwithstanding provisions of RA 1405, RA 6426 and RA 8791, the AMLC may inquire into or examine any particular deposit or Investment with any bank and non-bank financial institution if there is a probable cause that the deposits are related to unlawful activity under the Anti-money laundering law as in this case. Bank inquiry order from the court is not necessary since the predicate crime is violation of the Dangerous Drugs Law (Sectio of RA 9160, as amended).

Flora, a frequent traveller, found a purse concealed between the cushions of a large sofa inside the VIP lounge in NAIA while she was waiting for her flight to be called. Inside the purse was a very valuable diamond-studded necklace. She decided not to turn over the purse to the airport management, and instead to keep it. On her return from her travels, she had a dependable jeweller appraise the necklace, and the latter told her that the necklace was easily worth at least \$\int\$5,000,000.00 in the open market. To test the appraisal, she pawned the necklace for \$\int\$2,000,000.00. She then deposited the entire amount in her checking account with Metro Bank. Promptly, Metro Bank reported the transaction to the Anti-Money Laundering Council (AMLC).

Given that her appropriation of the necklace was theft; may Flora be successfully prosecuted for money laundering? Explain briefly your answer. (4%) (2017 BAR)

Flora may not be prosecuted for money laundering. Money laundering is a crime whereby the proceeds of an unlawful activity are transacted, thereby making it appear that they originated from legitimate sources. One ways of committing money laundering is if a person knows the cash relates to unlawful activity and transaction. Under the rules implementing the Anti-Money Laundering Law, however, only qualified theft (not simple theft) is considered an unlawful activity. In the case presented the theft committed by Flora did not become qualified because it was no committed with grave abuse of discretion.

Rudy is jobless but is reputed to be a jueteng operator. He has never been charged or convicted of any crime. He maintains several banks accounts and has purchased 5 houses and lots for his children from the Luansing Realty, Inc. since he does not have any visible job, the company reported his purchases to the AMLC. Thereafter, AMLC charged him with violation of the Anti-Money Laundering Law. Upon request of the AMLC, the bank disclosed to it Rudy's bank deposits amounting to P100 M. Subsequently, he was charged in court for violation of the Anti-Money Laundering Law.

Can Rudy move to dismiss the case on the ground that he has no criminal record?

Suggested Answer:

No. As with any crime, the absence of a criminal record is not a defense against a charge for violation of the Anti-Money Laundering Law. Moreover, having a criminal record is not an element of Money Laundering Offense defined under Section 4 of the Anti-Money Laundering Law.

To raise funds for his defense, Rudy sold the houses and lots to a friend. Can Luansing Realty, Inc. be compelled to transfer to the buyer ownership of the houses and lots?

Suggested Answer:

Yes. In the absence of a freeze order on the subject houses and lots pending criminal proceedings against Rudy, the ownership thereof may be validly transferred to another, and Luansing Realty, Inc. can be compelled to recognize the rights of the buyer as the new owner. Section 7(6) in relation to Section 10 of the Anti-Money Laundering Law required an Order from the Court of Appeals for the freezing of any money or property believed to be the proceeds of any unlawful activity.

In disclosing Rudy's bank accounts to the AMLC, did the bank violate any law?

Suggested Answer:

Yes. The bank violated RA No. 1405 (Secrecy of Bank Deposits Act), which considers all deposits of whatever nature with banks or banking institutions as absolutely

confidential and may not be examined, inquired or looked into by any person, government officials, bureau or office except upon depositor's written permission; in cases of impeachment; upon order of a competent court in cases of bribery of, or dereliction of duty by public official; and in cases where the money deposited or invested is the subject matter of the litigation. The disclosure was made before Rudy was charged in court for violation of the Anti-Money Laundering Law. Hence, his deposits were technically not yet the subject matter of litigation.

Moreover, under RA No. 9160, the AMLC may inquire into or examine any particular deposit or investment with any banking institution upon order of any competent court for violation of the said Act. In the case at bar, the AMLC merely requested the disclosure; it did not secure the requisite court order. The bank, therefore, was under no obligation to disclose Rudy's deposits.

- A. Policy of the Law
- **B. Covered Institutions**
- C. Obligations of Covered Institutions

Under the Anti-Money Laundering Law, a covered institution is required to maintain a system of verifying the true identity of their clients as well as persons purporting to act on behalf of

- a. Those doing business with such clients.
- b. Unknown principals.
- c. The covered institution.
- d. Such clients.

Suggested Answer:

d. Such clients. (BAR 2011)

The Anti-Money Laundering Law is a law that seeks to prevent money laundering activities by providing for more transparency in the Philippine Financial System, hence the following institutions are covered by the law, except:

- A. Bank and any financial institutions;
- B. Pawnshops;
- C. Casino operators;
- D. All of the above.

Suggested Answer:

- C. Casino operators. (BAR 2012)
 - D. Covered Transactions
 - E. Suspicious Transactions

What is the distinction between a "covered transaction report" and a "suspicious transaction report"? (2015)

A covered transaction report involves transaction/s in cash or other equivalent monetary instrument involving a total amount in excess of 500k within one banking day while suspicion transaction report involves transactions with covered institutions regardless of the amounts involved made under any of the suspicious circumstances enumerated by law.

Does the Anti-Money Laundering Council have the authority to freeze deposits? Explain. (2015)

Suggested Answer:

No. The authority to freeze deposits is lodged with and based upon the order of the Court of Appeals (Section 10 of RA 9160 as amended).

For purposes of determining violation of the provisions of the Anti-Money Laundering Law, a transaction is considered as a "Suspicious Transaction" with "Covered Institutions" regardless of the amount involved, where which the following circumstances exists?

- A. The amount involved is not commensurate with the client's business or financial capacity;
- B. There is no underlying legal or trade obligation, purpose or economic justification
- C. Client is not properly identified;
- D. All of the above.

Suggested Answer:

- D. All of the above. (BAR 2012)
 - F. When Is Money Laundering Committed
 - G. Unlawful Activities or Predicate Crimes

Name at least 5 predicate crimes to money laundering.

Suggested Answer:

- 1. Kidnapping for ransom under Article 267 of Act no. 3815, otherwise known as the RPC, as amended;
- 2. Sections 3,4,5,7,8, and 9 of Article Two of R.A. No. 6425, as amended, otherwise known as the Dangerous Drugs Act of 1972;
- 3. Section 3 paragraphs B,C,E,G,H, and I of R.A. No. 3019, as amended, otherwise known as the Anti-Graft and Corrupt Practices Act;
- 4. Plunder under R.A. No. 7080, as amended;
- 5. Robbery and extortion under Articles 294, 295, 296, 300, 301, and 302 of the RPC, as amended:
- 6. Jueteng and Masiao punished as illegal gambling under PD No. 1602;

- 7. Piracy on the high seas under the RPC, as amended and PD No. 532;
- 8. Qualified theft under Article 310 of the RPC, as amended;
- 9. Swindling under Article 315 of the RPC, as amended;
- 10. Smuggling under R.A. Nos. 455 and 1937;
- 11. Violations under RA No. 8792, otherwise known as the Electronic Commerce Act of 2000:
- 12. Hijacking and other violations under RA No. 6235; destructive arson and murder, as defined under the RPC, as amended, including those perpetrated by terrorists against non-combatant persons and similar targets;
- 13. Fraudulent practices and other violations under RA No. 8799, otherwise known as the SRC of 2000:
- 14. Felonies or offenses of a similar nature that are punishable under the penal laws of other countries.
- H. Anti-Money Laundering Council
- I. Functions
- J. Freezing of Monetary Instrument or Property

Under AMLA, a depositor's bank account may be frozen.

- a. By the bank when the account is the subject of a suspicious or covered transaction report;
- b. By the AMLC when the account belongs to a person already convicted of money laundering;
- c. By the RTC, upon ex parte motion by the AMLC, in a criminal prosecution for money laundering pending before it;
- d. By the Court of Appeals *motu proprio* in an appeal from a judgment of conviction of a criminal charge for money laundering;
- e. None of the above.

Suggested Answer:

- e) None of the above. (BAR 2013)
 - K. Authority to Inquire Into Bank Deposits
- C. Foreign Investments Act (R.A. No. 7042)
 - A. Policy of the Law
 - **B.** Definition of Terms
 - 1. Foreign Investment
 - 2. "Doing Business" in the Philippines
 - 3. Export Enterprise
 - 4. Domestic Market Enterprise
 - C. Registration of Investments on Non-Philippine Nationals
 - D. Foreign Investments in Export Enterprise
 - E. Foreign Investments in Domestic Market Enterprise

What does "doing business in the Philippines" under the Foreign Investments Act of 1991 mean? (2016 BAR)

Suggested Answer:

The phrase "doing business in the Philippines" under the Foreign Investments Act of 1991 shall include soliciting orders, service contracts, opening offices, whether called "liaison" offices or branches; appointing representatives or distributors domiciled in the Philippines or who in any calendar year stay in the country for a period or periods totalling one hundred eighty (180) days or more; participating in the management, supervision or control of any domestic business, firm, entity or corporation in the Philippines; and any other act or acts that imply a continuity of commercial dealings or arrangements, and contemplate to that extent the performance of acts or works, or the exercise of some of the functions normally incident to, and in progressive prosecution of, commercial gain or of the purpose and object of the business organization: Provided, however. That the phrase "doing business: shall not be deemed to include mere investment as a shareholder by a foreign entity in domestic corporations duly registered to do business, and/or the exercise of rights as such investor; nor having a nominee director or officer to represent its interests in such corporation; nor appointing a representative or distributor domiciled in the Philippines which transacts business in its own name and for its own account

A foreign company has a distributor in the Philippines. The latter acts in his own name and account. Will this distributorship be considered as doing business by the foreign company in the Philippines? (2015)

Suggested Answer:

The appointment of a distributor in the Philippines is not sufficient to constitute doing business unless it is under the full control of the foreign corporation. If the distributor is an independent entity doing business for its own name and account, the latter cannot be considered as doing business (Steel Case v. Design International Selection, GR No 171995, April 18, 2012).

A foreign delegation of business man and investment bankers called on your law firm to discuss the possibilities of investing in various projects in the Philippines, and wanted your thoughts on certain issues regarding foreign investments in the Philippines.

The delegation asked: aside from Filipino citizens, what entities would fall under the definition of "Philippine National" under FIA '91?

You replied that the definition of "Philippine National" under FIA '91 covers ____.

- a. Domestic partnership wholly composed of Filipino citizens;
- b. Domestic corporations 60% of whose capital stock, outstanding and entitled to vote, are owned and held by Filipino citizens;

- c. Foreign corporations considered as doing business in the Philippines under the Corporation Code, 100% of whose capital stock, outstanding and entitled to vote, are wholly-owned by Filipino citizens;
- d. All of the above, because the law considers the juridical personality, whether domestic or foreign, as a mere medium; the test of nationality is on the individuals who control the medium;
- e. None of the above, because the term Philippine national can only cover individuals and not juridical entities.

d. All of the above, because the law considers the juridical personality, whether domestic or foreign, as a mere medium; the test of nationality is on the individuals who control the medium. (BAR 2013)

The delegation heard that foreigners can invest up to 100% of the equity in "export oriented enterprises" and you were asked exactly what the term covers.

You replied that an "export oriented enterprises" under FIA '91 is an enterprise that

- a. Only engages in the export of goods and services, and does not sell goods or services to the domestic market;
- b. Exports consistently at least 40% of its goods or services, and sells at least 60% of the rest to the domestic market;
- c. Exports consistently at least 60% of the goods or services produced, and sells at least 40% of the rest to the domestic market;
- d. Exports consistently at least 60% of its goods or services produced, and can sell goods or services to the domestic market;
- e. None of the above.

Suggested Answer:

e. None of the above. (BAR 2013)

As a last question and by way of a concrete example, a delegation member finally inquired— which of the following corporations or businesses in the Philippines may it invest and up to what extent?

- a. A lifestyle magazine publication corporation up to 40% equity;
- b. An advertising corporation, up to 100% equity;
- c. A commercial bank, up to 60% equity;
- d. A jeepney manufacturing corporation, up to 100% equity;
- e. A real estate development corporation, up to 60% equity.

Suggested Answer:

d) A jeepney manufacturing corporation, up to 100% equity. (BAR 2013)

F. Foreign Investment Negative List

The main feature of the Foreign Investment Act of 1991 is to introduce the concept of "Negative Lists". Under the said law, what is a "Negative List"?

- a. It is a list of business activities or enterprises in the Philippines that foreigners are disqualified to engage in;
- b. It is a list of business activities or enterprises in the Philippines that foreigners are qualified to engage in;
- c. It is a list of business activities or enterprises that are open to foreign investments provided it is with the approval of the Board of Investment.
- d. It is a list of business activities or enterprises that are open to foreign investments provided it is with the approval of the SEC.

Suggested Answer:

a) It is a list of business activities or enterprises in the Philippines that foreigners are disqualified to engage in. (BAR 2012)

A foreign delegation of business man and investment bankers called on your law firm to discuss the possibilities of investing in various projects in the Philippines, and wanted your thoughts on certain issues regarding foreign investments in the Philippines.

The delegation has been told about the Foreign Investments Act of 1991, as amended (FIA '91), and they asked what exactly is the law's essential thrust regarding foreign investments in Philippine business and industries.

You replied that FIA '91 essentially reflects _____.

- a. The "Filipino First Policy";
- b. The "Foreign Investments Positive Lists" concept;
- c. The "Foreign Investments Negative Lists" concept;
- d. The "Control Test" concept;
- e. All of the above.

Suggested Answer:

c) The "Foreign Investments Negative Lists" concept. (BAR 2013)

Truth In Lending Act (R.A. No. 3765)

A. Disclosure Requirement

Dana Gianina purchase on a 36-month installment basis the latest model of the NISSAN Sentra Sedan car from the Jobel Cars, Inc. In addition to the advertised selling price, the latter imposed finance charges consisting of interests, fees and service charges. It did not, however, submit to Dana a written statement setting forth therein the information required by the Truth in Lending Act (RA No. 3765). Nevertheless, the conditional deed of sale which the parties executed mentioned that the total amount indicated therein included such finance charges.

Has there been substantial compliance of the aforesaid Act?

Suggested Answer:

No. there was no substantial compliance with the Truth in Lending Act. The law provides that the creditor must make a full disclosure of the credit cost. The statement that the total amount due includes the principal and the financial charges, without specifying the amounts due on each portion thereof would be insufficient and unacceptable.

If your answer to the foregoing question is in the negative, what is the effect of the violation on the contract?

Suggested Answer:

A violation of the Truth in Lending Act will not adversely affect the validity of the contract itself.

XYZ Corporation bought 10 units of Honda Civic from CCC Corporation. ABC Bank granted a loan to XYC Corporation which executed a financing agreement which provided for the principal amount, the installment payments, the interest rates and the due dates. On due dates of the installment payments, XYZ Corporation was asked to pay for some handling charges and other fees which were not mentioned in the financing Agreement. Can XYC Corporation refuse to pay the same?

- a. No, because handling charges and other fees are usual in certain banking transactions:
- b. Yes, because ABC Bank is required to provide XYZ Corporation not only the amount of the monthly installments but also the details of the finance charges as required by the Truth in Lending Act;
- c. No, because the Financing Agreement is a valid document to establish the existence of the obligation;
- d. Yes, because legally, finance charges are never allowed in any banking transaction.

Suggested Answer:

b) Yes, because ABC Bank is required to provide XYZ Corporation not only the amount of the monthly installments but also the details of the finance charges as required by the Truth in Lending Act. (BAR 2012)

TRUE or FALSE. A loan agreement which provides that the debtor shall pay interest at the rate determined by the bank's branch manager violates the disclosure requirement of the Truth in Lending Act.

Suggested Answer:

True. This is contrary to the duty of the creditor to disclose in detail the interests, charges and other figures indicating in detail the cost of the credit granted to the debtor. (BAR 2009)

PDIC Law

When OCCIDENTAL Bank folded up to insolvency, Manuel had the following separate deposits in his name; P200,000 in savings deposit; P250,000 in time deposit; P50,000 in a current account; P1 M in a trust account; and P3 M in money market placement. Under the PDIC Act, how much could Manuel recover?

Suggested Answer:

Manuel can recover P500,000 because this is the total of his savings deposit, time deposit and current account. The trust account and the money market placements are not included in the insured deposits. (BAR 2010)

X is a depositor of AAA Bank. She has 3 deposit accounts all under her name. One, in checking account, one in saving account and another one in time deposit account. Each account has a balance of P250,000. AAA Bank became insolvent. PDIC closed the Bank. X therefore is unable to withdraw from all of the accounts. She then filed her claims with the PDIC. Which statement is most accurate?

- a. X can claim a total of P500,000 for all 3 accounts;
- b. X can only claim from 1 account of P250,000;
- c. X can claim a total of P750,000 from all 3 accounts;
- d. X cannot claim anything from any of the deposit accounts.

Suggested Answer:

a) X can claim a total of P500,000 for all 3 accounts. (BAR 2012)

Warehouse Receipts Law

- A. Definitions
- **B.** Three Functions of Documents of Title
- C. Negotiability of Warehouse Receipts
- D. Formalities
- E. Negotiation of Warehouse Receipts
 - 1. By Delivery

For a fee, X deposited 1,000 sacks of corn in the warehouse owned by Y. Y is in the business of warehousing. Y issued a warehouse receipt as proof of the possession of the 1,000 sacks of corn. The warehouse receipt states as follows: "Deliver to X or bearer 1,000 sacks of corn." X wanted to use the warehouse receipt as payment of his debt in favor of Z. how can the ownership of the goods covered b the warehouse receipt be transferred?

- a. Negotiate the warehouse receipt by just delivering the warehouse receipt to Z.
- b. Assign the warehouse receipt to Z to transfer ownership of the goods.
- c. Negotiate the warehouse receipt by specifically indorsing it to Z.
- d. The warehouse receipt in this case is non-negotiable.

Suggested Answer:

a) Negotiate the warehouse receipt by just delivering the warehouse receipt to Z. (BAR 2012)

2. By Indorsement

- F. Effects of Negotiation of Warehouse Receipt
- **G.** Warranties
- H. Non-negotiable Receipts
- I. Warehouseman's defenses for Non-delivery or Misdelivery

The warehouseman, by issuing the warehouse receipt, acknowledges that the goods are in possession, but he can refuse to deliver the goods to the holder of the warehouse receipt covering the goods if—

- a. The warehouse receipt covering the goods is not presented;
- b. The lien of the warehouseman is not satisfied;
- c. The said holder presents a materially altered warehouse receipt;
- d. All of the above.

Suggested Answer:

All of the above. (BAR 2012)

J. Loss of the Receipt

To guarantee the payment of a loan obtained from a bank, Raoul pledged 500 bales of tobacco deposited in a warehouse to said bank and endorsed in blank the warehouse receipt. Before Raoul could pay for the loan, the tobacco disappeared from the warehouse.

Who should bear the loss—the pledgor or the bank? Why?

Answer:

The pledgor should bear the loss. In the pledge of a warehouse receipt the ownership of the goods remain with depositor or his transferee. Any contract or real security, among them a pledge, does not amount to or result in an assumption of risk of loss by the creditor. The Warehouse Receipts Law did not deviate from this rule. (BAR 1992)

K. Warehouseman's Liability

The authorized alteration of a warehouse receipt which does not change its tenor renders the warehouseman liable according to the term of the receipt.

- a. In its original tenor if the alteration is material.
- b. In its original tenor.
- c. As altered if there is fraud.
- d. As altered.

B. In its original tenor. (BAR 2011)

L. Warehouseman's Lien

X, warehouseman, sent a text message to Y, to whom X had issued a warehouse receipt for Y's 500 sacks of corn, notifying him of the due date and time to settle the storage fees. The message stated also that if Y does not settle the warehouse charges within 10 days, he will advertise the goods for sale at a public auction. When Y ignored the demand, X sold 100 sacks of corn at a public auction. For X's failure to comply with the statutory requirement of written notice to satisfy his lien, the sale of the 100 sacks of corn is

- a. Voidable.
- b. Rescissible.
- c. Unenforceable.
- d. Void.

Suggested Answer:

e. Void. (BAR 2011)

TRUE or FALSE. Under the Warehouse Receipts Law, a warehouseman loses his lien upon the goods when he surrenders possession thereof.

Suggested Answer:

True. A lien is dependent on possession. When a warehouseman surrenders possession, he thereby loses his lien on the goods over which he no longer has possession. (BAR 2009)

M. Adverse Claimant

G, a grocery goods supplier, sold 100 sacks of rice to H who promised to pay once he has sold all the rice. H, in the meantime, delivered the goods to W, a warehouseman, who issued a warehouse receipt. Without the knowledge of G and W, H negotiated the receipt to P who acquired it in good faith and for value. P then claimed the goods from W, who released them. After the rice was loaded on a ship bound for Manila, G invokes his right to stop the goods in transit due to his unpaid lien. Who has a better right to the rice?

- A. P, since he has superior rights as a purchaser for value and in good faith.
- B. P, regardless of whether or not he is a purchaser for value and in good faith.
- C. G, since as an unpaid seller, he has the right of stoppage in transitu.
- D. W, since it appears that the warehouse charges have not been paid.

A. P, since he has superior rights as a purchaser for value and in good faith. (BAR 2011)

X, creditor of Y, obtained a judgment in his favor in connection with Y's unpaid loan to him. The court's sheriff then levied on the goods that Y stored in T's warehouse, for which the latter issued a warehouse receipt. A month before the levy, however, Z bought the warehouse receipt for value. Who has a better right over the goods?

- A. T, being the warehouseman with a lien on the goods.
- B. Z, being a purchaser for value of the warehouse receipt.
- C. X, being Y's judgment creditor.
- D. Y, being the owner of the goods.

Suggested Answer:

B. Z, being a purchaser for value of the warehouse receipt. (BAR 2011)

T delivers two refrigerators to the warehouse of W who then issues a negotiable receipt undertaking the delivery of the refrigerators to "T or bearer". T entrusted the receipt to B for safekeeping only. B negotiated it, however, to F who bought it in good faith and for value. Who is entitled to the delivery of the refrigerators?

- a. T, since he is a real owner of the refrigerators.
- b. F, since he is a purchaser in good faith and for value.
- c. B, since T entrusted the receipt to him.
- d. W, since he has as a warehouseman a lien on the goods.

Suggested Answer:

b. F, since he is a purchaser in good faith and for value. (BAR 2011)

The legal remedy of the warehouseman in case of conflicting claims is to—

- A. File an action for interpleader;
- B. Give the goods to the first one who first presented the warehouse receipt;
- C. Use his discretion as to who he believes has the prior right;
- D. Keep the goods and appropriate them to himself.

Suggested Answer:

A. File an action for interpleader. (BAR 2012)

N. Attachment or Levy

A Warehouse Company received for safekeeping 1000 bags of rice from a merchant. To evidence the transaction, the Warehouse Company issued a receipt expressly providing that the goods be delivered to the order of said merchant.

A month after, a creditor obtained judgment against the said merchant for a sum of money. The sheriff proceeded to levy on the rice and directed the Warehouse Company to deliver to him the deposited rice.

What advice will you give the Warehouse Company? Explain your answer.

Suggested Answer:

The 1000 bags of rice were delivered to the Warehouse Company by a merchant, and a negotiable receipt was issued therefore. The rice cannot thereafter, while in possession of the Warehouse Company, be attached by garnishment or otherwise, or be levied upon under an execution unless the receipt be first surrendered to the warehouseman, or its negotiation enjoined. The Warehouse Company cannot be compelled to deliver the actual possession of the rice until the receipt is surrendered to it or impounded by the court.

Financial Rehabilitation and Insolvency Act (FRIA)

Wyatt, an Internet entrepreneur, engaged in a sideline business of creating computer programs for selected clients on a per project basis and for servicing basic computer problems of his friends and family members. His main job was being an IT consultant at Futures Co., a local computer company.

Because of his ill-advised investments in the stock market and the fraud perpetrated against him by his trusted confidente, Wyatt was already drowning in debt, that is, he had far more liabilities than his entire assets.

What legal recourse remained available to Wyatt? Explain your answerr. (5%) (2017 BAR)

Suggested Answer:

If Wyatt is registered as sole proprietorship, he may file a petition for rehabilitation or voluntary liquidation. Under FRIA, an insolvent debtor may file a petition for rehabilitation even if the assets are less than liabilities. The petition should include a rehabilitation plan and nominee for rehabilitation receiver. He can also file a petition for voluntary liquidation since his liabilities exceed his assets. The objective of liquidation is to get discharge, maximize recovery of assets and effect equitable distribution of such assets based on the rules on concurrence and preference of credit.

If he is not registered as a sole proprietorship, he may only file petition for voluntary liquidation since his assets are less than liabilities (Section 103 of FRIA). Petition for suspension of payments is not available as a remedy to an individual debtor not registered as a sole proprietorship

Hortencio owned a modest grocery business in Laguna. Because of the economic downturn, he incurred huge financial liabilities. He remained afloat only because of the properties inherited from his parents who had both come from landed

families in Laguna. His main creditor was Puresilver Company (Puresilver), the principal supplier of the merchandise sold in his store. To secure his credit with Puresilver, he executed a real estate mortgage with a dragnet clause involving his family's assets worth several millions of pesos.

Nonetheless, Hortencio, while generally in the black, now faces a situation where he is unable to pay his liabilities as they fall due in the ordinary course of business. What will you advise him to do to resolve his dire financial condition? Explain your answer. (5%) (2017 BAR)

Suggested Answer:

If Hortencio is doing business as a registered sole proprietorship he can file a petition for rehabilitation. Under FRIA, a sole proprietorship can now file a petition for rehabilitation. The remedy may be availed of in case of actual or technical insolvency. In the petition, he can pray for the issuance of a commencement order which includes a stay order. The stay order, once issued, has the effect of enjoining the enforcement of claim against Hortencio. If Hortencio is not registered as a sole proprietorship, he can file a petition for suspension of payments in the city or province in which he has resided for six months prior to the filing of the petition, a remedy available to an individual debtor who has more assets than liabilities but foresees the Impossibility of paying his debts when they respectively fall due (Section 94, FRIA).

DMP Corporation (DMP) obtained a loan of P20 M from National Bank (NB) secured by a real estate mortgage over a 63,380-square meter land situated in Cabanatuan City. Due to the Asian Economic Crisis, DMP experienced liquidity problems disenabling it from paying its loan on time. For that reason, NB sought the extrajudicial foreclosure of the said mortgage by filing a petition for sale on June 30, 2003. On September 4, 2003, the mortgaged property was sold at public auction, which was eventually awarded to NB as the highest bidder. That same day, the Sheriff executed a Certificate of Sale in favor of NB.

On October 21, 2003, DMP filed a Petition for Rehabilitation before the RTC. Pursuant to this, a Stay Order was issued by the RTC on October 27, 2003.

On the other hand, NB caused the recording of the Sheriff's certificate of Sale on December 3, 2003 with the Register of Deeds of Cabanatuan City. NB executed an Affidavit of Consolidation of Ownership and had the same annotated on the title of DMP. Consequently, the Register of Deeds cancelled DMP's title and issued a new title in the name of NB on December 10, 2003.

NB also filed on March 17, 2004 an Ex-Parte Petition for Issuance of Writ of Possession before the RTC of Cabanatuan City. After hearing, the RTC issued on September 6, 2004 an Order directing the Issuance of the Writ of Possession, which was issued on October 4, 2004.

DMP claims that all subsequent actions pertaining to the Cabanatuan property should have been held in abeyance after the Stay Order was issued by the rehabilitation court. Is DMP correct?

Suggested Answer:

No. DMP is not correct. Since the foreclosure of the mortgage and the issuance of the certificate of sale in favor of the mortgagee were done prior to the appointment of a Rehabilitation Receiver and the issuance of the Stay Order, all the actions taken with respect to the foreclosed mortgaged property which were subsequent to the issuance of the Stay Order were not affected by the Stay Order. Thus, after the redemption period expired without the mortgagor redeeming the foreclosed property, the mortgagee becomes the absolute owner of the property and it was within its right to ask for consolidation of title and the issuance of new title in its favor. The writ of possession procured by the mortgagee despite the subsequent issuance of Stay Order in the rehabilitation proceeding instituted is also valid. (BAR 2014)

A. Liquidation of Insolvent Juridical Debtors

a. Voluntary Liquidation

Under the Financial Rehabilitation and Insolvency Act (FRIA), the filing of a petition for voluntary rehabilitation must be approved by:

- A. A majority vote of the Board of Directors and authorized by the vote of the stockholders representing at least a majority of the outstanding capital stock.
- B. A majority vote of the Board of Directors and authorized by the vote of the stockholders representing at least 2/3 of the outstanding capital stock.
- C. 2/3 vote of the Board of Directors and authorized by the vote of the stockholders representing at least a majority of the outstanding capital stock.
- D. 2/3 vote of the Board of Directors and authorized by the vote of the stockholders representing at least 2/3 of the outstanding capital stock.

Suggested Answer:

b. A majority vote of the Board of Directors and authorized by the vote of the stockholders representing at least 2/3 of the outstanding capital stock. (BAR 2014)

b. Involuntary Liquidation

- c. Conversion by the Court into Liquidation Proceedings
- d. Powers of the SEC
- A. Insolvency of Individual Debtors
- a. Suspension of Payments

i. Petition

- ii. Action on the Petition
- iii. Actions suspended; Suspension Order

Procopio, a Director and the CEO of Parisian Hotel CO., Inc. (Parisian), was charged along with other company officials with several counts of estafa in connection with the non-remittance of SSS premiums the company had collected from its employees. During the pendency of the cases, Parisian filed a petition for rehabilitation. The court, finding the petition to be sufficient in form and substance, issued a commencement order together with a stay or suspension order. Citing the commencement order, Procopio and the other officers facing the criminal charges moved to suspend the proceedings in the estafa cases.

(a) What is a commencement order, and what is the effect of its issuance? Explain your answer. (4%) (2017 BAR)

Suggested Answer:

A commencement order is an order issued by the Rehabilitation Court if the petition for rehabilitation filed by the financially distressed debtor or by its creditor is sufficient in form and substance. The rehabilitation proceedings are commenced upon issuance by the rehabilitation court of a commencement order. The stay order which is included in the commencement order shall suspend all actions or proceedings for the enforcement of claims against the debtor (Section 16 of FRIA).

(b) Suppose you are the trial judge, will you grant the motion to, suspend of Procopio, et al.? Explain your answer. (4%)

Suggested Answer:

- (b) Under Section 18 of FRIA, the stay order does not in-clude criminal action against the individual debtor, or owner, partner, director or officer of the debtor.
 - iv. Creditors' Meeting
 - v. Persons who may refrain from voting
 - vi. Rejection of the proposed agreement
 - vii. Objections
 - viii. Effects of approval of proposed agreement
 - ix. Failure of individual debtor to perform agreement

b. Voluntary Liquidation

2.2.1 Application

ii. 2.2.2 Liquidation Order

c. Involuntary Liquidation

i. 2.3.1 The Petition

ii. 2.3.2 Acts of Insolvency

iii. 2.3.3 Order to Individual Debtor to Show Cause

iv. 2.3.4 Default

v. 2.3.5 Absent individual debtor

vi. 2.3.6 All property held for all creditors; Appeal bonds; Exemptions to sureties

vii. 2.3.7 Sale under execution

B. Common provisions

a. Determination of Claims

PA Assurance (PA) was incorporated in 1980 to engage in the sale of pre-need educational plans. It sold open-ended educational plans which guaranteed the payment of tuition and other fees to planholders irrespective of the cost at the time of availment. It also engaged in the sale of fixed value plans which guaranteed the payment of a pre-determined amount to planholders. In 1982, PA was among the country's top corporations. However, it subsequently suffered financial difficulties.

On September 8, 2005, PA filed a Petition for Corporate Rehabilitation before the RTC of Makati City. On October 17, 2005, 10 plan holders filed an Opposition and Motion to Exclude Planholders from Stay Order on the ground that planholders are not creditors as they (planholders) have a trust relationship with PA. Are the planholders correct?

Suggested Answer:

No. The planholders is not correct. On November 21, 2000, the Court approved the Interim Rules of Procedure on Corporate Rehabilitation of 2000 (Interim Rules), which took effect on December 15, 2000. The Interim Rules apply to petitions for rehabilitation filed by corporations, partnerships, and associations pursuant to PD 902-A, as amended. Under the Interim Rules, "claim" shall include "all claims or demands of whatever nature or character against the debtor or its property, whether for money or otherwise." "Creditor" shall mean "any holder of a claim." Hence, the claim of the planholders from PA is included in the definition of "claims" under the Interim Rules. (BAR 2014)

i. Registry of Claims

ii. Right of Set-off
iii. Opposition or Challenge to Claims

iv. Submission of Disputed to the Court b. Avoidance Proceedings

Retail Trade Law

With a capital of P92,000, Maria operates a stall in the public market. She manufactures soap that she sells to the general public. Her common law husband, Ma Lee, who has a pending petition for naturalization, occasionally finances the purchase of goods for resale, and assist in the management of business.

Is there a violation of the Retail trade Law? Explain.

Suggested Answer:

No, there is no violation of the Retail Trade Law. Maria is a manufacturer who sells to the general public, through her stall in the public market, the soap which she manufactures. Inasmuch as her capital does not exceed P5,000 then she is considered under Sec.4 (a) of the Retail Trade Law as not engaged in the "retail business". Inasmuch as Maria's business is not a "retail business," then the requirement in Section 1 of the Retail Trade Law that only Philippine nationals shall engage, directly or indirectly, in the retail business is inapplicable. For this reason, the participation of Ma Lee in the management of the business would not be a violation of the Retail Trade Law in relation to the Anti-Dummy Law.

Bulk Sales Law

Venezia is a famous international fashion chain outlets in Makati, Ortigas, and Manila. It has complied with the minimum capitalization required under the Retail Trade Nationalization Act and carries on retail business worth more than \$3 M for each outlets. As its Manila outlet is not doing very well, it decides to sell all of its business there consisting of remaining inventory, furniture and fixtures and other assets to its competitor.

Venezia's Manila outlet constitutes 1/3 of its total business. Should it comply with the requirements of the Bulk Sales Law? Why or why not?

Suggested Answer:

Venezia need not comply with the requirements of the Bulk Sales Law as its Manila outlet constitutes only 1/3 of its total business and, therefore, it would not be a sale of all or substantially all of the business conducted by Venezia. Moreover, the requirements of the Bulk Sales Law reflected in Sections 3, 4, 5, and 9, by the express language of

said provisions, apply only to the first type of bulk sales, i.e., to any sale, transfer, mortgage or assignment of a stock of goods, wares, merchandise, provisions or materials otherwise than in the ordinary course of trade and the regular prosecution of business of the vendor, mortgagor, transferor, or assignor, and not to the second type (as in the sale described in the problem) or the third type (i.e., sale, etc. Of all or substantially all of the fixtures and equipment used in and about the business). As the Bulk Sales Law is penal in nature, it should be interpreted strictly against the State.

If instead of selling its Manila outlet, Venezia merely mortgages its assets there, would it need to comply with the requirements of the Bulk Sales Law?

Suggested Answer:

For the same reasons stated in the answer to (1) above, Venezia need not comply with the requirements of the Bulk Sales Law. The second type of bulk sales also includes the mortgage of all or substantially all of the business of the mortgagor.

What are the legal consequences of a failure to comply with the requirements of a Bulk Sales Law?

Suggested Answer:

Failure to comply with the requirements of a Bulk Sales Law renders the sale, transfer, mortgage, or assignment fraudulent and void, and makes any person found guilty of violating any provision of the Bulk Sales Law punishable by imprisonment for not less than 6 months nor more than 5 years, or a fine in an amount not exceeding P5,000, or both such imprisonment and fine in the discretion of the court. (BAR 2010)

TRUE OR FALSE. Even if the seller and the buyer in a sale in bulk violate the Bulk Sales Law, the sale would still be valid.

Suggested Answer:

False. When the Bulk Sale Law is violated, the sale is null and void. When the provision of the said law have not been complied with, the sale is considered as being "fraudulent and void" and even when coupled with delivery, the title over the goods does not transfer to the buyer. However, the civil liabilities arising from the transaction remain enforceable between the parties thereto. (BAR 2009)

XXX Corporation (XXX) and its sister company, YYY Corporation (YYY), are both under judicial receivership. The receiver has the option to sell all or substantially all of the properties of YYY to XXX, or simply merge the two corporations. Under either option, the requirements under the Corporation Code have to be complied with.

The receiver seeks your advice on whether the Bulk Sales Law will apply to either, or both, options. What will your advice be?

Suggested Answer:

I will advice the receiver that the Bulk Sales Law does not apply to both options. Section 8 of the Bulk Sales Law expressly provides that it will not apply to executors, administrators, receivers, and assignees in insolvency, or public officers, acting under judicial process. In this case, the receiver is acting under judicial process. (BAR 2009)

Anti-Dummy Law

2009 BAR EXAMINATION

Cecilio is planning up a grocery store in the subdivision where he and his family reside. To promote this proposed business venture, he told his wife and 3 children to send out promotional text messages to all the residents in the subdivision. Cecilio's family members did as instructed, and succeeded in reaching, through text messages, more than 80% of the residents in the subdivision.

Is Cecilio habitually engaged in commerce even if the grocery store has yet to be established? Explain your answer.

Suggested Answer:

Yes. Even if the grocery store has yet to be established, Cecilio already habitually engaged in commerce, when per his instruction the members of his family contacted more than 80% the residents of the subdivision where they reside. According to Article 3 of the Code of Commerce, "legal presumption of habitually engaging in commerce shall exist from the moment the person who intends to engage therein announced through circulars, newspapers, handbills, posters exhibited to the public, or in any other manner whatsoever, an establishment which has for its object some commercial operation." Text messages may qualify to be equivalent to electronic documents.