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THIRD DIVISION

[G.R. No. 157479. November 24, 2010]

PHILIP TURNER and ELNORA TURNER, *petitioners, vs.* **LORENZO SHIPPING CORPORATION,** *respondent.*

SYLLABUS

1. **COMMERCIAL LAW; CORPORATIONS; STOCKHOLDER; RIGHT OF APPRAISAL; EXPLAINED.—** A stockholder who dissents from certain corporate actions has the right to demand payment of the fair value of his or her shares. This right, known as the right of appraisal, is expressly recognized in Section 81 of the *Corporation Code*. x x x [T]he right of appraisal may be exercised when there is a fundamental change in the charter or articles of incorporation substantially prejudicing the rights of the stockholders. It does not vest unless objectionable corporate action is taken. It serves the purpose of enabling the dissenting stockholder to have his interests purchased and to retire from the corporation.

2. **ID.; ID.; ID.; ID.; PAYMENT TO THE DISSENTING STOCKHOLDER MUST COME FROM THE CORPORATION'S UNRESTRICTED RETAINED EARNINGS.—** [N]o payment shall be made to any dissenting stockholder unless the corporation has unrestricted retained earnings in its books to cover the payment. In case the corporation has no available unrestricted retained earnings in its books, Section 83 of the *Corporation Code* provides that if the dissenting stockholder is not paid the value of his shares within 30 days after the award, his voting and dividend rights shall immediately be restored.

3. **ID.; ID.; ID.; ID.; ID.; TRUST FUND DOCTRINE, EXPLAINED.—** The *trust fund doctrine* backstops the requirement of unrestricted retained earnings to fund the payment of the shares of stocks of the withdrawing stockholders. Under the doctrine, the capital stock, property, and other assets of a corporation are regarded as equity in trust for the payment of corporate creditors, who are preferred in the distribution of corporate assets. The creditors of a corporation have the right to assume that the board of directors will not use the assets of

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the corporation to purchase its own stock for as long as the corporation has outstanding debts and liabilities. There can be no distribution of assets among the stockholders without first paying corporate debts. Thus, any disposition of corporate funds and assets to the prejudice of creditors is null and void.

4. **ID.; ID.; ID.; ID.; ID.; FOR A DISSENTING STOCKHOLDER TO HAVE A VALID CAUSE OF ACTION, THE UNRESTRICTED RETAINED EARNINGS MUST EXIST AT THE TIME OF THE DEMAND.—** That the respondent had indisputably no unrestricted retained earnings in its books at the time the petitioners commenced Civil Case No. 01-086 on January 22, 2001 proved that the respondent's legal obligation to pay the value of the petitioners' shares did not yet arise. Thus, the CA did not err in holding that the petitioners had no cause of action, and in ruling that the RTC did not validly render the partial summary judgment. x x x Section 1, Rule 2, of the *Rules of Court* requires that every ordinary civil action must be based on a cause of action. Accordingly, Civil Case No. 01-086 was dismissible from the beginning for being without any cause of action. The RTC concluded that the respondent's obligation to pay had accrued by its having the unrestricted retained earnings after the making of the demand by the petitioners. It based its conclusion on the fact that the *Corporation Code* did not provide that the unrestricted retained earnings must already exist at the time of the demand. The RTC's construal of the *Corporation Code* was unsustainable, because it did not take into account the petitioners' lack of a cause of action against the respondent. In order to give rise to any obligation to pay on the part of the respondent, the petitioners should first make a valid demand that the respondent refused to pay despite having unrestricted retained earnings. Otherwise, the respondent could not be said to be guilty of any actionable omission that could sustain their action to collect.

5. **ID.; ID.; ID.; ID.; ID.; ID.; SUBSEQUENT EXISTENCE OF UNRESTRICTED RETAINED EARNINGS DID NOT CURE THE LACK OF CAUSE OF ACTION AT THE TIME OF THE COMMENCEMENT OF THE ACTION.—** Neither did the subsequent existence of unrestricted retained earnings after the filing of the complaint cure the lack of cause of action in Civil Case No. 01-086. The petitioners' right of action could only spring from an *existing* cause of action. Thus, a complaint

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whose cause of action has not yet accrued cannot be cured by an amended or supplemental pleading alleging the existence or accrual of a cause of action during the pendency of the action. For, only when there is an invasion of primary rights, not before, does the adjective or remedial law become operative. Verily, a premature invocation of the court's intervention renders the complaint without a cause of action and dismissible on such ground. In short, Civil Case No. 01-086, being a groundless suit, should be dismissed. Even the fact that the respondent already had unrestricted retained earnings more than sufficient to cover the petitioners' claims on June 26, 2002 (when they filed their *motion for partial summary judgment*) did not rectify the absence of the cause of action at the time of the commencement of Civil Case No. 01-086. The *motion for partial summary judgment*, being a mere application for relief other than by a pleading, was not the same as the complaint in Civil Case No. 01-086. Thereby, the petitioners did not meet the requirement of the *Rules of Court* that a cause of action must exist at the commencement of an action, which is "commenced by the filing of the original complaint in court."

APPEARANCES OF COUNSEL

Beltran Beltran Rubrico Koa & Mendoza for petitioners.
Herrera Teehankee Faylona & Cabrera for respondent.

D E C I S I O N

BERSAMIN, *J.*:

This case concerns the right of dissenting stockholders to demand payment of the value of their shareholdings.

In the stockholders' suit to recover the value of their shareholdings from the corporation, the Regional Trial Court (RTC) upheld the dissenting stockholders, herein petitioners, and ordered the corporation, herein respondent, to pay. Execution was partially carried out against the respondent. On the respondent's petition for *certiorari*, however, the Court of Appeals (CA) corrected the RTC and dismissed the petitioners' suit on the ground that their cause of action for collection had

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not yet accrued due to the lack of unrestricted retained earnings in the books of the respondent.

Thus, the petitioners are now before the Court to challenge the CA's decision promulgated on March 4, 2003 in C.A.-G.R. SP No. 74156 entitled *Lorenzo Shipping Corporation v. Hon. Artemio S. Tipon, in his capacity as Presiding Judge of Branch 46 of the Regional Trial Court of Manila, et al.*[1]

Antecedents

The petitioners held 1,010,000 shares of stock of the respondent, a domestic corporation engaged primarily in cargo shipping activities. In June 1999, the respondent decided to amend its articles of incorporation to remove the stockholders' pre-emptive rights to newly issued shares of stock. Feeling that the corporate move would be prejudicial to their interest as stockholders, the petitioners voted against the amendment and demanded payment of their shares at the rate of ₱2.276/share based on the book value of the shares, or a total of ₱2,298,760.00.

The respondent found the fair value of the shares demanded by the petitioners unacceptable. It insisted that the market value on the date before the action to remove the pre-emptive right was taken should be the value, or ₱0.41/share (or a total of ₱414,100.00), considering that its shares were listed in the Philippine Stock Exchange, and that the payment could be made only if the respondent had unrestricted retained earnings in its books to cover the value of the shares, which was not the case.

The disagreement on the valuation of the shares led the parties to constitute an appraisal committee pursuant to Section 82 of the *Corporation Code*, each of them nominating a representative, who together then nominated the third member who would be chairman of the appraisal committee. Thus, the appraisal committee came to be made up of Reynaldo Yatco, the petitioners' nominee; Atty. Antonio Acyatan, the respondent's

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[1] *Rollo*, pp. 20-35; penned by Associate Justice Portia Aliño-Hormachuelos, with Associate Justice Jose L. Sabio, Jr. (retired) and Associate Justice Amelita G. Tolentino concurring.

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nominee; and Leo Anoche of the Asian Appraisal Company, Inc., the third member/chairman.

On October 27, 2000, the appraisal committee reported its valuation of ₱2.54/share, for an aggregate value of ₱2,565,400.00 for the petitioners.[2]

Subsequently, the petitioners demanded payment based on the valuation of the appraisal committee, plus 2%/month penalty from the date of their original demand for payment, as well as the reimbursement of the amounts advanced as professional fees to the appraisers.[3]

In its letter to the petitioners dated January 2, 2001,[4] the respondent refused the petitioners' demand, explaining that pursuant to the *Corporation Code*, the dissenting stockholders exercising their appraisal rights could be paid only when the corporation had unrestricted retained earnings to cover the fair value of the shares, but that it had no retained earnings at the time of the petitioners' demand, as borne out by its Financial Statements for Fiscal Year 1999 showing a deficit of ₱72,973,114.00 as of December 31, 1999.

Upon the respondent's refusal to pay, the petitioners sued the respondent for collection and damages in the RTC in Makati City on January 22, 2001. The case, docketed as Civil Case No. 01-086, was initially assigned to Branch 132.[5]

On June 26, 2002, the petitioners filed their *motion for partial summary judgment*, claiming that:

> 7) xxx the defendant has an accumulated unrestricted retained earnings of ELEVEN MILLION NINE HUNDRED SEVENTY FIVE THOUSAND FOUR HUNDRED NINETY (₱11,975,490.00) PESOS, Philippine Currency, evidenced by its Financial Statement as of the Quarter Ending March 31, 2002; xxx

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[2] *Id.,* p.127.

[3] *Id.,* p. 100.

[4] *Id.,* pp. 118-119.

[5] *Id.,* p. 120-124.

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> 8) xxx the fair value of the shares of the petitioners as fixed by the Appraisal Committee is final, that the same cannot be disputed xxx
>
> 9) xxx there is no genuine issue to material fact and therefore, the plaintiffs are entitled, as a matter of right, to a summary judgment. xxx[6]

The respondent opposed the *motion for partial summary judgment*, stating that the determination of the unrestricted retained earnings should be made at the end of the fiscal year of the respondent, and that the petitioners did not have a cause of action against the respondent.

During the pendency of the *motion for partial summary judgment*, however, the Presiding Judge of Branch 133 transmitted the records to the Clerk of Court for re-raffling to any of the RTC's special commercial courts in Makati City due to the case being an intra-corporate dispute. Hence, Civil Case No. 01-086 was re-raffled to Branch 142.

Nevertheless, because the principal office of the respondent was in Manila, Civil Case No. 01-086 was ultimately transferred to Branch 46 of the RTC in Manila, presided by Judge Artemio Tipon,[7] pursuant to the *Interim Rules of Procedure on Intra-Corporate Controversies* (Interim Rules) requiring intra-corporate cases to be brought in the RTC exercising jurisdiction over the place where the principal office of the corporation was found.

After the conference in Civil Case No. 01-086 set on October 23, 2002, which the petitioners' counsel did not attend, Judge Tipon issued an order,[8] granting the petitioners' *motion for partial summary judgment*, stating:

> As to the motion for partial summary judgment, there is no question that the 3-man committee mandated to appraise the shareholdings of

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[6] *Id.*, pp. 151-152.

[7] Already retired.

[8] *Rollo*, pp. 91-93.

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plaintiff submitted its recommendation on October 27, 2000 fixing the fair value of the shares of stocks of the plaintiff at ₱2.54 per share. Under Section 82 of the Corporation Code:

> "The findings of the majority of the appraisers shall be final, and the award shall be paid by the corporation within thirty (30) days after the award is made."
>
> "The only restriction imposed by the Corporation Code is—"
>
> "That no payment shall be made to any dissenting stockholder unless the corporation has unrestricted retained earning in its books to cover such payment."

The evidence submitted by plaintiffs shows that in its quarterly financial statement it submitted to the Securities and Exchange Commission, the defendant has retained earnings of ₱11,975,490 as of March 21, 2002. This is not disputed by the defendant. Its only argument against paying is that there must be unrestricted retained earning at the time the demand for payment is made.

This certainly is a very narrow concept of the appraisal right of a stockholder. The law does not say that the unrestricted retained earnings must exist at the time of the demand. Even if there are no retained earnings at the time the demand is made if there are retained earnings later, the fair value of such stocks must be paid. The only restriction is that there must be sufficient funds to cover the creditors after the dissenting stockholder is paid. No such allegations have been made by the defendant.[9]

On November 12, 2002, the respondent filed a *motion for reconsideration*.

On the scheduled hearing of the *motion for reconsideration* on November 22, 2002, the petitioners filed a *motion for immediate execution* and a *motion to strike out motion for reconsideration*. In the latter motion, they pointed out that the *motion for reconsideration* was prohibited by Section 8 of the Interim Rules. Thus, also on November 22, 2002, Judge Tipon

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[9] *Id.,* p. 92.

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denied the *motion for reconsideration* and granted the petitioners' *motion for immediate execution*.[10]

Subsequently, on November 28, 2002, the RTC issued a *writ of execution*.[11]

Aggrieved, the respondent commenced a special civil action for *certiorari* in the CA to challenge the two aforecited orders of Judge Tipon, claiming that:

A.

JUDGE TIPON GRAVELY ABUSED HIS DISCRETION IN GRANTING SUMMARY JUDGMENT TO THE SPOUSES TURNER, BECAUSE AT THE TIME THE "COMPLAINT" WAS FILED, LSC HAD NO RETAINED EARNINGS, AND THUS WAS COMPLYING WITH THE LAW, AND NOT VIOLATING ANY RIGHTS OF THE SPOUSES TURNER, WHEN IT REFUSED TO PAY THEM THE VALUE OF THEIR LSC SHARES. ANY RETAINED EARNINGS MADE A YEAR AFTER THE "COMPLAINT" WAS FILED ARE IRRELEVANT TO THE SPOUSES TURNER'S RIGHT TO RECOVER UNDER THE "COMPLAINT", BECAUSE THE WELL-SETTLED RULE, REPEATEDLY BROUGHT TO JUDGE TIPON'S ATTENTION, IS "IF NO RIGHT EXISTED AT THE TIME (T)HE ACTION WAS COMMENCED THE SUIT CANNOT BE MAINTAINED, ALTHOUGH SUCH RIGHT OF ACTION MAY HAVE ACCRUED THEREAFTER.

B.

JUDGE TIPON IGNORED CONTROLLING CASE LAW, AND THUS GRAVELY ABUSED HIS DISCRETION, WHEN HE GRANTED AND ISSUED THE QUESTIONED "WRIT OF EXECUTION" DIRECTING THE EXECUTION OF HIS PARTIAL SUMMARY JUDGMENT IN FAVOR OF THE SPOUSES TURNER, BECAUSE THAT JUDGMENT IS NOT A FINAL JUDGMENT UNDER SECTION 1 OF RULE 39 OF THE RULES OF COURT AND THEREFORE CANNOT BE SUBJECT OF EXECUTION

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[10] *Id.,* pp. 94-96.

[11] *Id.,* p. 97.

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UNDER THE SUPREME COURT'S CATEGORICAL HOLDING IN *PROVINCE OF PANGASINAN VS. COURT OF APPEALS.*

Upon the respondent's application, the CA issued a temporary restraining order (TRO), enjoining the petitioners, and their agents and representatives from enforcing the *writ of execution.* By then, however, the *writ of execution* had been partially enforced.

The TRO lapsed without the CA issuing a writ of preliminary injunction to prevent the execution. Thereupon, the sheriff resumed the enforcement of the *writ of execution.*

The CA promulgated its assailed decision on March 4, 2003,[12] pertinently holding:

> However, it is clear from the foregoing that the Turners' appraisal right is subject to the legal condition that no payment shall be made to any dissenting stockholder unless the corporation has unrestricted retained earnings in its books to cover such payment. Thus, the Supreme Court held that:
>
> > The requirement of unrestricted retained earnings to cover the shares is based on the trust fund doctrine which means that the capital stock, property and other assets of a corporation are regarded as equity in trust for the payment of corporate creditors. The reason is that creditors of a corporation are preferred over the stockholders in the distribution of corporate assets. There can be no distribution of assets among the stockholders without first paying corporate creditors. Hence, any disposition of corporate funds to the prejudice of creditors is null and void. Creditors of a corporation have the right to assume that so long as there are outstanding debts and liabilities, the board of directors will not use the assets of the corporation to purchase its own stock.
>
> In the instant case, it was established that there were no unrestricted retained earnings when the Turners filed their Complaint. In a letter dated 20 August 2000, petitioner informed the Turners that payment of their shares could only be made if it had unrestricted earnings in

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[12] *Id.,* pp. 20-35.

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its books to cover the same. Petitioner reiterated this in a letter dated 2 January 2001 which further informed the Turners that its Financial Statement for fiscal year 1999 shows that its retained earnings ending December 31, 1999 was at a deficit in the amount of ₱72,973,114.00, a matter which has not been disputed by private respondents. Hence, in accordance with the second paragraph of sec. 82, BP 68 supra, the Turners' right to payment had not yet accrued when they filed their Complaint on January 22, 2001, albeit their appraisal right already existed.

In *Philippine American General Insurance Co. Inc. vs. Sweet Lines, Inc.*, the Supreme Court declared that:

> Now, before an action can properly be commenced all the essential elements of the cause of action must be in existence, that is, the cause of action must be complete. All valid conditions precedent to the institution of the particular action, whether prescribed by statute, fixed by agreement of the parties or implied by law must be performed or complied with before commencing the action, unless the conduct of the adverse party has been such as to prevent or waive performance or excuse non-performance of the condition.
>
> It bears restating that a right of action is the right to presently enforce a cause of action, while a cause of action consists of the operative facts which give rise to such right of action. The right of action does not arise until the performance of all conditions precedent to the action and may be taken away by the running of the statute of limitations, through estoppel, or by other circumstances which do not affect the cause of action. Performance or fulfillment of all conditions precedent upon which a right of action depends must be sufficiently alleged, considering that the burden of proof to show that a party has a right of action is upon the person initiating the suit.

The Turners' right of action arose only when petitioner had already retained earnings in the amount of ₱11,975,490.00 on March 21, 2002; such right of action was inexistent on January 22, 2001 when they filed the Complaint.

In the doctrinal case of *Surigao Mine Exploration Co. Inc., vs. Harris*, the Supreme Court ruled:

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> Subject to certain qualifications, and except as otherwise provided by law, an action commenced before the cause of action has accrued is prematurely brought and should be dismissed. The fact that the cause of action accrues after the action is commenced and while it is pending is of no moment. It is a rule of law to which there is, perhaps, no exception, either at law or in equity, that to recover at all there must be some cause of action at the commencement of the suit. There are reasons of public policy why there should be no needless haste in bringing up litigation, and why people who are in no default and against whom there is as yet no cause of action should not be summoned before the public tribunals to answer complaints which are groundless. An action prematurely brought is a groundless suit. Unless the plaintiff has a valid and subsisting cause of action at the time his action is commenced, the defect cannot be cured or remedied by the acquisition or accrual of one while the action is pending, and a supplemental complaint or an amendment setting up such after-accrued cause of action is not permissible.

The afore-quoted ruling was reiterated in *Young vs. Court of Appeals* and *Lao vs. Court of Appeals*.

The Turners' apprehension that their claim for payment may prescribe if they wait for the petitioner to have unrestricted retained earnings is misplaced. It is the legal possibility of bringing the action that determines the starting point for the computation of the period of prescription. Stated otherwise, the prescriptive period is to be reckoned from the accrual of their right of action.

Accordingly, We hold that public respondent exceeded its jurisdiction when it entertained the herein Complaint and issued the assailed Orders. Excess of jurisdiction is the state of being beyond or outside the limits of jurisdiction, and as distinguished from the entire absence of jurisdiction, means that the act although within the general power of the judge, is not authorized and therefore void, with respect to the particular case, because the conditions which authorize the exercise of his general power in that particular case are wanting, and hence, the judicial power is not in fact lawfully invoked.

We find no necessity to discuss the second ground raised in this petition.

WHEREFORE, upon the premises, the petition is GRANTED. The assailed Orders and the corresponding Writs of Garnishment are

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NULLIFIED. Civil Case No. 02-104692 is hereby ordered DISMISSED without prejudice to refiling by the private respondents of the action for enforcement of their right to payment as withdrawing stockholders.

SO ORDERED.

The petitioners now come to the Court for a review on *certiorari* of the CA's decision, submitting that:

I.

THE COURT OF APPEALS COMMITTED SERIOUS ERRORS OF LAW WHEN IT GRANTED THE PETITION FOR *CERTIORARI* WHEN THE REGIONAL TRIAL COURT OF MANILA DID NOT ACT BEYOND ITS JURISDICTION AMOUNTING TO LACK OF JURISDICTION IN GRANTING THE MOTION FOR PARTIAL SUMMARY JUDGMENT AND IN GRANTING THE MOTION FOR IMMEDIATE EXECUTION OF JUDGMENT;

II.

THE COURT OF APPEALS COMMITTED SERIOUS ERRORS OF LAW WHEN IT ORDERED THE DISMISSAL OF THE CASE, WHEN THE PETITION FOR *CERTIORARI* MERELY SOUGHT THE ANNULMENT OF THE ORDER GRANTING THE MOTION FOR PARTIAL SUMMARY JUDGMENT AND OF THE ORDER GRANTING THE MOTION FOR IMMEDIATE EXECUTION OF THE JUDGMENT;

III.

THE HONORABLE COURT OF APPEALS HAS DECIDED QUESTIONS OF SUBSTANCE NOT THEREFORE DETERMINED BY THIS HONORABLE COURT AND/OR DECIDED IT IN A WAY NOT IN ACCORD WITH LAW OR WITH JURISPRUDENCE.

Ruling

The petition fails.

The CA correctly concluded that the RTC had exceeded its jurisdiction in entertaining the petitioners' complaint in Civil Case No. 01-086, and in rendering the summary judgment and issuing writ of execution.

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A.
Stockholder's Right of Appraisal, In General

A stockholder who dissents from certain corporate actions has the right to demand payment of the fair value of his or her shares. This right, known as the right of appraisal, is expressly recognized in Section 81 of the *Corporation Code*, to wit:

> Section 81. *Instances of appraisal right.* — Any stockholder of a corporation shall have the right to dissent and demand payment of the fair value of his shares in the following instances:
>
> 1. In case any amendment to the articles of incorporation has the effect of changing or restricting the rights of any stockholder or class of shares, or of authorizing preferences in any respect superior to those of outstanding shares of any class, or of extending or shortening the term of corporate existence;
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> 2. In case of sale, lease, exchange, transfer, mortgage, pledge or other disposition of all or substantially all of the corporate property and assets as provided in the Code; and
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> 3. In case of merger or consolidation. (n)

Clearly, the right of appraisal may be exercised when there is a fundamental change in the charter or articles of incorporation substantially prejudicing the rights of the stockholders. It does not vest unless objectionable corporate action is taken.[13] It serves the purpose of enabling the dissenting stockholder to have his interests purchased and to retire from the corporation.[14]

Under the common law, there were originally conflicting views on whether a corporation had the power to acquire or purchase its own stocks. In England, it was held invalid for a corporation to purchase its issued stocks because such purchase was an indirect method of reducing capital (which was statutorily restricted), aside from being inconsistent with the privilege of

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[13] 18 CJS, *Corporations*, §314, pp. 641-642.

[14] *Ibid.*

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limited liability to creditors.[15] Only a few American jurisdictions adopted by decision or statute the strict English rule forbidding a corporation from purchasing its own shares. In some American states where the English rule used to be adopted, statutes granting authority to purchase out of surplus funds were enacted, while in others, shares might be purchased even out of capital provided the rights of creditors were not prejudiced.[16] The reason underlying the limitation of share purchases sprang from the necessity of imposing safeguards against the depletion by a corporation of its assets and against the impairment of its capital needed for the protection of creditors.[17]

Now, however, a corporation can purchase its own shares, provided payment is made out of surplus profits and the acquisition is for a legitimate corporate purpose.[18] In the Philippines, this new rule is embodied in Section 41 of the *Corporation Code*, to wit:

> Section 41. *Power to acquire own shares.* — A stock corporation shall have the power to purchase or acquire its own shares for a legitimate corporate purpose or purposes, including but not limited to the following cases: Provided, That the corporation has unrestricted retained earnings in its books to cover the shares to be purchased or acquired:
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> 1. To eliminate fractional shares arising out of stock dividends;
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> 2. To collect or compromise an indebtedness to the corporation, arising out of unpaid subscription, in a delinquency sale, and to purchase delinquent shares sold during said sale; and
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> 3. To pay dissenting or withdrawing stockholders entitled to payment for their shares under the provisions of this Code. (n)

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[15] Ballantine, *Law of Corporations*, Revised Edition, Callaghan and Co., Chicago, 1946, p. 603.

[16] *Id.*, p. 604.

[17] *Id.*, p. 605.

[18] II Campos Jr., *The Corporation Code, Comments, Notes and Selected Cases (*1990).

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The *Corporation Code* defines how the right of appraisal is exercised, as well as the implications of the right of appraisal, as follows:

1. The appraisal right is exercised by any stockholder who has voted against the proposed corporate action by making a written demand on the corporation within 30 days after the date on which the vote was taken for the payment of the fair value of his shares. The failure to make the demand within the period is deemed a waiver of the appraisal right.[19]

2. If the withdrawing stockholder and the corporation cannot agree on the fair value of the shares within a period of 60 days from the date the stockholders approved the corporate action, the fair value shall be determined and appraised by three disinterested persons, one of whom shall be named by the stockholder, another by the corporation, and the third by the two thus chosen. The findings and award of the majority of the appraisers shall be final, and the corporation shall pay their award within 30 days after the award is made. Upon payment by the corporation of the agreed or awarded price, the stockholder shall forthwith transfer his or her shares to the corporation.[20]

3. All rights accruing to the withdrawing stockholder's shares, including voting and dividend rights, shall be suspended from the time of demand for the payment of the fair value of the shares until either the abandonment of the corporate action involved or the purchase of the shares by the corporation, except the right of such stockholder to receive payment of the fair value of the shares.[21]

4. Within 10 days after demanding payment for his or her shares, a dissenting stockholder shall submit to the corporation the certificates of stock representing his shares for notation thereon that such shares are dissenting shares. A failure to do so shall, at the option of the corporation, terminate his rights under this Title X of the *Corporation Code*. If shares represented by the

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[19] Section 82, *Corporation Code*.

[20] *Ibid.*

[21] *Id.,* Section 83.

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certificates bearing such notation are transferred, and the certificates are consequently canceled, the rights of the transferor as a dissenting stockholder under this Title shall cease and the transferee shall have all the rights of a regular stockholder; and all dividend distributions that would have accrued on such shares shall be paid to the transferee.[22]

5. If the proposed corporate action is implemented or effected, the corporation shall pay to such stockholder, upon the surrender of the certificates of stock representing his shares, the fair value thereof as of the day prior to the date on which the vote was taken, excluding any appreciation or depreciation in anticipation of such corporate action.[23]

Notwithstanding the foregoing, no payment shall be made to any dissenting stockholder unless the corporation has unrestricted retained earnings in its books to cover the payment. In case the corporation has no available unrestricted retained earnings in its books, Section 83 of the *Corporation Code* provides that if the dissenting stockholder is not paid the value of his shares within 30 days after the award, his voting and dividend rights shall immediately be restored.

The *trust fund doctrine* backstops the requirement of unrestricted retained earnings to fund the payment of the shares of stocks of the withdrawing stockholders. Under the doctrine, the capital stock, property, and other assets of a corporation are regarded as equity in trust for the payment of corporate creditors, who are preferred in the distribution of corporate assets.[24] The creditors of a corporation have the right to assume

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[22] *Id.*, Section 86.

[23] *Id.*, Section 82.

[24] *Boman Environment Development Corporation v. Court of Appeals*, G.R. No. 77860, November 22, 1988, 167 SCRA 540, 541; citing *Steinberg v. Velasco*, 52 Phil. 953 (1929).

According to 42A, Words and Phrases, *Trust Fund Doctrine*, p. 445, the "trust fund doctrine" is a "rule that the property of a corporation is a trust fund for the payment of creditors, but such property can be called a trust fund 'only by way of analogy or metaphor.' As between the corporation

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that the board of directors will not use the assets of the corporation to purchase its own stock for as long as the corporation has outstanding debts and liabilities.[25] There can be no distribution of assets among the stockholders without first paying corporate debts. Thus, any disposition of corporate funds and assets to the prejudice of creditors is null and void.[26]

B.

Petitioners' cause of action was premature

That the respondent had indisputably no unrestricted retained earnings in its books at the time the petitioners commenced Civil Case No. 01-086 on January 22, 2001 proved that the respondent's legal obligation to pay the value of the petitioners' shares did not yet arise. Thus, the CA did not err in holding that the petitioners had no cause of action, and in ruling that the RTC did not validly render the partial summary judgment.

A cause of action is the act or omission by which a party violates a right of another.[27] The essential elements of a cause of action are: (*a*) the existence of a legal right in favor of the plaintiff; (*b*) a correlative legal duty of the defendant to respect such right; and (*c*) an act or omission by such defendant in violation of the right of the plaintiff with a resulting injury or damage to the plaintiff for which the latter may maintain an action for the recovery of relief from the defendant.[28] Although

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itself and its creditors it is a simple debtor, and as between its creditors and stockholders its assets are in equity a fund for the payment of its debts" (citing *McIver v. Young Hardware Co.*, 57 S.E. 169, 171, 144 N.C. 478, 119 Am. St. Rep. 970; *Gallagher v. Asphalt Co. of America*, 55 A. 259, 262, 65 N.J. Eq. 258).

[25] *Boman Environment Development Corporation v. Court of Appeals*, *supra.*

[26] *Id.*

[27] Section 2, Rule 2, *Rules of Court*.

[28] *Rebollido v. Court of Appeals*, G.R. No. 81123, February 28, 1989, 170 SCRA 800; *Heirs of Ildefonso Coscolluela v. Rico General Insurance Corporation*, G.R. No. 84628, November 16, 1989, 179 SCRA 511; *Nabus*

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the first two elements may exist, a cause of action arises only upon the occurrence of the last element, giving the plaintiff the right to maintain an action in court for recovery of damages or other appropriate relief.[29]

Section 1, Rule 2, of the *Rules of Court* requires that every ordinary civil action must be based on a cause of action. Accordingly, Civil Case No. 01-086 was dismissible from the beginning for being without any cause of action.

The RTC concluded that the respondent's obligation to pay had accrued by its having the unrestricted retained earnings after the making of the demand by the petitioners. It based its conclusion on the fact that the *Corporation Code* did not provide that the unrestricted retained earnings must already exist at the time of the demand.

The RTC's construal of the *Corporation Code* was unsustainable, because it did not take into account the petitioners' lack of a cause of action against the respondent. In order to give rise to any obligation to pay on the part of the respondent, the petitioners should first make a valid demand that the respondent refused to pay despite having unrestricted retained earnings. Otherwise, the respondent could not be said to be guilty of any actionable omission that could sustain their action to collect.

Neither did the subsequent existence of unrestricted retained earnings after the filing of the complaint cure the lack of cause of action in Civil Case No. 01-086. The petitioners' right of action could only spring from an *existing* cause of action. Thus, a complaint whose cause of action has not yet accrued cannot be cured by an amended or supplemental pleading alleging the

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v. Court of Appeals, G.R. No. 91670, February 7, 1990, 193 SCRA 732;*Mathay v. Consolidated Bank*, G.R. No. L-23136, August 26, 1974, 58 SCRA 559; *Leberman Realty Corporation v. Typingco*, G.R. No. 126647, July 29, 1998, 293 SCRA 316.

[29] *Swagman Hotels and Travel, Inc. v. Court of Appeals*, G.R. No. 161135, April 8, 2005, 455 SCRA 175.

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existence or accrual of a cause of action during the pendency of the action.[30] For, only when there is an invasion of primary rights, not before, does the adjective or remedial law become operative.[31] Verily, a premature invocation of the court's intervention renders the complaint without a cause of action and dismissible on such ground.[32] In short, Civil Case No. 01-086, being a groundless suit, should be dismissed.

Even the fact that the respondent already had unrestricted retained earnings more than sufficient to cover the petitioners' claims on June 26, 2002 (when they filed their *motion for partial summary judgment*) did not rectify the absence of the cause of action at the time of the commencement of Civil Case No. 01-086. The *motion for partial summary judgment*, being a mere application for relief other than by a pleading,[33] was not the same as the complaint in Civil Case No. 01-086. Thereby, the petitioners did not meet the requirement of the *Rules of Court* that a cause of action must exist at the commencement of an action, which is "commenced by the filing of the original complaint in court."[34]

The petitioners claim that the respondent's petition for *certiorari* sought only the annulment of the assailed orders of the RTC (*i.e.*, granting the *motion for partial summary judgment* and the *motion for immediate execution*); hence, the CA had no right to direct the dismissal of Civil Case No. 01-086.

The claim of the petitioners cannot stand.

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[30] *Lao v. Court of Appeals*, G.R. No. L-47013, February 17, 2000, 325 SCRA 694.

[31] *Id.*

[32] *Estrada v. Court of Appeals,* G.R. No. 137862, November 11, 2004, 442 SCRA 117.

[33] Section 1, Rule 15, *Rules of Court.*

[34] Section 5, Rule 1, *Rules of Court*; *A.G. Development Corporation v. Court of Appeals*, G.R. No. 111662, October 23, 1997, 281 SCRA 155.

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Although the respondent's petition for *certiorari* targeted only the RTC's orders granting the *motion for partial summary judgment* and the *motion for immediate execution*, the CA's directive for the dismissal of Civil Case No. 01-086 was not an abuse of discretion, least of all grave, because such dismissal was the only proper thing to be done under the circumstances. According to *Surigao Mine Exploration Co., Inc. v. Harris*:[35]

> Subject to certain qualification, and except as otherwise provided by law, **an action commenced before the cause of action has accrued is prematurely brought and should be dismissed**. The fact that the cause of action accrues after the action is commenced and while the case is pending is of no moment. It is a rule of law to which there is, perhaps no exception, either in law or in equity, that to recover at all there must be some cause of action at the commencement of the suit. There are reasons of public policy why there should be no needless haste in bringing up litigation, and why people who are in no default and against whom there is as yet no cause of action should not be summoned before the public tribunals to answer complaints which are groundless. An action prematurely brought is a groundless suit. **Unless the plaintiff has a valid and subsisting cause of action at the time his action is commenced, the defect cannot be cured or remedied by the acquisition or accrual of one while the action is pending**, and a supplemental complaint or an amendment setting up such after-accrued cause of action is not permissible.

Lastly, the petitioners argue that the respondent's recourse of a special action for *certiorari* was the wrong remedy, in view of the fact that the granting of the *motion for partial summary judgment* constituted only an error of law correctible by appeal, not of jurisdiction.

The argument of the petitioners is baseless. The RTC was guilty of an error of jurisdiction, for it exceeded its jurisdiction by taking cognizance of the complaint that was not based on an existing cause of action.

WHEREFORE, the petition for review on *certiorari* is denied for lack of merit.

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[35] 68 Phil 113 (1939).

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We affirm the decision promulgated on March 4, 2003 in C.A.-G.R. SP No. 74156 entitled *Lorenzo Shipping Corporation v. Hon. Artemio S. Tipon, in his capacity as Presiding Judge of Branch 46 of the Regional Trial Court of Manila, et al.*

Costs of suit to be paid by the petitioners.

SO ORDERED.

Carpio Morales (Chairperson), Brion, Villarama, Jr., and *Sereno, JJ.,* concur.

THIRD DIVISION

[G.R. No. 160933. November 24, 2010]

NICEAS M. BELONGILOT, *petitioner, vs.* **ROLANDO S. CUA, ROEL ERIC C. GARCIA, LORENZO R. REYES, AUGUSTO P. QUIJANO, IANELA G. JUSI-BARRANTES and SALVADOR P. RAMOS,** *respondents.*

SYLLABUS

1. REMEDIAL LAW; SPECIAL CIVIL ACTIONS; *CERTIORARI*; RULE 65 PETITION, PROPER REMEDY; SUBSTANCE OF THE PETITION, GIVEN PRIMACY OVER FORM AND PROCEDURE.— The petitioner's complaint before the Ombudsman, charging the respondents with violation of Section 3(e) of R.A. No. 3019, as amended, is undoubtedly criminal in nature. The petitioner's recourse to this Court should have, therefore, been through a petition for *certiorari* under Rule 65, instead of a petition for review on *certiorari* under Rule 45. Thus, from a procedural perspective, the OSG's claim that the petitioner availed of the wrong remedy appears to be correct. We would have readily agreed with the OSG's conclusion had