

The Practical Implications of *Ponce v. Alsons* in Philippine Commercial Relations: A Closer Look at Section 63 of the Corporation Code

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INTRODUCTION	268
I. BACKGROUND: PRINCIPLES OF SECTION 63	270
II. AN OVERVIEW OF <i>Ponce v. Alsons</i>	273
A. <i>Facts of the Case</i>	
B. <i>Ratio: The Supreme Court Upholds Stare Decisis</i>	
C. <i>The Gaping Hole</i>	
III. ANALYSIS: FOLLOWING THE TRAIL	277
A. <i>Jurisprudential History on Certificates of Stocks</i>	
B. <i>What the Hole Means: Implications</i>	
IV. RESOLUTION	284
CONCLUSION	284

The great object of the law is to encourage commerce.¹

- Judge Chambre

INTRODUCTION

Corporations, the vehicles of choice of modern-day capitalism, need capital to survive. Equity investments and debt contracts are the two basic sources by which a corporation is able to finance its operations, aside from operational or transactional income.² Debt involves borrowing money to be paid with interest, if applicable, while equity involves raising money by selling interests of the company. Equity investment in a corporation is essentially stock ownership. A stock is an aliquot ownership of a corporation

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The author wishes to thank Atty. Cesar L. Villanueva, Professor of Corporate Law and Associate Dean of the Ateneo Law School, whose valuable insights contributed greatly to this work, and Ms. Rosalyn C. Rayco for her research and editing assistance.

Cite as 48 ATENEO L.J. 268 (2003).

1. Beale v. Thompson, 4 East 546 (1803).
2. CESAR L. VILLANUEVA, PHILIPPINE CORPORATE LAW 532 (1998).

represented by shares that are a claim on the corporation's earnings and assets. When a company earns profits, its shareholders can benefit if the share price rises and if the corporation pays a dividend per share. When the company suffers a loss, its shareholders likewise absorb the same by a decrease in the value of the stocks owned.

From the point of view of the corporation, the obvious advantage of equity over debt is the absence of carrying cost since the corporate enterprise is not bound to pay any return on the investment unless there are profits, and even then, the board of directors is generally granted business discretion to determine when to declare such return in the form of dividends.³ For the investors on the other hand, stock ownership creates a right, however inchoate,⁴ on the earnings and assets of the corporation. That is why they invest only in those corporations they perceive to be a profitable or a potentially profitable enterprise. The registration of shares in a stockholder's name, the issuance of stock certificates, and the right to receive dividends which pertain to the said shares are all rights that flow from such ownership.⁵ This ownership is in turn evidenced by certificates of stock.

Shares of stock and certificates of stock are two distinct concepts. While the former is an intangible form of ownership, the latter is concrete evidence of that ownership. On one hand, although shares of stock represent aliquot parts of the corporation's capital, or the right to share in the proceeds when the remaining assets of the corporation are distributed according to law and equity, its holders do not own any part of the assets represented by the capital of the corporation; nor are the stockholders entitled to the possession of any definite portion of the corporation's assets or properties.⁶ The corporation owns the capital and its assets as a separate juridical person. In *Magsaysay-Labrador v. Court of Appeals*,⁷ the Supreme Court characterized a stockholder's interest in corporate contracts, transactions and properties "[I]f it exists at all...[a]s indirect, contingent, remote, conjectural, consequential and collateral." At the very least, their interest is purely inchoate or in sheer expectancy of a right in the management of the corporation and to share in its profits and in the properties and assets upon dissolution thereof, after payment of the corporate debts and obligations.⁸

On the other hand, a certificate of stock is a written acknowledgment by the corporation of the interest of a shareholder in the corporate property and

3. *Id.* at 533.
4. *Stockholders of F. Guanzon and Sons Inc. v. Register of Deeds of Manila*, 6 SCRA 373 (1962).
5. *Lim Tay v. Court of Appeals*, 293 SCRA 634 (1998).
6. *Boyer Roxas v. Court of Appeals*, 211 SCRA 470 (1992).
7. 180 SCRA 266 (1989).
8. *Id.* at 271.

franchises.⁹ It does not necessarily make one a stockholder in a corporation. Nevertheless, a certificate of stock is tangible evidence of the stock itself and of the various interests therein. It expresses the contract between the corporation and the stockholder, but it is not essential to the existence of a share in stock or the creation of the relation of shareholder to the corporation.¹⁰ In other words, a person may not possess any certificate of stock and still be considered a shareholder of the corporation and vice versa. Under Philippine law, the operative act to make one a shareholder in the eyes of the corporation is the recording or registration of the issuance or transfer of shares in the Stock and Transfer Book of the corporation.

The central question presented in *Ponce v. Alsons*¹¹ was whether or not it was ministerial on the part of the corporation to issue a certificate of stock to a transferee without express instructions, written or otherwise, from the transferor. In answering this question in the negative, the Supreme Court held that a written authority is required in order to give rise to a legal obligation on the part of the corporation to issue a certificate of stock. This Essay, however, asserts that the Court should have broadened the discussion by closely scrutinizing the corollary effects of such a doctrine. By its failure to address this aspect and move out from the legal vacuum, the Court failed to call attention to the changes that Section 63 of the Corporation Code¹² must necessarily undergo in the legislative mill so that the fundamental purpose of encouraging commerce may be served.

I. BACKGROUND: PRINCIPLES OF SECTION 63

Section 63 of the Corporation Code¹³ defines the nature of shares of stock and provides for the manner by which they are transferred from one owner

9. 11 FLETCHER, CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATION, § 5091.

10. *Tan v. Securities and Exchange Commission*, 206 SCRA 741 (1997) (citing 13 AM.JUR. 2d 769).

11. G.R. No. 139802, Dec. 10, 2002.

12. The Corporation Code of the Philippines, Batas Pambansa Blg. 68 [CORPORATION CODE].

Section 63. The capital stock of stock corporations shall be divided into shares for which certificates signed by the president or vice president, countersigned by the secretary or assistant secretary, and sealed with the seal of the corporation shall be issued in accordance with the by-laws. Shares of stock so issued are personal property and may be transferred by delivery of the certificate or certificates endorsed by the owner or his attorney-in-fact or other person legally authorized to make the transfer. No transfer, however, shall be valid, except as between the parties, until the transfer is recorded in the books of the corporation.

to another. It also prescribes the manner by which transfer of shares of stock may be made effective as against the corporation and third persons.¹⁴ Under this provision, shares of stock are considered to be personal in nature, hence, freely transferable upon proper negotiation thereof. This is a necessary feature by virtue of the free transferability attribute of the corporate vehicle. However, since the transfer of the certificate from the transferor to the transferee is almost always an element or an incident of transfers of stock, the possession of a transferable certificate and the right to have the corporation issue such a certificate are necessarily, albeit only incidentally, involved in the great majority of questions with respect to transfers.¹⁵ Corollarily, the nature of certificates of stock as held in *De los Santos v. Republic*¹⁶ is also drawn from Section 63. *De los Santos* held that a certificate of stock is regarded as a quasi-negotiable instrument in the sense that it may be transferred by endorsement, coupled with delivery, but it is not negotiable in the sense that the holder takes it without prejudice to such rights or defenses as the registered owners or transferor's creditor may have under the law, except insofar as such rights or defenses are subject to the limitations imposed by the principles governing estoppel. In other words, it is quasi-negotiable because of the mechanism used in the transfer of the document but it is still free from the defenses that would otherwise be available to a holder in due course in the case of a negotiable instrument. The distinction is important because the holder in due course of a negotiable instrument is guaranteed that the instrument would be honored on its face, whereas there is no similar protection afforded to the holder in good faith and for value of a quasi-negotiable document, such as a certificate of stock, who receives them in the course of their being negotiated, and that the ownership of the true owner would be preferred. The only exception to such rule is when the circumstances show that the true owner was guilty of negligence in causing the loss.¹⁷

Section 63 also embodies the centrality of the Stock and Transfer Book requirement in all commercial dealings involving shares of stock, and necessarily – as these are the tangible means with which transactions over shares of stock are conducted – certificates of stock as well. The key part of this provision states that no transfer shall be valid except as between the parties until the transfer is recorded in the books of the corporation. The effects of this provision are far-reaching. The Supreme Court has arrived at the peculiar interpretation that attachments or levies prevail over unrecorded,

No shares of stock against which the corporation holds any unpaid claim shall be transferable in the books of the corporation. (35)

14. 2 JOSE CAMPOS, COMMERCIAL LAWS OF THE PHILIPPINES 300 (1990).

15. 11 FLETCHER, CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATION 324, § 5164 (perm. ed.).

16. 96 Phil. 577 (1955).

17. VILLANUEVA, *supra* note 2, at 406.

albeit absolute, dispositions since mere encumbrances do not fall under the word 'transfer.'¹⁸ In one case, the Court upheld the validity of a later attachment over an earlier sale because the sale was not annotated in the books of the corporation.¹⁹ As one writer has observed,²⁰ the interpretation does not seem at all practical.

If a contract more onerous than encumbrance such as the assignment of shares could validly be annotated in the stock and transfer book to affect the whole world, why not provide the same requirement for a contract less invasive as a mortgage. The law should be interpreted, if not amended, to read that both encumbrances and transfer of shares should be valid only as against the parties and void as against third persons unless annotated in the stock and transfer book.²¹

The importance of the stock and transfer book was reiterated in several cases. In *Uson v. Disomito*,²² a landmark case decided in 1935, the question presented to the Court was whether a *bona fide* transfer of the shares of a corporation, not registered or noted in the books of the corporation, is valid as against a subsequent lawful attachment of said shares, regardless of whether the attaching creditor had actual notice of said transfer or not. The Court held that the attachment lien prevails over a prior unregistered *bona fide* stock transfer, following the impetus of Section 35 which stated that no transfer however shall be valid, except as between the parties, until the transfer is entered and noted upon the books of the corporation so as to show the names of the parties to the transaction, the date of the transfer, the number of the certificate and the number of shares transferred.

The Court's pronouncement in *Uson* provided the rationale for the registration requirement as a condition precedent for its validity against the corporation as held in the subsequent case of *Escano v. Filipinas Mining*.²³ First, to enable the corporation to know at all times who its actual stockholders are, because mutual rights and obligations exist between the corporation and its stockholders. Second, to afford the corporation an

18. See *Monserrat v. Ceron*, 58 Phil 469 (1933) (noting that when it comes to mortgages and other encumbrances covering shares of stock 'which are not a complete and absolute alienation of the dominion and ownership thereof, its entry and notation upon the books of the corporation is not a necessary requisite to its validity.)

19. *Chemphil Export & Import Corp v. Court of Appeals*, 251 SCRA 257 (1995).

20. See VILLANUEVA, *supra* note 2, at 436. The difficulties of the current interpretation of Section 63 with regard to different dealings with shares of stock are discussed at great length by Professor Villanueva in his book.

21. *Id.*

22. 61 Phil. 535 (1935).

23. *Escano v. Filipinas Mining*, 74 Phil. 711 (1944).

opportunity to object or refuse its consent to the transfer in case it has any claim against the stock sought to be transferred or for any other valid reason. Last, to avoid fictitious or fraudulent transfers. One commentator likewise gives the two-fold purpose of registration: (a) to enable the transferee to exercise all the rights of a stockholder, and (b) to inform the corporation of any change in share ownership so that it can ascertain the persons entitled to the rights and subject to the liabilities of a stockholder. More importantly, it protects the corporation when it pays dividends to the registered owner despite a previous transfer of which it had no knowledge.²⁴

However, even in the light of these purposes, the difficulty of this doctrine is still apparent. Sound reason dictates that the present interpretation actually destroys the centrality of the stock and transfer book requirement by making it less reliable for third party purchasers and by making the effectivity of various transactions a matter of race toward different finish lines.²⁵

II. OVERVIEW OF *Ponce v. Alsons*

A. Facts of the Case

The case stemmed from an action for *mandamus* filed by Vicente C. Ponce with the Securities and Exchange Commission (SEC) against Alsons Cement Corporation and its corporate secretary Francisco M. Giron Jr. for refusing to issue the corresponding certificates of stock covering 239,500 shares, as indicated by a Deed of Undertaking and Indorsement.

The stocks in question were originally issued to the late Fausto G. Gaid as incorporator and subscriber to 239,500 shares of Victory Cement Corporation (VCC), Alsons' predecessor-in-interest. On February 3, 1968, Fausto Gaid executed a Deed of Undertaking and Indorsement acknowledging his ownership over the said shares and at the same time, assigning or endorsing the same to Vicente C. Ponce. Since the incorporation of VCC, no certificates of stock corresponding to the 239,500 subscribed and fully paid shares of Gaid were issued in the name of either Gaid or Ponce.

After Ponce's repeated demands from Alsons to secure the corresponding certificates of stock were met by the latter's persistent refusal, Ponce filed an

24. CAMPOS, *supra* note 14, at 301.

25. Different rules are provided for different dealings with shares of stock in order to ascertain which becomes effective. The rules are but a matter of race, whoever registers first, wins. For instance, in case of an earlier sale and a later chattel mortgage, the sale is considered binding against the corporation only if recorded in the stock and transfer book while a mortgage becomes effective upon delivery and indorsement of said shares to the pledgee or mortgagee, even if nothing was indicated in the stock and transfer book.

action for *mandamus* with the SEC to compel the issuance of such certificates of stock in his name and prayed for damages. Alsons then moved to dismiss the complaint stating that, among others, there was no cause of action and assuming that there was, *mandamus* was an improper remedy.

The hearing officer of the SEC granted Alsons' motion to dismiss on the following grounds: (a) the SEC was without jurisdiction to entertain the dispute since there is no showing that Ponce was a registered stockholder of the corporation; (b) the complaint did not state a cause of action since Ponce was not the real party-in-interest and he could not step into the shoes of Gaid upon a mere showing of a document which purportedly shows that Gaid transferred the ownership of the said shares to him absent any written instruction or authority from the transferor. In other words, there was no record of such transfer in the books of the corporation which is a prerequisite to the issuance of a stock certificate in favor of the transferee.

This decision was later reversed by the SEC *en banc*, citing the Supreme Court ruling in *Abejo v. De la Cruz*²⁶ which states that the transfer or assignment of stocks need not be registered before the SEC can take cognizance of the case to rule on the petitioner's rights as a stockholder. More important, it likewise held that the corporation had a ministerial duty to register in its stock and transfer book the shares of stock in the name of Ponce subject to the determination of the validity of the Deed of Assignment in the proper tribunal. The Court of Appeals later on reversed the ruling of the SEC *en banc* and held that Ponce's action for *mandamus* failed to state a cause of action since there was no allegation whatsoever that the transfer of shares was registered in the stock and transfer book of the corporation as provided for in Section 63 of the Corporation Code.

In presenting his case to the Court, Ponce anchored his argument on the fact that there was no law, rule or regulation requiring a transferor of shares of stock to first issue express instructions or execute a power of attorney for the transfer of said shares before a certificate of stock is issued in the name of the transferee and the transfer registered in the books of the corporation. He likewise contended that the ruling in *Hager v. Bryan*,²⁷ did not apply since what was involved in that case was the recording of a transfer of shares in the stock and transfer book and not the issuance of a certificate of stock as was involved in the case herein.

B. Ratio: Supreme Court Upholds Stare Decisis

Ponce essentially involves the right of a transferee of shares of stock to demand a new certificate which is duly titled in his name. Relying on the

text of Section 63 of the Corporation Code and the precedents set by *Hager* and *Rural Bank of Salinas*,²⁸ the Court answered the issue of whether or not an action of *mandamus* is proper given the abovementioned circumstances in the negative. And while *Ponce* is apparently novel in the sense that it involves the issuance of a stock certificate as opposed to *Hager* and *Rural Bank* which involved the recording of the transfer in the stock and transfer book, the Court applied the same well-established rules.

First, on the basis of Section 63 and a long list of jurisprudence,²⁹ a transfer of shares of stock not recorded in the stock and transfer book of the corporation is non-existent insofar as the corporation is concerned. Consequently, as Ponce is not a valid stockholder in the eyes of the corporation, no legal obligation arises on the part of the corporation to issue a stock certificate in his name. From the corporation's point of view, the transfer is not effective until it is recorded. Unless and until such recording is made, the demand for the issuance of stock certificates to the alleged transferee has no legal basis. As between the corporation on the one hand, and its shareholders and third persons on the other, the corporation looks only to its books for the purpose of determining who its shareholders are.³⁰

Second, applying the *Hager* and *Rural Bank* rulings, the Court restated the need for express instructions, written or otherwise, from the registered stockholder to cause the disposition of stocks registered in his name. Thus, the mere presentation of the Deed of Undertaking with Indorsement by Ponce was held to be inadequate for the purpose of establishing a *prima facie* right to demand for the registration of the transfer and the issuance of certificates of stock.

Looking at the Court's ruling, there are two important points that merit discussion. The first is the nature of an action for *mandamus*. *Mandamus* is a legal remedy to compel the corporation to comply with a legal duty.³¹ As a rule, every stockholder has a right to have a proper certificate issued by the corporation as soon as there has been compliance with the conditions which entitle the shareholder to one, in the absence of some provision or agreement to the contrary or the existence of some legal obstacle to issuance

26. 149 SCRA 645 (1987).

27. 19 Phil. 138 (1911).

28. 210 SCRA 510 (1992).

29. *Hager v. Bryan*, 19 Phil. 138 (1911); *Fleischer v. Nolasco*, 47 Phil. 583 (1925); *Hodges v. Lezama*, 14 SCRA 1030 (1963); *Nava v. Peers*, 74 SCRA 65 (1976); *Escano v. Filipinas Mining*, 74 Phil. 711 (1944); *Lim Tay v. Court of Appeals*, 293 SCRA 634 (1998); *Rural Bank of Salinas v. Court of Appeals*, 210 SCRA 510 (1992); *De los Santos v. Republic*, 96 Phil. 577 (1955).

30. *Hager*, 19 Phil. at 140-41.

31. 11 FLETCHER, CYCLOPEDIA ON THE LAW OF PRIVATE CORPORATIONS, § 5165 (perm. ed.).

erected by the stockholder.³² Therefore, if a corporation wrongfully refuses to issue a proper certificate of stock when it has the power and is under an obligation to issue the same, it may be compelled to do so by *mandamus* because its duty is considered to be ministerial. In transferring stock, the secretary of a corporation acts in a purely ministerial capacity, and does not have the duty to decide the question of ownership.³³ However, in the case of *Lim Tay v. Court of Appeals*,³⁴ the Court held that *mandamus* would not issue to establish a legal right, but only to enforce one that is already clearly established.³⁵ A *prima facie* showing of shareholder standing must therefore be established before a writ of *mandamus* may be issued.

Second is the accompanying evidentiary requirement to establish a *prima facie* right to demand for the registration of the transfer and the issuance of the certificate of stock and that would give rise to a ground for an action for *mandamus*. In *Ponce*, the Court held that the Deed of Undertaking with Indorsement is insufficient to establish a *prima facie* right. It must be coupled with a written authority from the transferor. In *Teng v. Court of Appeals*³⁶ however, the Court simply relied on the deed of transfer of shares executed by the transferor to the transferee and on the respondent's failure to repudiate such Deed in ruling in favor of the transferee. No other evidence was adduced in order to explain the ready reliance on the Deed whereas the decision in *Ponce* seemingly emphasized the prior need to establish the *prima facie* validity of the Deed of Undertaking with Indorsement, the absence of which eventually resulted in the dismissal of *Ponce's* complaint. One possible solution to the apparent inconsistency may be that in the case of *Teng*, the Court considered the fact that the transfer made was with the corporation's knowledge, whereas in *Ponce*, there was no such knowledge on the part of the corporation.

C. The Gaping Hole

The rule, as it now stands, is that a Deed of Assignment or Indorsement pertaining to shares of stocks is only valid and effective as between the parties and cannot give rise to a legal duty on the part of the corporation to issue a certificate of stock in favor of the transferee unless such transfer was also recorded in the stock and transfer book of the corporation. What is still missing from the Supreme Court rulings however, and which *Ponce* illustrates, is a discussion on the effects of both the present wording and

32. *Id.*

33. 12 FLETCHER, CYCLOPEDIA ON THE LAW OF PRIVATE CORPORATIONS 434, § 5524 (perm. ed.).

34. 239 SCRA 634 (1998).

35. *Id.*

36. TCL Sales Corporation and Anna Teng v. CA, 349 SCRA 35 (2001).

construction of Section 63. Notwithstanding *stare decisis*, this Essay contends that the Court must issue a pronouncement if it thinks that the wording of the law constrains Courts to rule in a particular way; the Court should also give reasons why it is interpreting the provision in a certain way. More than the legal considerations involved, the bottom line of all these rules must be that of the creation of an environment where commerce can develop and eventually thrive.

In *Ponce*, although the Court upheld *stare decisis*, it failed to see, much less state, the underlying effects of requiring a transferee to resort to an ordinary court action to enforce his rights under a Deed of Undertaking with Indorsement or the reason behind why a transferee must possess express instructions from his transferor in order to cause the issuance of a certificate of stock to him.

III. ANALYSIS: FOLLOWING THE TRAIL

A. Jurisprudential History on Certificates of Stock: From Hager to Teng

The first definitive Supreme Court pronouncement on the issue of certificates of stock was in the 1911 case of *Hager v. Bryan*.³⁷ In that case, A. R. Hager filed an action for *mandamus* against Albert Bryan, the corporate secretary of the Visayan Electric Company, to transfer in the books of the company certain shares of stock which he alleged to have been indorsed to him by the Bryan-Landon Company, a duly registered stockholder. However, there was no allegation that Hager held any power of attorney from the said company authorizing him to demand the secretary to make the transfer. The Court held that absent any clear legal obligation on the part of the company to record the transfer, such writ of *mandamus* will not issue. The *ratio* flowed from the express mandate of Section 52 of the Corporation Law,³⁸ which imposed a duty upon the corporation organized under that Act, and upon the officer in charge of the books of the corporation, to provide for the entry and noting upon the books of the corporation of lawful transfers of stock, where the entry of such transfers is lawfully demanded.³⁹ Therefore, insofar as the corporation is concerned, its books determine whether or not one is a shareholder of the corporation. Without a power of attorney from the Bryan-Landon Company, Hager's claim as the indorsee or transferee of the said shares must fail.

Two important implications were borne out of the *Hager* Doctrine, which interpreted the provisions of the Section 35 of the then Corporation

37. *Hager*, 19 Phil. at 138.

38. Philippine Corporation Law, Act No. 1459 (1906).

39. *Hager*, 19 Phil. at 140.

Law, the immediate precursor of Section 63 of the present Corporation Code. The first is that *Hager* set the Stock and Transfer Book at the center of every corporate transaction involving shares of stock. And second, the requirement of an express authority, written or otherwise, for the proper negotiation of certificates of stock further limited the quasi-negotiable nature of stock certificates. This would be the ruling case law for several years to come.

Subsequently, *Montserrat v. Ceron*⁴⁰ tackled the issue of whether or not it is necessary to record in the books of the corporation a mortgage of shares of stocks covered by a stock certificate. The Court held that although a recording in the stock and transfer book is needed for a transfer to be valid and binding against third persons, a chattel mortgage does not come under the word 'transfer' as contemplated in Section 35 of the Corporation Law. The Court interpreted this provision as requiring only the transfer or absolute conveyance of the ownership of the title to a share need be entered and noted on the books of the corporation and since a chattel mortgage does not come under the purview of complete and absolute alienation, then its entry and notation in the books of the corporation is not an essential requisite to its validity.⁴¹

The same rule, requiring entry and notation in the books of the corporation for the validity of the transfer, was later reiterated in *Uson v. Disomito*.⁴² As a result, the Court in that case held that a later attachment prevails over an earlier unregistered sale.

In *Tuason v. La Previsora Filipina*,⁴³ the importance of delivery was highlighted insofar as to constitute a valid issuance of a certificate of stock. The Court stated that while issuance or delivery of a certificate is not necessary to constitute one a stockholder, delivery is, generally speaking, an essential element of the issuance of certificates. So there is no issuance of a certificate where it is never detached from the stock book although the blanks therein are properly filled up, if the person whose name is inserted therein has no control over the books of the company. The exception to this rule is when the stockholders are officers of the company and have the custody of the stock book and can detach the certificates at any time. Moreover, it has also been held that stock is not issued where a certificate made out in the name of the subscriber is never delivered to him but is retained by the corporation as security for notes given by him for the unpaid

40. 58 Phil. 469 (1933).

41. *Id.* at 474.

42. 61 Phil. 535 (1935).

43. 67 Phil. 36 (1938).

portion of his subscription and this is true even when the subscriber votes the stock and dividends are declared on it.⁴⁴

Subsequently, the case of *Santamania v. Hongkong and Shanghai Banking Corporation*⁴⁵ held that a street certificate, which is a certificate indorsed in blank, entitles the holder, upon its face, to demand its transfer into his name from the issuing corporation. Such certificate is deemed quasi-negotiable and as such the transferee is justified in believing that it belongs to the holder and transferor. In this case, a buyer of 10,000 shares of stock from one mining corporation for which a certificate duly indorsed in blank was issued delivered the said certificate to another brokerage firm to comply with the latter's requirement that she deposit something on account if she wanted to buy shares from another mining corporation. The brokerage firm then delivered this certificate, among other securities, to the bank pursuant to a letter of hypothecation executed by the firm in favor of the bank. At the time of the transaction, there was no knowledge on the part of the bank that the said certificate belonged to a person other than the brokerage firm for it was in the form of a street certificate transferable by mere delivery. The Court held that the buyer could not recover the certificate as her negligence was the proximate cause of the damage. She could have asked the issuing corporation to cancel it and issue new certificates in her name. Thus, the bank could not be faulted for it need not look beyond the certificate to ascertain the ownership of the stock. A *bona fide* pledgee or transferee of a stock from the apparent owner is not chargeable with knowledge of the limitations placed on said certificates by the real owner, or of any secret agreement relating to the use of the stock by the holder.⁴⁶

In 1955, the Court had occasion to discuss the nature of certificates of stock in *De los Santos v. Republic*.⁴⁷ That case involved 1.6 million shares of stocks of Lepanto Mining Company which was duly registered in the books of the corporation under the name of Vicente Madrigal. The certificates of stock covering the said shares were also found to be indorsed in blank by Madrigal and which, without adequate explanation, somehow came into the possession of Hess and Campos, who allegedly transferred these shares to De los Santos and Astraquillo. There was no evidence however, that either Madrigal or the beneficial owner, the Mitsuis, conveyed or alienated said shares nor delivered the certificates to anybody during the period before the Japanese occupation. Briefly stated, De los Santos and his assistant Astraquillo were claiming these shares as a result of separate sales transactions with these

44. *Id.* at 41 (citing 11 FLETCHER'S CYCLOPEDIA OF CORPORATIONS, §§324-25 (perm. ed.)).

45. 89 Phil. 780 (1951).

46. *Id.* at 786.

47. *De los Santos v. Republic*, 96 SCRA 577 (1955).

transferors. In resolving the issue of whether or not the transfer of the shares to De los Santos and Astraquillo were valid, the Court resorted to the quasi-negotiable nature of stock certificates and consequently held that De los Santos could acquire no better title from his transferors who were not proven to have validly acquired any right to such certificates. Certificates of stock are not negotiable instruments. Consequently, a transferee under a forged assignment acquires no title which can be asserted against the true owner, unless his own negligence has been such as to create an estoppel against him.⁴⁸ The rationale behind quasi-negotiability was given as "the great principle that no one can be deprived of his property without his assent except by processes of the law, requires, in the case mentioned, that the property wrongfully transferred or stolen, should be restored to its rightful owner."⁴⁹

Notably, Justice Bengzon registered a strong dissent saying that adherence should be given to the prevailing view in a majority of the states in the United States which holds certificates of stock as negotiable instruments.

The Court reiterated the *De los Santos* doctrine in *Tan v. Securities and Exchange Commission*.⁵⁰ At the same time, it was also held in *Razon v. Intermediate Appellate Court*,⁵¹ that owing to its quasi-negotiable nature, necessarily, for a transfer of stock certificate to be effective, the certificate must be properly indorsed and delivered to the transferee.⁵² This was also the import of the recent decision in *Rural Bank of Lipa City v. Court of Appeals*⁵³ where the Court held that the mere assignment of certificates of stock not coupled with indorsement and delivery could not constitute a valid transfer.

In the case of *Bitong v. Court of Appeals*,⁵⁴ the Supreme Court harmonized the rulings in *Tan* and *Razon* and enumerated the requirements for a valid transfer of stocks, to wit:

1. There must be delivery of the stock certificate.
2. The certificate must be indorsed by the owner or his agent or other persons legally authorized to make the transfer; and
3. To be valid against third parties, the transfer must be recorded in the books of the corporation.⁵⁵

48. *Id.* at 600 (citing ROBERT CLARK, CORPORATE LAW 415 (2d ed. 1986)).

49. *Id.* (citing FISHER, THE PHILIPPINE LAW OF STOCK CORPORATIONS, 132).

50. 206 SCRA 740 (1992).

51. 207 SCRA 234 (1992).

52. *Id.* at 240.

53. 366 SCRA 188 (2001).

54. 292 SCRA 503 (1998).

It must be noted that even *Bitong* acknowledges the Stock and Transfer Book registration requirement to complete the process of the negotiation of the certificate of stocks.

The case that was almost on all fours with *Ponce* was that of *Rural Bank of Salinas*. However in that case, the transferor had a Special Power of Attorney executed in her favor by the original owner who was also the duly registered stockholder. It gave the transferor full authority to sell or otherwise dispose of the 473 shares of stock registered in the original subscriber's name and to execute the proper documents therefor. Pursuant to the authority so given, the transferor assigned the said shares of stock owned and presented to the Rural Bank of Salinas the deeds of assignment covering the assigned shares. The transferor herself prayed for the transfer of the stocks in the stock and transfer book and the issuance of stock certificates in the name of the new owners. Based on those circumstances, the Court held that there was a clear duty on the part of the corporate secretary to register the shares in favor of the new owners, since the person who sought the transfer of shares had express instructions from and specific authority given by the registered stockholder to cause the disposition of stocks registered in his name.

A similar issue was likewise tackled in *Lim Tay v. Court of Appeals*.⁵⁶ The Court ruled that although the duty of a corporate secretary to record transfers of stocks is ministerial, he cannot be compelled to do so when the transferee's title to said shares has no *prima facie* validity or is uncertain. However, the factual circumstances surrounding the ruling lends little support to applying the doctrine lock, stock and barrel to *Ponce*. In *Lim Tay*, the pledgee was claiming ownership over the shares of stocks in question even prior to foreclosure and sale on the basis of the pledgor's inability to fulfill his obligation. Clearly, such amounts to *pactum commissorium* which is contrary to law.

Finally, *Teng v. Court of Appeals*⁵⁷ enunciated the same ruling in *Lim Tay*, although it further muddled up the area which pertains to the proof of *prima facie* validity in order to give rise to a legal obligation on the part of the corporation to accord stockholder standing to the transferee. In this case, there was no discussion as to how the Court arrived at the conclusion that the deed of transfer adverted to by the transferee was sufficient in itself, without further need for express instructions or any written authority from the duly registered stockholder. It was merely declared conclusively that because of the respondents' failure to repudiate the deed of transfer, then such deed is entitled to recording in the books of the corporation. There was

55. *Id.*

56. 293 SCRA 634 (1998).

57. 349 SCRA 35 (2001).

no indication as to the reason why the burden of proof was shifted from one side to another.

B. What The Hole Means: Implications

Ponce is a straightforward application of law and existing jurisprudence involving certificates of stock. The Court held that *mandamus* is not the proper remedy and therefore an ordinary action must be resorted to by the parties in order to prove and enforce their rights. The correctness of the ruling is of no doubt but this Essay asserts that the Court should have broadened the discussion to include the merits and demerits of the present interpretation of various aspects of Section 63 which are relevant or related to the issues presented in the case because it involves some implications which might affect the development of commercial relations. The result of this interpretation essentially limits the quasi-negotiable character of certificates of stock, thus diminishing its value in the commercial world.

1. The transferee must resort to ordinary action instead of *mandamus* to seek stockholder standing.

In the present case, the transferee, commencing an ordinary action in order to prove his right as a stockholder under a written instrument such as a Deed of Assignment or a Deed of Indorsement, must necessarily implead the seller or transferor in a litigious proceeding which makes it a bit impractical for people to deal with shares of stocks. In *Ponce*, the effect is that since Gaid was no longer available to substantiate *Ponce's* claim under the Deed of Indorsement, *Ponce* was then left holding an empty bag as the stock and transfer book of the corporation still lists Gaid as the duly registered stockholder. He would not be able to exercise the rights of ownership over such shares. His only remedy is to resort to a court action to compel Gaid's heirs to recognize the Deed of Indorsement and enforce his rights under the said Deed. If in the unfortunate instance that the duly registered stockholder cannot be found, then the transferee would be left with nothing at all.

As mentioned earlier, shares of stock are the basic units of ownership in today's corporate setting. Certificates of stock in turn, are the tangible representatives of ownership of these units. One of the key features of the corporate vehicle is the free transferability of units of investment, which means that shares of stocks can be transferred even without the consent of other stockholders⁵⁸. However, it can also be argued that in general, free transferability means that shares of stock can be transferred without unnecessary impediments, one of which is the consent of other stockholders. Another one of these impediments is that the implication of the present

⁵⁸. VILLANUEVA, *supra* note 2 at 22.

import of Section 63 which requires that the transferee in an unrecorded sale of shares may be given stockholder standing despite possessing a duly-indorsed and even notarized Deed of Assignment or Indorsement but without an express authority from the transferor, only after a litigious proceeding⁵⁹ in the regular courts as opposed to resorting to a summary action for *mandamus* with the SEC. Therefore, if one is to stay true to one of the crucial features of the corporation as a juridical person and a vehicle of economic development, the law must be interpreted or even changed in favor of one that does not give any additional and unnecessary burden on the stockholder to acquire, transfer or dispose of his investment as his personal or financial circumstances would require. This will better encourage investors to channel their resources through the corporate medium and consequently contribute to the development of the stock market.

2. Transferee must possess express instructions from the transferor ordering the corporation to transfer the ownership of the said shares to him.

What *Ponce* clearly imposes as a natural consequence of the stock and transfer book registration requirement is that a transferee who wishes to have the transaction recorded in the books of the corporation and consequently cause the issuance of a stock certificate in his name must likewise possess express instructions from the stockholder of record, written or otherwise, giving the corporation specific authority to effect such transfer. The Court has held that the mere showing of an indorsement or even a duly notarized Deed of Assignment of stock is not sufficient to justify an obligation from the corporation to record it in its books.

The rule is baffling. The only plausible reason is that for all intents and purposes, what purports to be a sale may not actually be a sale. In other words, it could be a transaction of equitable mortgage, a pledge or any other that in all appearances look very much like a sale but is actually not. It is argued, however, that this reason is insufficient to justify the additional burden imposed on the transferee, thereby lessening the commercial value of transacting in terms of shares of stocks. One of the purposes of the registration requirement is to inform the corporation of any change in share ownership to help it ascertain the persons entitled to the rights and subjected to the liabilities of a stockholder. Insofar as fully paid shares of stock are concerned, this purpose is not relevant at all. In that scenario, it is now argued that the choice must be made by the parties to the transaction and not by the corporation. In practical terms, an equitable mortgage transaction which purports to be a sale between two parties should not have any consequence insofar as the corporation is concerned because there remains a legal owner whom the corporation can hold accountable and subject to the

⁵⁹. *Lim Tay*, 293 SCRA 634 (1998).

liabilities of a stockholder. It may precisely be the kind of business arrangement most convenient for the parties concerned. The purpose so mentioned only becomes relevant when it comes to unpaid or partially paid shares of stocks. From an economic point of view, the benefits of such an arrangement vastly outweigh the concerns regarding the protection of the corporation from paying dividends to those who are only nominal owners in the books of the corporation. Those seeking to deal with shares of stock must be trusted to have taken the proper precautions in order to protect their rights.

IV. RESOLUTION

Justice Bengzon, in his dissenting opinion in the 1955 case of *De los Santos* stated that he deemed it necessary to write a rather extended dissent, due principally to the far-reaching effect of the Court's ruling upon future operations of the local stock market and corporate business.⁶⁰ The resulting doctrines of *Ponce* and that of the long list of cases preceding it prove his point. While it may not be practical or even helpful to overturn the plethora of well-established rulings, the current interpretations of Section 63 and its resulting effects all point towards the necessity of a major overhaul of how shares of stock, and necessarily, certificates of stock, are dealt with in the commercial world.

What this Essay suggests, other than a full legislative review of the present construction of Section 63, is the possibility of something akin to a national stock-and-transfer book system, which incorporates qualities such as reliability, simplicity and suitability in order to facilitate smoothly transactions involving certificates of stock. This national stock and transfer book would register both absolute dispositions and mere encumbrances affecting shares of stock. The unique certificates circulating in that national system may be guaranteed as to its authenticity and reliability by the Government. The system would achieve two important goals. One, it will greatly simplify the issuance of certificates of stock and will encourage investors to deal with it. More importantly, this will consequently change the nature of these certificates from being quasi-negotiable to fully negotiable. And two, for stabilizing purposes, it will involve the Government as an active and necessary player in the development of a fragile economy.

CONCLUSION

The rules governing the issuance of certificates of stock as one of the inherent rights flowing from the ownership of shares of stock are necessarily

60. *De los Santos*, 96 Phil. at 605 (Bengzon, J., dissenting) ("A dissent may at least indicate what is not the law.").

part and parcel of the whole gamut of laws and rules which govern the transfer of stocks. As the great object of all commercial laws is the encouragement of commerce, these rules must serve to facilitate and not to impede the transactions occurring in the commercial arena. In a developing country like the Philippines, greater effort to develop the local stock market must be made because it is a standard indicator of a country's economic progress and we cannot afford not to keep up with the fast-paced dealings in the corporate world today. In this light the Court must expose the rigidity of the law and leave it to the legislature to come up with a creative answer to the problem.