Republic of the Philippines
Department of Finance
Securities and Exchange Commission
SEC Building, EDSA, Greenhills, Mandaluyong City

RESTITUTO T. LOPEZ, on his own behalf and for and on behalf of FERNANDEZ, SANTOS & LOPEZ

Petitioner-Appellee,

- versus -

SEC AC-622
(SEC SICD Case No. 09-95-5140)

ATTY. ELISEO A. FERNANDEZ, WILFREDO Z. PALAD and LINA A. ASENETA

Respondents-Appellants.

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DECISION

This is an Appeal from the 26 June 1998 Decision ("Assailed Decision") of the Securities Investigation and Clearing Department ("SICD") of the Securities and Exchange Commission ("Commission"), the dispositive portion of which states:

> "**WHEREFORE**, in view of all the foregoing, judgment is hereby rendered:
>
> 1. Declaring the partners [sic] meeting held on May 19, 1995 and the resolutions passed thereon null and void.
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> 2. Declaring the Executive Committee of FS&L [sic] still exists and continues to function.
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> While there appears a justification for the creation of a Management Committee, nevertheless, the creation of the same is no longer necessary in view of the pronouncement that the Executive Committee of FS&L [sic] still in existence and therefore it should continue to administer the affairs of the partnership and exercise its duties and responsibilities in accordance with the express provisions of the Articles of Partnership and Partnership Agreement. Considering that the two (2) remaining members of the Executive Committee of the FS&L are the Petitioner Restituto T. Lopez and Atty. Eliseo A. Fernandez, it is necessary that a third person be appointed to the Executive Committee in order to normalize and attain a smooth management and administration of the affairs of the partnership and also to avoid any deadlock in the decision making.

The parties are hereby directed to submit [sic] this Commission the name of the person to be appointed or named as third member of the FS&L Executive Committee who is acceptable to both parties within fifteen (15) days from receipt hereof. In the event that the parties could not agree to a neutral person then, the Commission would select from among the list of nominees [sic] the parties will submit to this Commission also within fifteen (15) days from receipt hereof.

Once constituted, the Executive Committee shall immediately convene and assume the powers, duties and function of FS&L's Executive Committee. In addition thereto, the Committee is also tasked to do immediately the following:

1. To take custody of and control over all the existing assets and properties of FS&L and the management of the said firm to protect the interest of the parties litigant, the [sic] creditors and the general public.

2. To bill services already performed and all unbilled services thereafter.

3. To collect all receivables of FS&L and all other receivables of FS&L and all other receivables that will be identified by the Executive Committee.

4. To bill and require Emerald and Registry Corporation to pay immediately its unpaid share in the rental and other charges and

5. To render an accurate accounting of the FS&L's Financial transactions.

3. As to damages, petitioners [sic], is entitled to:

   a. Actual damages and other entitlements as a senior partner and member of the executive committee corresponding to his accrued regular monthly drawings, which the respondents had withdrawn to be computed based on actual Execom drawings.

   b. Moral damages in the amount of Two Million (P2,000,000.00) Pesos for the injury suffered, mental anguish, anxiety, sleepless [nights] that respondents have caused to the petitioner.

Further the writ of preliminary injunction issued by the Commission on (sic) 2nd day of September 1996 is hereby made permanent and the preliminary injunction bond posted by the petitioner is hereby lifted.

SO ORDERED."[1]

ANTECEDENT FACTS AND PROCEEDINGS

As borne out by the evidence on record, the following are the antecedent facts and proceedings:

On 11 September 1995, Petitioner-Appellee Restituto T. Lopez ("Lopez") filed a Petition[2] for appointment of management committee/receiver with preliminary injunction and/or immediate restraining order on his behalf and for and on behalf of Fernandez, Santos and Lopez ("FS&L") against Respondents-Appellants Atty. Eliseo A. Fernandez ("Fernandez"), Wilfredo Z. Palad ("Palad") and Lina A. Aseneta ("Aseneta"). The Petition prayed for the following: a) the issuance of a restraining order and/or writ of preliminary injunction enjoining Respondents-Appellants from making further unauthorized withdrawals of partnership funds from FS&L's accounts and from taking the remaining assets and properties of FS&L from its official principal office; and b) the appointment of a management committee and/or receiver to take custody of, and control over the remaining assets, resources and properties of FS&L and to undertake the management of the partnership.

FS&L is a general and professional partnership engaged in accountancy, which was organized on 01 July 1990 and governed by the Articles of Partnership ("AOP") signed and executed by Fernandez, Lopez and Petronilo S. Santos ("Santos"), the three (3) senior partners and principal owners of FS&L.[3] As stated in the AOP of FS&L, each senior partner shall contribute the amount of Two Hundred Fifty Thousand Pesos (P250,000.00) or a total of Seven Hundred Fifty Thousand Pesos (P750,000.00). Subsequently, the three senior partners entered into a General Partnership Agreement ("GPA") with the Junior Partners of FS&L, including Palad and Aseneta.[4]

Article VII of the AOP and Article VI of the GPA provides that FS&L shall be governed and administered by an Executive Committee composed of the three (3) senior partners-Fernandez, Santos and Lopez, *viz*:

> Section 1. – The affairs of the partnership shall be administered by an Executive Committee which shall be composed of the signatories of this agreement and who shall continue to serve as members of the Executive Committee until they resign or

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[1] Original Records SEC SICD Case No. 09-95-5140, Decision of the SICD dated 26 June 1998, Records pp. 320-322, Volume IV.
[2] *Ibid.*, Petition dated 08 August 1995, Records pp. 103-127, Volume I.
[3] *Ibid.*, Articles of Partnership dated 04 June 1990, Records pp. 94-102, Volume I.
[4] *Ibid*, General Partnership Agreement dated 01 July 1990, Records pp. 82-92, Volume I.

shall have been replaced, pursuant to a holding two-thirds (2/3) vote of the partners of the units of participation.

On 07 November 1990, the Executive Committee executed a Partners' Certificate which authorized its three members to open FS&L's current and saving deposit accounts.[5] Similarly, the 07 November 1990 Partner's Certificate provides that all withdrawals and disbursements of funds from FS&L's accounts shall be made only on the authority or signature of any two of the three Executive Committee members, except for withdrawals/disbursements not exceeding Php 5,000.00 which may be made upon the authority or signature of any two of the four individuals: Fernandez, Santos, Lopez or Aseneta.

In June 1993, Santos withdrew from the firm, thus, the Executive Committee was reduced into a two-member committee composed of Lopez and Fernandez. Consequently, in 1995, Lopez filed the instant Petition for himself and on behalf of the partnership allegedly to prevent wanton dissipation, loss, wastage and destruction of the assets, resources and properties of FS&L, and the paralization of its business, resulting from the gross mismanagement and the fraudulent and unauthorized acts of Fernandez in conspiracy with the Junior Partners of the firm. [6]

In his Petition, Lopez alleged the following fraudulent and unauthorized acts of gross mismanagement of Fernandez, in conspiracy with the Junior Partners of the firm: [7]

a. Sometime in 1995, Respondents-Appellants committed unauthorized and fraudulent withdrawals of the partnership funds contrary to the 07 November 1990 Partner's Certificate. Fernandez and Aseneta circumvented the limit imposed by issuing multiple checks to same payees that Metrobank honored with face amounts in excess of Five Thousand Pesos (₱5,000.00) and co-signed by said Fernandez and Aseneta. Upon inquiry with Metrobank, it was discovered that Respondents-Appellants signed a Partner's Certificate dated 22 May 1995, supposedly amending the Partnership Certificate dated 07 November 1990 and authorizing any withdrawals and/or disbursements of the funds of the partnership in Metrobank by any two (2) of the following partners, signing jointly: Lopez, Fernandez, Aseneta and Palad. By virtue of said Partners' Certificate dated 22 May 1995, a total amount of Two Million Seven Hundred Sixty Four Thousand Six Hundred Ninety Three Pesos and Seventy Seven Centavos (₱2,764,693,77) was withdrawn as of 28 August 1995, to the damage and prejudice of Lopez as fifty percent (50%) owner of the partnership, and to the damage and prejudice of FS&L and its creditors.

[5] *Ibid.*, Partners' Certificate dated 07 November 1990, Records p. 80, Volume I.
[6] *Supra*, Note 2.
[7] *Ibid.*

b. Emerald Registry Transfers Corporation ("Emerald Registry"), which is owned and controlled by Fernandez, has been occupying an 80 square meter portion of FS&L's office space in Metrobank Plaza without paying rentals to FS&L, its share in the bills for utilities and use of common areas, as well as its shares in the salaries of FS&L's employees involved in the operations of Emerald Registry. Per Fernandez, Emerald Registry has purportedly been extending loans to FS&L, thus, Emerald Registry can avoid payment of rentals, and its shares in the bills of utilities and salaries.

c. Fernandez, as Chairman of FS&L, has grossly mismanaged the affairs of the partnership by: a) engaging in unprofessional and unethical conduct, b) failing to bill and collect from clients for services rendered by FS&L, c) removing most of the partnership records, supplies, equipment and other remaining assets and properties from FS&L's Principal office, and d) deliberately withholding from Lopez financial reports and various related documents and vital communications pertaining to the business of FS&L.

On 05 June 1996, Respondents-Appellants submitted their Answer[8] to the Petition categorically denying all the material allegations in the Petition. As their special and affirmative defenses, they alleged that:

a. FS&L partnership had been dissolved by operation of law (Articles 1828 and 1830 of the Civil Code) by virtue of the withdrawal of Santos as senior partner and because of the dissolution of FS&L, the Executive Committee created and organized under the AOP and GPA rendered the said committee *functus officio*. Article VII, Section 1 of the GPA stipulates that the senior partners shall have seventy percent (70%) units of participation while the junior partners shall have thirty percent (30%) units of participation. Prior to the withdrawal of Santos, the senior partners shared the seventy percent (70%) amongst themselves in the following proportion: Fernandez, forty percent (40%); Santos, thirty percent (30%); and Lopez, thirty percent (30%). Thus, subsequent to Santos' withdrawal, the units of his participation were automatically allocated between the two (2) remaining senior partners, namely, Lopez and Fernandez, in accordance with their respective actual interests. Accordingly, Lopez and Fernandez's share in the seventy percent (70%) units of participation were proportionally increased to forty three percent (43%) and fifty seven percent (57%), respectively.

b. Contrary to Lopez's allegations, Respondents-Appellants have not committed any fraudulent or unauthorized withdrawal of partnership funds. The Partners' Certificate dated 22 May 1995 was unanimously approved and adopted by the partners present during a partners' meeting held on 19 May 1995 which was attended by Respondents-

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[8] *Ibid.*, Answer dated 04 June 1996, Records pp. 190-199, Volume II.

Appellants, who held units of participation that were more than enough to constitute a quorum. Lopez was duly notified of such meeting but did not attend without any justifiable reason. The modification of the banking arrangements was prompted by Lopez's unjustified refusal to sign the firm's checks to pay for its outstanding obligations and expenses necessary for the day-to-day operations. Thus, all payments were made in good faith in the interest of the partnership and without intending to cause, nor actually causing, prejudice or damage to Lopez or to any other partner, or to FS&L.

c. Regarding Emerald Registry, Lopez was aware of the fact that Emerald Registry gave substantial advances in favor of FS&L when the latter was unable to meet its outstanding obligations. The rent that Emerald Registry was supposed to pay was deducted from the obligations of FS&L to it.

d. Respondents-Appellants did not make any fraudulent removal of partnership assets and properties. The lease of FS&L over its former office had expired and that the lessor no longer intended to renew the lease because of FS&L's repeated failure or delay to pay the lease rentals caused by Lopez's refusal to sign the check payments. Thus, they were forced to transfer to its present location.

e. Lopez has no cause of action and that Respondents-Appellants' acts are valid even without the consent of the latter as they have been administering the affairs of the partnership in good faith in order to avoid grave and irreparable injury in accordance with Article 1802 of the Civil Code. As compulsory counterclaim, Respondents-Appellants prayed for attorney's fees, moral damages and costs.

After the issues were joined, a preliminary conference was conducted on 03 April 1997. Subsequently, the parties submitted their respective Formal Offers of Evidence[9] and their respective Memoranda[10]. In sum, the issues[11] to be resolved were:

1. Whether or not Respondents-Appellants committed fraudulent acts of gross mismanagement which resulted in wastage and dissipation of partnership's assets that would justify the appointment of a management committee;

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[9] *Ibid.*, Petitioner-Appellee's Formal Offer of Evidence filed on 30 July 1997, Records pp.423-512, Volume IV.; Respondents-Appellants' Formal Offer of Evidence filed on 12 February 1998, Records pp. 585-591, Volume IV.

[10] *Ibid.*, Petitioner-Appellee's Memorandum dated 28 April 1998 filed on 05 May 1998, Records pp. 629-687, Volume IV; Respondents-Appellants Memorandum dated 04 May 1998 filed on 08 May 1998, Records, pp. 688-715, Volume IV.

[11] *Ibid.*, Preliminary Conference Order dated 28 May 1997, Records pp. 403-410, Volume IV.

2. Whether the partners' meeting held on 19 May 1995 and the resolutions passed thereon are valid or not;

3. Whether or not the Executive Committee of FS&L still exists and continues to function as such; and

4. Whether or not petitioner Lopez is liable for damages against respondents and vice versa.

On 26 June 1998, the Hearing Officer rendered the assailed Decision against Respondents-Appellants.

On 29 July 1998, Respondents-Appellants filed a Notice of Appeal together with their Memorandum on Appeal dated 27 July 1998[12] before the Commission *En Banc*. Petitioner-Appellee filed his Reply Memorandum on 06 August 1998[13].

On 11 May 2004, the Commission *En Banc* rendered a Decision[14] dismissing the appeal. The dispositive portion of which reads:

> "WHEREFORE, premises considered, (the) instant appeal is hereby DISMISSED for lack of jurisdiction.
>
> The writ of preliminary injunction issued on 29 August 1996 is DISSOLVED.
>
> No pronouncement as to costs.
>
> SO ORDERED."

As a result, Respondents-Appellants filed a Petition for Certiorari before the Court of Appeals. In an Amended Decision dated 08 December 2006,[15] the Court of Appeals ruled that the provision in Section 5.2 of R.A. 8799[16] retaining the jurisdiction of the Securities and Exchange Commission over pending intra-corporate disputes already submitted for decision upon the law's enactment should be made applicable to the case at bar. Thus, the Court of Appeals directed the Commission *En Banc* to resolve and rule on the appeal filed by herein Respondents-Appellants.

Hence, we rule on this Appeal.

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[12] *Ibid.*, Memorandum on Appeal dated 27 July 1998, Records pp. 1-40, Volume V.
[13] *Ibid.*, Reply Memorandum dated 05 August 1998, Records pp. 33-78, Volume V.
[14] *Ibid.* Decision of En Banc dated 11 May 2004, Records pp. 181-184, Volume V.
[15] *Ibid.*
[16] Republic Act No. 8799, "The Securities Regulation Code" approved on July 19, 2000.

The Appeal of the Respondents-Appellants raises the following assignment of errors:

i. The Honorable Hearing Officer erred in ruling that FS&L was not dissolved by the withdrawal of Santos;

ii. The Honorable Hearing Officer erred in holding that the partners' meeting held on 19 May 1995 and the resolutions passed during that meeting as null and void;

iii. The Honorable Hearing Officer erred in holding that the Executive Committee of FS&L still exists;

iv. The finding that Petitioner-Appellee was denied access to the partnership's financial records is erroneous and not supported by evidence;

v. The Honorable Hearing Officer erred in holding for a fact that Appellant Fernandez had tolerated and/or engaged in corrupt and unethical practice;

vi. The Honorable SEC Hearing Officer erred in finding that the Appellants committed gross mismanagement of FS&L;

vii. The award of actual and moral damages is legally and factually baseless and hence erroneous;

viii. The Honorable SEC Hearing Officer erred in making permanent the injunction earlier issued against the Appellants;

ix. The Honorable Hearing Officer erred in not finding that the Appellants are entitled to their counterclaim against the Petitioner-Appellee

ISSUES:

Respondents-Appellants' assignment of errors may be summarized as follows:

i. Whether or not FS&L was dissolved after the resignation of Santos from the partnership;

ii. Whether or not the Executive Committee of FS&L continued to exist and function after the resignation of Santos from the partnership;

iii. Whether or not the meeting held on 19 May 1995 and the resolutions passed thereon are void;

iv. Whether or not Respondents-Appellants committed fraudulent acts of mismanagement of FS&L;

v. Whether or not Petitioner-Appellee is entitled to actual and moral damages;

vi. Whether or not the SEC Hearing Officer erred in making permanent the injunction earlier issued against the Respondent-Appellants; and

vii. Whether or not Respondents-Appellants are entitled to their counterclaim.

RULING:

After a diligent review of the evidence and the applicable laws, rules and jurisprudence, we find the instant Appeal to be **partly meritorious.**

The findings of fact of the SEC Hearing Officer must be respected as long as they are supported by substantial evidence. In the instant case, the SEC Hearing Officer had the opportunity to personally observe the demeanor of all the witnesses presented and to study thoroughly all the evidence submitted. His Decision threshed out in detail all the established facts, the issues, and evidence presented.

Whether or Not FS&L was Dissolved After the Resignation of Santos from The Partnership

As to the first issue, Respondents-Appellants argued in their Appeal that Articles 1828 and 1829 of the Civil Code of the Philippines ("Civil Code") are applicable in the case at bar, and that the Honorable SEC Hearing Officer was confused by the terms "dissolution", "winding-up" and "termination." Respondents-Appellants claim that Santos, by withdrawing from the partnership, ceased to be associated in carrying on of the business, as his withdrawal falls within the definition of the term "dissolution" in Article 1828 of the Civil Code. The pertinent provisions of the Civil Code provide, to wit:

> "Article 1828. The dissolution of a partnership is the change in the relation of the partners caused by any partner ceasing to be associated in the carrying on as distinguished from the winding up of the business."

> "Article 1829. On dissolution the partnership is not terminated, but continues until the winding up of the partnership affairs is completed.

Article 1828 gives the definition of dissolution while Article 1829 explains the effect of such dissolution under the Civil Code. The causes of dissolution are either judicial or extrajudicial. The extrajudicial causes are those enumerated in Article 1830[18] of the Civil Code while the judicial causes are those mentioned in Article 1831.[19]

Although Article 1830 includes the withdrawal of a partner as one of the causes for dissolution (*i.e.*, by the express will of any partner, who must act in good faith, when no definite term or particular undertaking is specified), we agree with the findings of the SEC Hearing Officer that the said provision does not apply in this case. It must be remembered that the AOP executed by Lopez, Santos, and Fernandez is binding amongst them. Thus, an evaluation of the AOP and GPA of FS&L is pertinent. Section 1, Article III of the AOP[20] and Article III of the GPA[21] provide:

> "This agreement shall take effect on July 1, 1990 and shall continue for an indefinite duration of time unless the Executive Committee shall decide otherwise. Except as

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[18] Article 1830. Dissolution is caused: (1)Without violation of the agreement between the partners: (a) By the termination of the definite term or particular undertaking specified in the agreement; (b) By the express will of any partner, who must act in good faith, when no definite term or particular is specified; (c) By the express will of all the partners who have not assigned their interests or suffered them to be charged for their separate debts, either before or after the termination of any specified term or particular undertaking; (d) By the expulsion of any partner from the business bona fide in accordance with such a power conferred by the agreement between the partners; (2) In contravention of the agreement between the partners, where the circumstances do not permit a dissolution under any other provision of this article, by the express will of any partner at any time; (3) By any event which makes it unlawful for the business of the partnership to be carried on or for the members to carry it on in partnership; (4) When a specific thing which a partner had promised to contribute to the partnership, perishes before the delivery; in any case by the loss of the thing, when the partner who contributed it having reserved the ownership thereof, has only transferred to the partnership the use or enjoyment of the same; but the partnership shall not be dissolved by the loss of the thing when it occurs after the partnership has acquired the ownership thereof; (5) By the death of any partner; (6) By the insolvency of any partner or of the partnership; (7) By the civil interdiction of any partner; (8) By decree of court under the following article. (1700a and 1701a)

[19] Article 1831. On application by or for a partner the court shall decree a dissolution whenever: (1) A partner has been declared insane in any judicial proceeding or is shown to be of unsound mind; (2) A partner becomes in any other way incapable of performing his part of the partnership contract; (3) A partner has been guilty of such conduct as tends to affect prejudicially the carrying on of the business; (4) A partner wilfully or persistently commits a breach of the partnership agreement, or otherwise so conducts himself in matters relating to the partnership business that it is not reasonably practicable to carry on the business in partnership with him; (5) The business of the partnership can only be carried on at a loss; (6) Other circumstances render a dissolution equitable. On the application of the purchaser of a partner's interest under article 1813 or 1814: (1) After the termination of the specified term or particular undertaking; (2) At any time if the partnership was a partnership at will when the interest was assigned or when the charging order was issued. (n)

[20] *Supra,* Note 3.

[21] *Supra,* Note 4.

> otherwise provided by law, the death, incapacity, **withdrawal** or retirement **of any partner shall not bring about the dissolution of the *partnership*, which shall continue to exist and carry on its activities among the remaining or surviving partners.**" (Emphasis ours)

An agreement of the partners, like any other contract, is binding among them and normally takes precedence to the extent applicable over the Civil Code's general provisions.[22] Clearly, there is an express provision in FS&L's AOP and GPA that the withdrawal of any partner shall not bring about the dissolution of the partnership, and the same shall continue to exist and carry on its activities among the remaining or surviving partners. Instructive on this point is the case of *Eufracio D. Rojas v. Constancio B. Maglana,*[23] where the Supreme Court recognized the existence and continuation of a partnership despite one partner's withdrawal where it appeared evident that it was not the intention to dissolve the partnership upon the said partner's withdrawal. In the present case, records disclose that the partnership of FS&L continued its operations even after the resignation of Santos as evidenced by a report dated June 1995 of the accounts receivable of FS&L as of 10 June 1995.[24] Evidently, it was not the intention of the remaining partners to dissolve the partnership. Therefore, Respondents-Appellants' contention that Articles 1828 and 1829 of the Civil Code are applicable, is incorrect. In this case, FS&L's AOP and GPA provide for an exception to the general rule stated in the Civil Code and the same shall govern. Hence, FS&L was not dissolved after the resignation of Santos from the partnership.

Whether or Not the Executive Committee of FS&L Continued to Exist After the Resignation of Santos from the Partnership

As to the second issue, we find no reason to disturb the findings of the SEC Hearing Officer insofar as he declared that the Executive Committee of FS&L still exists. The SEC Hearing Officer determined:

> "FS&L Executive Committee was initially composed of the three (3) senior partners, namely: Atty. Eliseo A. Fernandez, Mr. Petronilo S. Santos, and Restituto T. Lopez. However, upon the retirement of Petronilo S. Santos on June 20, 1993, there are still two (2) members left in the Executive Committee of FS&L namely: Atty. E. Fernandez and Mr. R. Lopez. The records also show that the partnership of FS&L continues to operate. From July 1, 1993 to May 19, 1995 or almost two years,

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[22] *Ortega v. Court of Appeals*, G.R. No. 109248, 03 July 1995.
[23] G.R. No. 30616, 10 December 1990.
[24] Original Records SEC SICD Case No. 09-95-5140, FS&L's Report on Accounts Receivable as of 10 July 1995, Records pp. 269-289, Volume II.

the remaining majority members of the Executive Committee continue to discuss matters related to the partnership. Respondent Fernandez and petitioner Lopez remained as members of FS&L Executive Committee as both have neither resigned nor replaced. Sections 1 and 3 of Article VII of FS&L Articles of Partnership provide "**that members of the Executive Committee will continue to serve in such positions until they resign or shall have been replaced**." (Emphasis ours)

As a result of FS&L's continuing existence and carrying on its operations among the remaining partners, it therefore follows that the Executive Committee was not rendered *functus officio* by the resignation of Santos. To reiterate, after the withdrawal of Santos, the partnership continued to exist and operate,[25] which necessarily means that the Executive Committee also continue to function considering that the AOP of FS&L expressly provides that it is the Executive Committee which shall administer the affairs of the partnership. Further, the AOP provides that the members of the Executive Committee shall continue to serve in such capacity until they resign or shall have been replaced. Obviously, since Fernandez and Lopez neither resigned nor were replaced, they continued to be members of the Executive Committee. If only Fernandez and Lopez, after the withdrawal of Santos agreed to admit a replacement in the 3-member Executive Committee by inviting a new senior partner, or elevating one of the junior partner to senior partner status[26] the management impasse should have been avoided.

Be that as it may, the vacancy created by the withdrawal of Santos from the partnership in the Executive Committee of FS&L, did not incapacitate the Committee.

Whether or Not the Meeting Held on 19 May 1995 and the Resolutions Passed thereon are Void

As to the third issue, we likewise agree with the findings of the Hearing Officer that the 19 May 1995 meeting and the resolutions passed are null and void.

It was argued by Respondents-Appellants that the partners holding majority of units of participation were present at the meeting held on 19 May 1995. However, it must be emphasized that the issue that must be resolved is whether the calling of such meeting was compliant with Article VIII of the AOP and Article XII of the GPA, *viz:*

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[25] Art. 1785 of the Civil Code provides that a continuation of the business by the partners without any settlement or liquidation of the partnership affairs is prima facie evidence of the continuation of the partnership.
[26] Allowed under Sec. 1, Art V of the FAOP.

Meetings of Partners; Voting at Such Meetings

Section 1. – **Subject to the approval of the Executive Committee**, a meeting of the partners shall be held at any time on written notice by any two partners at least two (2) days in advance, specifying the hour and purposes of the meeting.

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Section 3. – A quorum for any issue at any meeting shall exist if [sic] partners holding a majority of such units are present in person or voting by proxy or written instruction." (Emphasis ours, underscoring theirs)

From the foregoing, it is evident that the approval of the Executive Committee must first be obtained prior to the calling of a partners' meeting. With the remaining Executive Committee being a two (2) member committee composed of Lopez and Fernandez, it means that in order to call a meeting, both partners, acting as the Executive Committee, should approve such action.

However, in this case, a perusal of the Notice of the 19 May 1995 meeting shows that it was signed by Fernandez alone acting as Senior Managing Partner. Hence, though Lopez was notified[27] of the said meeting, the calling thereof is still violative of the provisions in the AOP and GPA considering that the calling of a meeting must be approved by the now two-member Executive Committee.

As to the resolutions passed during the said meeting, Article XVIII of the AOP and Article XIX of the GPA provide:

Partnership Funds

All funds of the partnership, except petty cash for daily expenses, shall be deposited in the name of the firm in a bank or banks to be designated by the Executive Committee. No withdrawals from the account shall be allowed except by check or any other negotiable instrument signed by persons **authorized by the Executive Committee**. (Emphasis ours)

Thus, the Hearing Officer correctly held:

"It is very clear from the foregoing provision that no withdrawal of funds can be allowed unless signed by persons authorized by the Executive Committee. Sec. 1 of Article VIII explicitly [says] that partners' meeting is subject to approval by the Executive Committee. The provisions on the Articles of Partnership are binding upon the partners. **Since the May 19, 1995 meeting was not approved by the Executive Committee, the said meeting was invalid. It, therefore, follows that the**

[27] *Ibid.*, Notice of Partner's Meeting, Records p. 72, Volume III. But did not attend.

resolutions passed thereon amending the check signatories are also invalid." (Emphasis ours.)

Whether or Not Respondents-Appellants Committed fraudulent Acts of Mismanagement of FS&L

We now discuss the fourth issue. We disagree with the findings of the SEC Hearing Officer that gross mismanagement was committed by Respondents-Appellants, justifying the creation of a management committee. His findings were:

> "The unauthorized disbursements of the partnership funds, by themselves alone may not be considered fraudulent acts **but (1)** the failure to bill services already performed amounting to millions of pesos as of April 30, 1993 (TSN dated May 20, 1997, Exhs. "C" to "C-1-a") **(2)** failure to collect receivables amounting to millions of pesos (Exhs "M" & "N") **(3)** accumulation of losses amounting to P8,088.676 [sic] as of December 31, 1993 (Exhs "Q" tp "Q-45", "L to L-2", TSN dated May 20, 1997 pp 42-52) **(4)** failure to charge or bill Emerald Registry & Transfers Corporation its rightful share in the rentals (Exhs "K", "CC & BB" and TSN dated May 20, 1997) **(5)** failure to account and give petitioner Lopez from exercising his powers as member of the Executive Committee **constitute gross mismanagement**. (Exhs "Z", "Z-1", "AA" to "A-2")" (Emphasis ours)

At the time this Appeal was filed, the applicable law was Section 6 (d) of Presidential Decree 902-A, as amended ("PD 902-A)[28]" which grants the Commission the power to create and appoint a management committee, to wit:

> "d) To create and appoint a management committee, board, or body upon petition or *motu propio* to undertake the management of corporations, partnerships or other associations not supervised or regulated by other government agencies in appropriate cases **when there is imminent danger of dissipation, loss, wastage or destruction of assets or other properties or paralization of business operations of such corporations or entities which may be prejudicial to the interest of minority stockholders, parties-litigants or the general public**: Provided, further, That the Commission may create or appoint a management committee, board or body to undertake the management of corporations, partnerships or other associations supervised or regulated by other government agencies, such as banks and insurance companies, upon request of the government agency concerned." (Emphasis supplied)

[28] Reorganization of the Securities and Exchange Commission with Addition Powers and Placing the Said Agency Under Administrative Supervision of the Office of the President; March 11, 1976, as amended by P.D. 1799, January 16, 1981.

Thus, the Supreme Court in the case of *Rizal Commercial Banking Corporation v. Intermediate Appellate Court,*[29] in explaining Section 6 (d) of PD 902-A, held:

> "A petition for rehabilitation does not always result in the appointment of a receiver or the creation of a management committee. The SEC has to initially determine whether such appointment is appropriate and necessary under the circumstances. Under Paragraph (d), Section 6 of Presidential Decree No. 902-A, **certain situations must be shown to exist before a management committee may be created or appointed**, such as:
>
> 1. When there is imminent danger of dissipation, loss, wastage or destruction of assets or other properties; ***or***
>
> 2. When there is paralization of business operations of such corporations or entities which may be prejudicial to the interest of minority stockholders, parties-litigants or to the general public." (Emphasis ours)

Therefore, in order for the Commission to create and appoint a management committee, the two circumstances enumerated above must first be proven.

The word "*imminent*" has been defined as "impending or on the point of happening" while "*danger*" means "peril or exposure to loss or injury."[30] In order to establish these, the allegations in the pleadings and documentary evidence submitted should be examined. In addition, not only must these circumstances be proven, but the Supreme Court in the case of *Rev. Luis Ao-As v. Court of Appeals*[31] declared:

> "It is the general rule that a receiver (or a management committee) will not be appointed unless it appears that the appointment is **necessary either to prevent fraud, or to save the property from fraud or threatened destruction**, or at least in case of solvent corporation x x x. The burden of proof is a heavy one which requires a **clear showing that an emergency exists**. (Emphasis ours)

In the case at bar, Lopez failed to establish that Respondents-Appellants committed fraudulent acts of mismanagement of FS&L that caused imminent danger of dissipation, loss, wastage or destruction of the assets or other properties of FS&L. Likewise, it cannot be said that there is paralization of business operations of FS&L to the prejudice of the parties-litigants. Instead, what the parties were able to establish was that there is **serious**

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[29] G.R. No. 74851, 09 December 1999.
[30] *Jacinto v. First Women's Credit Corporation*, G.R. No. 154049, 28 August 2003.
[31] *Rev. Luis Ao-As v. Court of Appeals*, G.R. No. 128464, 20 June 2006.

disagreement as to the management of the partnership affairs while business operations were ongoing.[32]

We must note that the SEC Hearing Officer considered the following acts as gross mismanagement:

a) Failure to bill services already performed amounting to millions of pesos as of April 30 1993;
b) Failure to collect receivables amounting to millions of pesos;
c) Accumulation of losses amounting to 8,088,676 as of December 1993;
d) Failure to charge or bill Emerald Registry & Transfer Corporation its rightful share in the rentals;
e) Failure to account for and give Lopez his regular drawings and entitlement; and
f) Preventing Lopez from exercising his power as member of the Executive Committee;

However, the first four acts abovementioned pertain to losses incurred by the partnership *per se* which may not be imputed to Respondents-Appellants alone.

Lopez distanced himself from the partnership refusing to participate in its affairs, thus paralyzing the Executive Committee and, in turn, the firm's daily operations. Still, even though Lopez took an indifferent approach toward FS&L affairs, Fernandez had no right to resort to measures that find no sanction under the FAOP, GPA or law, let alone take matters into his own hands. He could not validly exclude Lopez form FS&L, as was the case with the May 19, 1995 partners' meeting, which could not have been held validly without Executive Committee's approval as required under the FAOP. Fernandez's recourse was not to digress from what was agreed upon, but to resort to avenues or processes authorized by its charter or the law.

He may have been motivated by the desire to continue FS&L's business, in the absence of Lopez, but failed in observing the proper legal measures for want of legal knowledge. If his management of FS&L's affairs resulted in losses and lost opportunities, Lopez should equally share the blame, since he ceased to productively participate in the management. He is in *pari delicto*. And, where the parties are in *pari delicto,* no affirmative relief of any kind will be given to one against the other.[33]

As to the fifth and sixth acts considered by the SEC Hearing officer as gross mismanagement, we likewise disagree as said acts rather indicate and portray the falling-out

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[32] Emphasis ours.
[33] Hulst v. PR Builders, Inc., G.R. 156364, September 3, 2007

and disagreements between Lopez and Fernandez. Moreover, other that Lopez's mere allegation these were not supported by evidence on record.

Accordingly, there is no basis for the SEC Hearing Officer to conclude that there was gross mismanagement on the part of Respondents-Appellants that justifies the creation of a management committee.

Nevertheless, assuming *arguendo* that there was gross mismanagement, the same case of *Ao-Ao*[35] explained that the appointment of a receiver (or a management committee) for a going concern is a last resort remedy, and should not be employed when another remedy is available.[36] Relief by receivership (or creation of a management committee) is an extraordinary remedy and is never exercised if there is an adequate remedy at law or if the harm can be prevented by an injunction or a restraining order.[37] **Bad judgment by directors, or even unauthorized use and misapplication of the company's funds, will not justify the appointment of a receiver (or a creation of a management committee) for the corporation if appropriate relief can otherwise be had.**[38]

Hence, although we disagree with the findings of the SEC Hearing Officer on the existence of mismanagement, we however agree with his declaration that it is not necessary to create a management committee considering that another remedy still exists, that is, the Executive Committee. Accordingly, a third person must be appointed to the Executive Committee to avoid deadlocks in decision making and smoothen the management and administration of the partnership's affairs.

Whether or Not Petitioner-Appellee is Entitled to Actual and Moral damages

As to the fifth issue, actual and moral damages must be proven before any award thereon can be granted.[39]

We disagree with the findings of the Hearing Officer that Lopez is entitled to actual damages corresponding to his accrued regular monthly drawings. The Civil Code provides that one is entitled to actual or compensatory damages as he has duly proved. Thus:

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[35] *Ao-Ao*
[36] *Ao-Ao.*
[37] *Ibid.*
[38] *Ibid.*
[39] *Renato S. Ong v. Court of Appeals*, G.R. No. 117103, 21 January 1999.

Article 2199 – Except as provided by law or by stipulation, one is entitled to an adequate compensation only for such pecuniary loss suffered by him as he has **duly proved**. Such compensation is referred to as actual or compensatory damages. (Emphasis supplied)

We wish to point out that nowhere in the records does it show that Lopez was able to prove actual or compensatory damages. The Supreme Court in the case of *Renato S. Ong v. Court of Appeals*[40] held:

"The fundamental principle of the law on damages is that one injured by a breach of contract (in this case, the contract of transportation) or by a wrongful or negligent act or omission shall have a fair and just compensation, commensurate with the loss sustained as a consequence of the defendant's acts. Hence, actual pecuniary compensation is the general rule, except where the circumstances warrant the allowance of other kinds of damages.

Actual damages are such compensation or damages for an injury that will put the injured party in the position in which he had been before he was injured. They pertain to such injuries or losses that are actually sustained and susceptible of measurement. Except as provided by law or by stipulation, a party is entitled to adequate compensation only for such pecuniary loss as he has duly proven.

To be recoverable, actual damages must be pleaded and proven in Court. In no instance may the trial judge award more than those so pleaded and proven. **Damages cannot be presumed. The award there of must be based on the evidence presented, not on the personal knowledge of the court**; and certainly not on flimsy, remote, speculative and nonsubstantial proof. Article 2199 of the Civil Code expressly mandates that "[e]xcept as provided by law or by stipulation, one is entitled to an adequate compensation only for such pecuniary loss suffered by him as he has duly proved." (Emphasis supplied)

We likewise disagree with the findings of the Hearing Officer that Lopez is entitled to moral damages. Again, the same is not supported by evidence on record. The case of *Igleserio Mahinay v. Atty. Gabino Velazquez, Jr.*[41] reiterates the rule that in order that moral damages may be awarded, there must be pleading and proof of moral suffering, mental anguish, fright and the like. Hence:

"While respondent alleged in his complaint that he suffered mental anguish, serious anxiety, wounded feelings and moral shock, he failed to prove them during the trial. Indeed, respondent should have taken the witness stand and should have testified on the mental anguish, serious anxiety, wounded feelings and other emotional and mental suffering he purportedly suffered to sustain his claim for moral

[40] *Ibid.*
[41] G.R. No. 152753, 13 January 2004.

damages. **Mere allegations do not suffice; they must be substantiated by clear and convincing proof**. No other person could have proven such damages except the respondent himself as they were extremely personal to him. (Emphasis supplied)

Whether or Not the SEC Hearing Officer Erred in Making Permanent the Injunction Earlier Issued Against the Respondent-Appellants

In relation to this issue, we wish to point out that in our Decision dated 11 May 2004, we declared the writ of preliminary injunction issued on 29 August 1996 to be dissolved. Hence, this issue has been rendered moot and academic.

Whether or Not Respondents-Appellants are Entitled to their Counterclaim for Payment of Attorney's Fees and Moral Damages

As to the last issue, we rule in the negative.

As explained in the case of *Benedicto v. Villaflores,*[42] it is settled that the award of attorney's fees is the exception rather than the general rule; counsel's fees are not awarded every time a party prevails in a suit because of the policy that no premium should be placed on the right to litigate. Attorney's fees, as part of damages, are not necessarily equated to the amount paid by a litigant to a lawyer. Attorney's fees as part of damages are awarded only in the instances specified in Article 2208[43] of the Civil Code.[44] As such, it is necessary for the

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[42] G.R. No. 185020, 06 October 2010.
[43] Article 2208. In the absence of stipulation, attorney's fees and expenses of litigation, other than judicial costs, cannot be recovered, except:
(1) When exemplary damages are awarded;
(2) When the defendant's act or omission has compelled the plaintiff to litigate with third persons or to incur expenses to protect his interest;
(3) In criminal cases of malicious prosecution against the plaintiff;
(4) In case of a clearly unfounded civil action or proceeding against the plaintiff;
(5) Where the defendant acted in gross and evident bad faith in refusing to satisfy the plaintiff's plainly valid, just and demandable claim;
(6) In actions for legal support;
(7) In actions for the recovery of wages of household helpers, laborers and skilled workers;
(8) In actions for indemnity under workmen's compensation and employer's liability laws;
(9) In a separate civil action to recover civil liability arising from a crime;

court to make findings of fact and law that would bring the case within the ambit of these enumerated instances to justify the grant of such award, and in all cases it must be reasonable.[45]

Consequently, Respondents-Appellants failed to establish that the present case falls in any of the instances mentioned in Article 2208 which will justify the award of attorney's fees, particularly the showing of gross and evident bad faith on the part of Lopez when he instituted this case.

As to the award of moral damages, as previously discussed, the same must be substantiated by clear and convincing proof. However, Respondents-Appellants failed to allege and establish that they experienced physical suffering, mental anguish, fright, serious anxiety, besmirched reputation, wounded feelings, moral shock, social humiliation, and similar injury.

WHEREFORE, premises considered, the Appeal is **PARTLY GRANTED**. The Decision of the Hearing Officer 26 June 1998 in SEC SICD Case No. 09-95-5140 is **AFFIRMED** insofar as it declared that:

1. The partners' meeting held on 19 May 1995 and the resolutions passed thereon are null and void;
2. The Executive Committee of FS&L still exists; and
3. A third person be appointed to the Executive Committee in order to normalize and attain a smooth management and administration of the affairs of the partnership and to avoid a deadlock in the decision making.

The Decision is **REVERSED** insofar as it ruled that:

1. Respondents-Appellants committed fraudulent acts of mismanagement of FS&L which justifies the creation of a Management Committee; and

2. Petitioner-Appellee Restituto T. Lopez is entitled to actual and moral damages.

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(10) When at least double judicial costs are awarded;
(11) In any other case where the court deems it just and equitable that attorney's fees and expenses of litigation should be recovered.
In all cases, the attorney's fees and expenses of litigation must be reasonable.
[44] Supra, Note 31.
[45] *Ibid.*

As to the counterclaim of Respondents-Appellants, the same is **DENIED** for failure to sufficiently establish the same.

SO ORDERED.

Mandaluyong City, 12 May 2015.

TERESITA J. HERBOSA
Chairperson

MANUEL HUBERTO B. GAITE
Commissioner

ANTONIETA F. IBE
Commissioner

EPHYRO LUIS B. AMATONG
Commissioner

BLAS JAMES G. VITERBO
Commissioner