

## LAW 101

By: Gregorio M. Batiller, Jr.

### PIERCING THE VEIL OF CORPORATE FICTION (Part 2)

The facts revisited:

On May 29, 1996 PNB International Finance Ltd. (PNB-IFL), a subsidiary company of PNB, organized and doing business in Hong Kong, extended a letter of credit in favor of the respondents in the amount of US\$300,000 secured by real estate mortgages constituted over 4 parcels of land in Makati City. The credit facility was later increased to US\$1,421,316.18 by April 1998.

Respondents-borrowers defaulted on their loans and PNB, representing itself as the attorney-in-fact of PNB-IFL, instituted foreclosure proceedings and the properties subject of the REMs were scheduled to be sold at public auction on May 27, 1997 at the Makati City Hall.

On May 25, 1999, respondents filed a complaint for injunction and/or Temporary Restraining Order with the RTC Makati against PNB. The RTC issued a TRO and subsequently a writ of preliminary injunction.

In justifying its ruling, the RTC reasoned that the corporate entity may be disregarded where a corporation is a mere alter ego or business conduit of a person or where the corporation is so organized and controlled and its affairs are so conducted as to make it merely an instrumentality, agency or adjunct of another corporation (citing *Koppel Phil., Inc. vs. Yatco*, 77 Phil 496). The Court of Appeals sustained the RTC's decision.

On petition for review, the Supreme Court rejected the argument as there was no showing that the subsidiary (PNB-IFL) was formed for an illegal purpose (as in the *Koppel* case: to evade payment of higher taxes).

Instead, the Supreme Court cited *Concept Builders, Inc. vs. NLRC* (257 SCRA 14) wherein it laid down the tests in determining the applicability of the doctrine of piercing the veil of corporation fiction:

- 1) Control, not mere majority control, but complete domination, not only of finances but of policy and business practice in respect to the transaction attacked so that the corporate entity as to this transaction had at the time no separate mind, will or existence of its own.
- 2) Such control must have been used by the defendant to commit fraud or wrong, to perpetuate the violation of a statutory or other positive legal duty, or dishonest and, unjust act in contravention of plaintiff's legal rights; and,
- 3) The aforesaid control and breach of duty must proximately cause the injury or unjust loss complained of.

The absence of any one of these elements prevents "piercing the corporate veil." In applying the "instrumentality" or "alter ego" doctrine, the courts are concerned with reality and not form, with how the corporation operated and the individual defendant's relationship to the operation.

In finally disposing of the case, however, the Supreme Court observed that the parent-subsidary relationship between PNB and PNB-IFL was not really the significant legal relationship involved in the case. Rather that PNB was being sued because it acted as an attorney-in-fact of PNB-IFL in initiating foreclosure proceedings. And since the Rules of Court, every action, must be prosecuted or defended in the name of the real party in interest, then the case against PNB should be dismissed. And since a writ of preliminary injunction is a mere ancillary remedy, the dismissal of the principal action necessarily results in the denial of the prayer for the issuance of the writ. (PNB vs. Ritratto Group, Inc, et. Al G.R. No. 142616, July 31, 2001)

(Note: Respondents, at the time that PNB filed its Motion to Dismiss, could have amended their complaint to implead PNB-IFL as additional party defendant and then perhaps the outcome may have been different).