

Title: Cebu Contractors Consortium Co. vs. Makati Leasing & Finance Corp., G.R. No. 104712, July 3, 1997

—

Facts:

****1. Lease Agreement:****

On August 25, 1976, Makati Leasing and Finance Corporation (MLFC) and Cebu Contractors Consortium Company (CCCC) entered into a lease agreement involving various equipment. The agreement, along with two lease schedules, defined the terms and conditions of the lease.

****2. Chattel Mortgage:****

To secure the lease rentals, CCCC executed a chattel mortgage and an amendment over its other equipment in favor of MLFC.

****3. Default on Lease Rentals:****

Starting June 30, 1977, CCCC defaulted on the lease payments. MLFC sent demand letters, which were ignored by CCCC.

****4. Filing of Complaint:****

MLFC filed a complaint for the payment of the due rentals and sought a writ of replevin to obtain possession of the leased equipment and to foreclose on the mortgaged equipment.

****5. MLFC's Forced Loan Scheme:****

CCCC claimed that it required additional capital for a government road project and approached MLFC for a loan. Instead, MLFC insisted on a sale-leaseback scheme where CCCC ostensibly sold its equipment to MLFC and leased it back. The lease rentals were supposed to be treated as installment payments to repurchase the equipment.

****6. Deed of Assignment:****

CCCC executed a deed of assignment of its collectibles from the Ministry of Public Highways as additional security for the lease payments.

****7. CCCC's Defense:****

CCCC claimed it was no longer indebted to MLFC because payments collected by MLFC from the ministry and the proceeds from foreclosed chattels sufficed to cover its liabilities. CCCC asserted that the deed of assignment had already settled their obligations.

****8. Trial Court Decision:****

The Regional Trial Court upheld the lease agreement and found CCCC liable to MLFC for P1,067,861.79 in lease rentals plus 25% attorney's fees and P486,442.28 in litigation expenses.

****9. Court of Appeals Decision:****

Upon appeal, the Court of Appeals affirmed but reduced the attorney's fees to 10% and eliminated the litigation expenses.

****10. Appeal to the Supreme Court:****

CCCC contested the decision, arguing that the sale-leaseback scheme was an equitable mortgage, that the deed of assignment should release them from their obligation, that they had overpaid MLFC, and requested damages.

Issues:

1. Was the sale-leaseback scheme an equitable mortgage rather than a financing lease?
2. Did the deed of assignment absolve CCCC of its obligations to MLFC?
3. Did subsequent partial payments by CCCC extinguish its obligations under the lease agreement?
4. Was CCCC entitled to damages against MLFC?

Court's Decision:

****1. Nature of the Transaction:****

The Supreme Court sided with CCCC, recognizing that the transaction was an equitable mortgage rather than a genuine financing lease as defined by Republic Act No. 5980. MLFC bought equipment already owned by CCCC solely to provide working capital.

****2. Assignment Not Absolute:****

The deed of assignment did not fully absolve CCCC of its obligations. Subsequent partial payments made by CCCC after the deed of assignment indicated continued liability. Additionally, the execution of a chattel mortgage after the deed of assignment further supported the existence of an ongoing obligation.

****3. Partial Payments:****

CCCC's partial payments and the chattel mortgage indicated the obligations persisted each time payments were made. The prescriptive period for this action had not lapsed.

****4. Overpayment Issue:****

The Court found no convincing evidence of overpayment by CCCC. The Court of Appeals' computation, which did not acknowledge alleged overpayments by CCCC or penalties incurred, remained intact.

****5. No Claim for Damages:****

As CCCC's liability to MLFC stood, their claim for damages was denied.

****Conclusion:****

The decision of the Court of Appeals was affirmed.

Doctrine:

****1. **Equitable Mortgage:****

A transaction initially labeled as a financing lease but structured as a sale-leaseback with existing equipment can be deemed an equitable mortgage if the client's intent was solely to obtain financing.

****2. **Assignment Not Automatic Release:****

An assignment of collectibles or payments does not automatically extinguish debts if subsequent payments by the debtor suggest otherwise.

****3. **Reformation of Instrument:****

When the true intent of a contract is not mirrored in the written instrument, reformation is an adjudicative remedy provided under the Civil Code's provisions on obligations and contracts.

Class Notes:

- **Equitable Mortgage:**** Factors indicating a mortgage rather than a lease (e.g., ownership of equipment, necessity for working capital).
- **Assignment vs. Payment:**** Distinction between the transfer of receivables vs. complete fulfillment of obligations.
- **Reformation of Contracts:**** Civil Code Articles 1359 and 1362 permit contract alteration to reflect actual intent amidst errors or deceit.
- **Statutory Basis:**** "Financial leasing" as defined in RA No. 5980.

****Cited Legal Statutes:****

- ****Republic Act No. 5980:**** Defines financial leasing and regulates financing companies.

- **Civil Code Articles 1359, 1362, and 1144:** Pertaining to reformation and prescription of contracts.

Historical Background:

During the time CCCC entered into agreements with MLFC, financial leasing was relatively novel in the Philippines, subject to evolving regulatory and judicial interpretation, crucial as small and medium enterprises sought innovative financing for capital-intensive projects, particularly for government infrastructure. This case helped clarify the differentiation between legitimate financing methods and disguised loans, further contributing to the jurisprudence on equitable mortgages and contractual intentions.