

PEOPLE'S BANK AND TRUST CO. AND ATLANTIC, GULF AND PACIFIC CO. OF MANILA, PLAINTIFFS AND APPELLANTS, VS. DAHICAN LUMBER COMPANY, DAHICAN AMERICAN LUMBER CORPORATION AND CONNELL ...

G. R. No. L-17500. May 16, 1967

Ponente: DIZON, J.

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DIZON, J.:

On September 8, 1948, Atlantic Gulf & Pacific Company of Manila, a West Virginia corporation licensed to do business in the Philippines, - hereinafter referred to as ATLANTIC - sold and assigned all its rights in the Dahican lumber concession to Dahican Lumber Company - hereinafter referred to as DALCO - for the total sum of \$500,000.00, of which only the amount of \$50,000.00 was paid. Thereafter, to develop the concession, DALCO obtained various loans from the People's Bank & Trust Company - hereinafter referred to as the BANK - amounting, as of July 13, 1950, to P200,000.00. In addition, DALCO obtained, through the BANK, a loan of \$250,000.00 from the Export-Import Bank of Washington D.C., evidenced by five promissory notes of \$50,000.00 each, maturing on different dates, executed by both DALCO and the Dahican American Lumber Corporation, a foreign corporation and a stockholder of DALCO, - hereinafter referred to as DAMCO, all payable to the BANK or its order.

As security for the payment of the abovementioned loans, on July 13, 1950 DALCO executed in favor of the BANK - the latter acting for itself and as trustee for the Export-Import Bank of Washington D.C. - a deed of mortgage covering five parcels of land situated in the province of Camarines Norte, together with all the buildings and other improvements existing thereon and all the personal properties of the mortgagor located in its place of business in the municipalities of Mambulao and Capalonga, Camarines Norte (Exhibit D). On the same date, DALCO executed a second mortgage on the same properties in favor of ATLANTIC to secure payment of the unpaid balance of the sale price of the lumber concession amounting to the sum of \$450,000.00 (Exhibit G). Both deeds contained the following provision extending the mortgage lien to properties to be subsequently acquired - referred to hereafter as "after acquired properties" - by the mortgagor:

"All property of every nature and description taken in exchange or replacement, and all buildings, machinery, fixtures, tools, equipment and other property which the Mortgagor may hereafter acquire, construct, install, attach, or use in, to, upon, or in connection with the premises, shall immediately be and become subject to the lien of this mortgage in the same manner and to the same extent as if now included therein, and the Mortgagor shall from time to time during the existence of this mortgage furnish the Mortgagee with an accurate inventory of such substituted and subsequently acquired property."

Both mortgages were registered in the Office of the Register of Deeds of Camarines Norte. In addition thereto DALCO and DAMCO pledged to the BANK 7,296 shares of stock of DALCO and 9,286 shares of DAMCO to secure the same obligations.

Upon DALCO's and DAMCO's failure to pay the fifth promissory note upon its maturity, the BANK paid the same to the Export-Import Bank of Washington D.C. and the latter assigned to the former its credit and the first mortgage securing it. Subsequently, the BANK gave DALCO and DAMCO up to April 1, 1953 to pay the overdue promissory note.

After July 13, 1950, - the date of execution of the mortgages mentioned above - DALCO purchased various machineries, equipment, spare parts and supplies in addition to, or in replacement of some of those already owned and used by it on the date aforesaid. Pursuant to the provision of the mortgage deeds quoted heretofore regarding "after acquired properties", the BANK requested DALCO to submit complete lists of said properties but the latter failed to do so. In connection with these purchases, there appeared in the books of DALCO as due to Connell Bros. Company (Philippines) - a domestic corporation who was acting as the general purchasing agent of DALCO - hereinafter called CONNELL - the sum of P452,860.55 and to DAMCO, the sum of P2,151,678.34.

On December 16, 1952, the Board of Directors of DALCO, in a special meeting called for the purpose, passed a resolution agreeing to rescind the alleged sales of equipment, spare parts and supplies by CONNELL and DAMCO to it. Thereafter, the corresponding agreements of rescission of sale were executed between DALCO and DAMCO, on the one hand, and between DALCO and CONNELL, on the other.

On January 23, 1953, the BANK, in its own behalf and that of ATLANTIC, demanded that said agreements be cancelled but CONNELL and DAMCO refused to do so. As a result, on February 12, 1953, ATLANTIC and the BANK, commenced foreclosure proceedings in the Court of First Instance of Camarines Norte against DALCO and DAMCO. On the same date they filed an ex parte application for the appointment of a Receiver and/or for the issuance of a writ of preliminary injunction to restrain DALCO from removing its properties. The court granted both remedies and appointed George H. Evans as Receiver. Upon defendants' motion, however, the court, in its order of February 21, 1953, discharged the Receiver.

On March 2, 1953, defendants filed their answer denying the material allegations of the complaint and alleging several affirmative defenses and a counterclaim.

On March 4 of the same year, CONNELL filed a motion for intervention alleging that it was the owner and possessor of some of the equipments, spare parts and supplies which DALCO had acquired subsequent to the execution of the mortgages sought to be foreclosed and which plaintiffs claimed were covered by their lien. In its order of March 18, 1953 the Court granted the motion, as well as plaintiffs' motion to set aside the order discharging the Receiver. Consequently, Evans was reinstated.

On April 1, 1953, CONNELL filed its answer denying the material averments of the complaint, and asserting affirmative defenses and a counterclaim.

Upon motion of the parties the Court, on September 30, 1953, issued an order transferring the venue of the action to the Court of First Instance of Manila where it was docketed as Civil Case No. 20987.

On August 30, 1958, upon motion of all the parties, the Court ordered the sale of all the machineries, equipment and supplies of DALCO, and the same were subsequently sold for a total consideration of P175,000.00 which was deposited in court pending final determination of the action. By a similar agreement one half (P87,500.00) of this amount was considered as representing the proceeds obtained from the sale of the "undebated properties" (those not claimed by DAMCO and CON-NELL), and the other half as representing those obtained from the sale of the "after acquired properties".

After due trial, the Court, on July 15, 1960, rendered judgment as follows:

"IN VIEW WHEREOF, the Court:

1. Condemns Dahican Lumber Co. to pay unto People's Bank the sum of P200,000.00 with 7% interest per annum from July 13, 1950, plus another sum of P100,000.00 with 5% interest per annum from July 13, 1950; plus 10% on both principal sums as attorney's fees;
2. Condemns Dahican Lumber Co. to pay unto Atlantic Gulf the sum of P900,000.00 with 4% interest per annum from July 13, 1950, plus 10% of the principal as attorney's fees;
3. Condemns Dahican Lumber Co. to pay unto Connell Bros, the sum of P425,860.55, and to pay unto Dahican American Lumber Co. the sum of P2,151,678.34 both with legal interest from the date of the filing of the respective answers of those parties, plus 10% of the principals as attorney's fees;
4. Orders that of the sum realized from the sale of the properties of P175,000.00, after deducting the recognized expenses, one-half thereof be adjudicated unto plaintiffs, the Court no longer specifying the share of each because of their announced intention under the stipulation of facts to 'pool their resources'; as to the other one half, the same should be adjudicated unto both plaintiffs, and defendant Dahican American and Connell Bros, in the proportion already set forth on page 9, lines 21, 22 and 23 of the body of this decision; but with the understanding that whatever plaintiffs and Dahican American and Connell Bros. should receive from the P175,000.00 deposited in the Court shall be applied to the judgments particularly rendered in favor of each;
5. No other pronouncement as to costs; but the costs of the receivership as to the debated properties shall be borne by People's Bank, Atlantic Gulf, Connell Bros., and Dahican American Lumber Co., pro-rata."

On the following day, the Court issued the following supplementary decision:

"IN VIEW WHEREOF, the dispositive part of the decision is hereby amended in order to add the following paragraph 6:

6. If the sums mentioned in paragraphs 1 and 2 are not paid within ninety (90) days, the Court orders the sale at public auction of the lands object of the mortgages to satisfy the said mortgages and costs of foreclosure."

From the above-quoted decision, all the parties appealed.

Main contentions of plaintiffs as appellants are the following: that the "after acquired properties" were subject to the deeds of mortgage mentioned heretofore; that said pro-perties were acquired from suppliers other than DAMCO and CONNELL; that even granting that DAMCO and CONNELL were the real suppliers, the rescission of the sales to DALCO could not prejudice the mortgage lien in favor of plaintiffs; that considering the foregoing, the proceeds obtained from the sale of the "after acquired properties" as well as those obtained from the sale of the "undebated properties" in the total sum of P175,000.00 should have been awarded exclusively to plaintiffs by reason of the mortgage lien they had thereon; that damages should have been awarded to plaintiffs against defendants, all of them being guilty of an attempt to defraud the former when they sought to rescind the sales already mentioned for the purpose of defeating their mortgage lien, and finally, that defendants should have been made to bear all the expenses of the Receivership, costs and attorney's fees.

On the other hand, defendants-appellants contend that the trial court erred: firstly, in not holding that plaintiffs had no cause of action against them because the promissory note sued upon was not yet due when the action to foreclose the mortgages was commenced; secondly, in not holding that the mortgages aforesaid were null and void as regards the "after acquired properties" of DALCO because they were not registered in accordance with the Chattel Mortgage Law, the court erring, as a consequence, in holding that said properties were subject to the mortgage lien in favor of plaintiffs; thirdly, in not holding that the provision of the fourth paragraph of each of said mortgages did not automatically make subject to such mortgages the "after acquired properties", the only

meaning thereof being that the mortgagor was willing to constitute a lien over such properties; fourthly, in not ruling that said stipulation was void as against DAMCO and CONNELL and in not awarding the proceeds obtained from the sale of the "after acquired properties" to the latter exclusively; fifthly, in appointing a Receiver and in holding that the damages suffered by DAMCO and CONNELL by reason of the depreciation or loss in value of the "after acquired properties" placed under receivership was *damnum absque injuria* and, consequently, in not awarding to said parties the corresponding damages claimed in their counterclaim; lastly, in sentencing DALCO and DAMCO to pay attorney's fees and in requiring DAMCO and CONNELL to pay the costs of the Receivership, instead of sentencing plaintiffs to pay attorney's fees.

Plaintiffs' brief as appellants submit six assignments of error, while that of defendants also as appellants submit a total of seventeen. However, the multifarious issues thus before Us may be resolved, directly or indirectly, by deciding the following issues:

Firstly, are the so-called "after acquired properties" covered by and subject to the deeds of mortgage subject of foreclosure?; secondly, assuming that they are subject thereto, are the mortgages valid and binding on the properties aforesaid inspite of the fact that they were not registered in accordance with the provisions of the Chattel Mortgage Law?; thirdly, assuming again that the mortgages are valid and binding upon the "after acquired properties", what is the effect thereon, if any, of the rescission of sales entered into, on the one hand, between DALCO and DAMCO, and between DALCO and CONNELL, on the other?; and lastly, was the action to foreclose the mortgages premature?

A. Under the fourth paragraph of both deeds of mortgage, it is crystal clear that all property of every nature and description taken in exchange or replacement, as well as all buildings, machineries, fixtures, tools, equipments, and other property that the mortgagor may acquire, construct, install, attach, or use in, to, upon, or in connection with the premises - that is, its lumber concession - "shall immediately be and become subject to the lien" of both mortgages in the same manner and to the same extent as if already included therein at the time of their execution. As the language thus used leaves no room for doubt as to the intention of the parties, We see no useful purpose in discussing the matter extensively. Suffice it to say that the stipulation referred to is common, and We might say logical, in all cases where the properties given as collateral are perishable or subject to inevitable wear and tear or were intended to be sold, or to be used - thus becoming subject to the inevitable wear and tear - but with the understanding - express or implied - that they shall be replaced with others to be thereafter acquired by the mortgagor. Such stipulation is neither unlawful nor immoral, its obvious purpose being to maintain, to the extent allowed by circumstances, the original value of the properties given as security. Indeed, if such properties were of the nature already referred to, it would be poor judgment on the part of the creditor who does not see to it that a similar provision is included in the contract.

B. But defendants contend that, granting without admitting, that the deeds of mortgage in question cover the "after acquired properties" of DALCO, the same are void and ineffectual because they were not registered in accordance with the Chattel Mortgage Law. In support of this and of the proposition that, even if said mortgages were valid, they should not prejudice them, the defendants argue (1) that the deeds do not describe the mortgaged chattels specifically, nor were they registered in accordance with the Chattel Mortgage Law; (2) that the stipulation contained in the fourth paragraph thereof constitutes "mere executory agree-ments to give a lien" over the "after acquired properties" upon their acquisition; and (3) that any mortgage stipulation concerning "after acquired properties" should not prejudice creditors and other third persons - such as DAMCO and CONNELL.

The stipulation under consideration strongly belies defendants' contention. As adverted to hereinbefore, it states that all property of every nature, buildings, machinery etc. taken in exchange or replacement by the mortgagor "shall immediately be and become subject to the lien of this mortgage in the same manner and to the same extent

as if now included therein". No clearer language could have been chosen.

Conceding, on the other hand, that it is the law in this jurisdiction that, to affect third persons, a chattel mortgage must be registered and must describe the mortgaged chattels or personal properties sufficiently to enable the parties and any other person to identify them, We say that such law does not apply to this case.

As the mortgages in question were executed on July 13, 1950 with the old Civil Code still in force, there can be no doubt that the provisions of said code must govern their interpretation and the question of their validity. It happens, however, that Articles 334 and 1877 of the old Civil Code are substantially reproduced in Articles 415 and 2127, respectively, of the new Civil Code. It is, therefore, immaterial in this case whether we take the former or the latter as guide in deciding the point under consideration.

Article 415 does not define real property but enumerates what are considered as such, among them being machinery, receptacles, instruments or replacements intended by the owner of the tenement for an industry or works which may be carried on in a building or on a piece of land, and shall tend directly to meet the needs of the said industry or works.

On the strength of the above-quoted legal provisions, the lower court held that inasmuch as "the chattels were placed in the real properties mortgaged to plaintiffs, they came within the operation of Art. 415, paragraph 5 and Art. 2127 of the New Civil Code".

We find the above ruling in agreement with our decisions on the subject:

(1) In *Berkenkotter vs. Cu Unjieng*, 61 Phil. 663, We held that Article 334, paragraph 5 of the Civil Code (old) gives the character of real property to machinery, liquid containers, instruments or replacements intended by the owner of any building or land for use in connection with any industry or trade being carried on therein and which are expressly adapted to meet the requirements of such trade or industry.

(2) In *Cu Unjieng e Hijos vs. Mabalacat Sugar Co.* 58 Phil. 439, We held that a mortgage constituted on a sugar central includes not only the land on which it is built but also the buildings, machinery and accessories installed at the time the mortgage was constituted as well as the buildings, machinery and accessories belonging to the mortgagor, installed after the constitution thereof.

It is not disputed in the case at bar that the "after acquired properties" were purchased by DALCO in connection with, and for use in the development of its lumber concession and that they were purchased in addition to, or in replacement of those already existing in the premises on July 13, 1950. In law, therefore, they must be deemed to have been immobilized, with the result that the real estate mortgages involved herein - which were registered as such - did not have to be registered a second time as chattel mortgages in order to bind the "after acquired properties" and affect third parties.

But defendants, invoking the case of *Davao Sawmill Company vs. Castillo*, 61 Phil. 709, claim that the "after acquired properties" did not become immobilized because DALCO did not own the whole area of its lumber concession all over which said properties were scattered.

The facts in the *Davao Sawmill* case, however, are not on all fours with the ones obtaining in the present. In the former, the *Davao Sawmill Company, Inc.* had repeatedly treated the machinery therein involved as personal property by executing chattel mortgages thereon in favor of third parties, while in the present case the parties had treated the "after acquired properties" as real properties by expressly and unequivocally agreeing that they shall automatically become subject to the lien of the real estate mortgages executed by them. In the *Davao Sawmill* decision, it was, in fact, stated that "the characterization of the property as chattels by the appellant is indicative of

intention and impresses upon the property the character determined by the parties" (61 Phil. 712, Underlines supplied). In the present case, the characterization of the "after acquired properties" as real property was made not only by one but by both interested parties. There is, therefore, more reason to hold that such consensus impresses upon the properties the character determined by the parties who must now be held in estoppel to question it.

Moreover, quoted in the Davao Sawmill case was that of *Valdez vs. Central Altagracia Inc.* (225 U.S. 58) where it was held that while under the general law of Puerto Rico, machinery placed on property by a tenant does not become immobilized, yet, when the tenant places it there pursuant to contract that it shall belong to the owner, it then becomes immobilized as to that tenant and even as against his assignees and creditors who had sufficient notice of such stipulation. In the case at bar it is not disputed that DALCO purchased the "after acquired properties" to be placed on, and be used in the development of its lumber concession, and agreed further that the same shall become immediately subject to the lien constituted by the questioned mortgages. There is also abundant evidence in the record that DAMCO and CONNELL had full notice of such stipulation and had never thought of disputing its validity until the present case was filed. Consequently, all of them must be deemed barred from denying that the properties in question had become immobilized.

What We have said heretofore sufficiently disposes of all the arguments adduced by defendants in support of their contention that the mortgages under foreclosure are void, and, that, even if valid, are ineffectual as against DAMCO and CONNELL.

Now to the question of whether or not DAMCO and CONNELL have rights over the "after acquired properties" superior to the mortgage lien constituted thereon in favor of plaintiffs. It is defendants' contention that in relation to said pro-perties they are "unpaid sellers"; that as such they had not only a superior lien on the "after acquired properties" but also the right to rescind the sales thereof to DALCO.

This contention - it is obvious - would have validity only if it were true that DAMCO and CONNELL were the suppliers or vendors of the "after acquired properties". According to the record, plaintiffs did not know their exact identity and description prior to the filing of the case at bar because DALCO, in violation of its obligation under the mortgages, had failed and refused theretofore to submit a complete list thereof. In the course of the proceedings, however, when defendants moved to dissolve the order of receivership and the writ of preliminary injunction issued by the lower court, they attached to their motion the lists marked as Exhibits 1, 2 and 3 describing the properties aforesaid. Later on, the parties agreed to consider said lists as identifying and describing the "after acquired properties", and engaged the services of auditors to examine the books of DALCO so as to bring out the details thereof. The report of the auditors and its annexes (Exhibits V, V-1 - V-4) show that neither DAMCO nor CONNELL had supplied any of the goods of which they respectively claimed to be the unpaid seller; that all items were supplied by different parties, neither of whom appeared to be DAMCO or CONNELL; that, in fact, CONNELL collected a 5% service charge on the net value of all items it claims to have sold to DALCO and which, in truth, it had purchased for DALCO as the latter's general agent; that CONNELL had to issue its own invoices in addition to those of the real suppliers in order to collect and justify such service charge.

Taking into account the above circumstances together with the fact that DAMCO was a stockholder and CONNELL was not only a stockholder but the general agent of DALCO, their claim to be the suppliers of the "after acquired properties" would seem to be preposterous. The most that can be claimed on the basis of the evidence is that DAMCO and CONNELL probably financed some of the purchases. But if DALCO still owes them any amount in this connection, it is clear that, as financiers, they can not claim any right over the "after acquired properties" superior to the lien constituted thereon by virtue of the deeds of mortgage under foreclosure. Indeed, the execution of the rescission of sales mentioned heretofore appears to be but a desperate attempt to better or improve DAMCO and CONNELL's position by enabling them to assume the role of "unpaid suppliers"

and thus claim a vendor's lien over the "after acquired properties". The attempt, of course, is utterly ineffectual, not only because they are not the "unpaid sellers" they claim to be but also because there is abundant evidence in the record showing that both DAMCO and CONNELL had known and admitted from the beginning that the "after acquired properties" of DALCO were meant to be included in the first and second mortgages under foreclosure.

The claim that Belden, of ATLANTIC, had given his consent to the rescission, expressly or otherwise, is of no consequence and does not make the rescission valid and legally effective. It must be stated clearly, however, in justice to Belden, that, as a member of the Board of Directors of DALCO, he opposed the resolution of December 16, 1952 passed by said Board and the subsequent rescission of the sales.

Finally, defendants claim that the action to foreclose the mortgages filed on February 12, 1953 was premature because the promissory note sued upon did not fall due until April 1 of the same year, concluding from this that, when the action was commenced, the plaintiffs had no cause of action. Upon this question the lower court says the following in the appealed judgment:

"The other is the defense of prematurity of the causes of action in that plaintiffs as a matter of grace, conceded an extension of time to pay up to 1 April, 1953 while the action was filed on 12 February, 1953, but as to this, the Court taking it that there is absolutely no debate that Dahican Lumber Co., was insolvent as of the date of the filing of the complaint, it should follow that the debtor thereby lost the benefit to the period,

' . . . unless he gives a guaranty or security for the debt . . . ' (Art. 1198, New Civil Code);

and as the guaranty was plainly inadequate since the claim of plaintiffs reached in the aggregate, P1,200,000 excluding interest while the aggregate price of the 'after-acquired' chattels claimed by Connell under the rescission contracts was P1,614,675.94, Exh. 1, Exh. V, report of auditors, and as a matter of fact, almost all the properties were sold afterwards for only P175,000.00, page 47, Vol. IV, and the Court understanding that when the law permits the debtor to enjoy the benefits of the period notwithstanding that he is insolvent by his giving a guaranty for the debt, that must mean a new and efficient guaranty, must concede that the causes of action for collection of the notes were not premature."

Very little need be added to the above. Defendants, however, contend that the lower court had no basis for finding that, when the action was commenced, DALCO was insolvent for purposes related to Article 1198, paragraph 1 of the Civil Code. We find, however, that the finding of the trial court is sufficiently supported by the evidence, particularly the resolution marked as Exhibit K which shows that on December 16, 1952 - in the words of the Chairman of the Board - DALCO was "without funds, neither does it expect to have any funds in the foreseeable future" (p. 64, record on appeal).

The remaining issues, namely, whether or not the proceeds obtained from the sale of the "after acquired properties" should have been awarded exclusively to the plaintiffs or to DAMCO and CONNELL, and if in law they should be distributed among said parties, whether or not the distribution should be pro-rata or otherwise; whether or not plaintiffs are entitled to damages; and, lastly, whether or not the expenses incidental to the Receivership should be borne by all the parties on a pro-rata basis or exclusively by one or some of them are of a secondary nature as they are already impliedly resolved by what has been said heretofore.

As regard the proceeds obtained from the sale of the "after acquired properties" and the "undebated properties", it is clear, in view of our opinion sustaining the validity of the mortgages in relation thereto, that said proceeds should be awarded exclusively to the plaintiffs in payment of the money obligations secured by the mortgages under foreclosure.

On the question of plaintiffs right to recover damages from the defendants, the law (Articles 1313 and 1314 of the New Civil Code) provides that creditors are protected in cases of contracts intended to defraud them, and that any

third person who induces another to violate his contract shall be liable for damages to the other contracting party. Similar liability is demandable under Arts. 20 and 21 - which may be given retroactive effect (Arts. 2252-53) - or under Arts. 1902 and 2176 of the Old Civil Code.

The facts of this case, as stated heretofore, clearly show that DALCO and DAMCO, after failing to pay the fifth promissory note upon its maturity, conspired jointly with CONNELL to violate the provisions of the fourth paragraph of the mortgages under foreclosure by attempting to defeat plaintiffs' mortgage lien on the "after acquired properties". As a result, the plaintiffs had to go to court to protect their rights thus jeopardized. Defendants' liability for damages is therefore clear.

However, the measure of the damages suffered by the plaintiffs is not what the latter claim, namely, the difference between the alleged total obligation secured by the mortgages amounting to around P1,200,000.00, plus the stipulated interest and attorney's fees, on the one hand, and the proceeds obtained from the sale of the "after acquired properties", and of those that were not claimed neither by DAMCO nor CONNELL, on the other. Considering that the sale of the real properties subject to the mortgages under foreclosure has not been effected, and considering further the lack of evidence showing that the true value of all the properties already sold was not realized because their sale was under stress, We feel that We do not have before Us the true elements or factors that should determine the amount of damages that plaintiffs are entitled to recover from defendants. It is, however, our considered opinion that, upon the facts established, all the expenses of the Receivership, which was deemed necessary to safeguard the rights of the plaintiffs, should be borne by all the defendants, jointly and severally, in the same manner that all of them should pay to the plaintiffs, jointly and severally, the attorney's fees awarded in the appealed judgment.

In consonance with the portion of this decision concerning the damages that the plaintiffs are entitled to recover from the defendants, the record of this case shall be remanded below for the corresponding proceedings.

MODIFIED AS ABOVE INDICATED, the appealed judgment is affirmed in all other respects. With costs.

Concepcion, C.J., Reyes, J.B.L., Regala, Makalintal, Bengzon, J.P., Zaldivar, Sanchez, and Castro, JJ., concur.

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