

CEBU CONTRACTORS CONSORTIUM CO., PETITIONER, VS. COURT OF APPEALS AND MAKATI LEASING & #038; FINANCE CORPORATION, RESPONDENTS.

G.R. No. 107199. July 22, 2003

Ponente: AZCUNA, J.

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AZCUNA, J.:

The instant Petition for Review on Certiorari stems from a complaint for collection of a sum of money with replevin[1] filed by respondent Makati Leasing and Finance Corporation (MLFC) against petitioner Cebu Contractors Consortium Company (CCCC) before the Regional Trial Court of Makati.[2]

MLFC alleges that on August 25, 1976 a lease agreement[3] relating to various equipment was entered into between MLFC, as lessor, and CCCC, as lessee. The terms and conditions of the lease were defined in said agreement and in two lease schedules of payment.[4] To secure the lease rentals, a chattel mortgage, and a subsequent amendment thereto, were executed in favor of MLFC over other various equipment owned by CCCC.[5]

On June 30, 1977, CCCC began defaulting on the lease rentals,[6] prompting MLFC to send demand letters.[7] When the demand letters were not heeded, MLFC filed a complaint for the payment of the rentals due and prayed that a writ of replevin be issued in order to obtain possession of the equipment leased and to foreclose on the equipment mortgaged.[8]

For its part, CCCC alleges[9] that it had a contract with the then Ministry of Public Highways[10] for the construction of the Iligan-Cagayan de Oro-Butuan Road. Being in need of additional capital, it approached MLFC for the purpose of securing a loan. MLFC agreed to extend financial assistance to CCCC but, instead of a customary loan covered by a security, MLFC induced CCCC to adopt and apply a sale and lease back scheme. The arrangement provided for the equipment of CCCC to be made to appear as sold to MLFC and then leased back to CCCC which will then pay lease rentals to MLFC. The rentals will be treated as installment payments to repurchase the equipment. It is CCCC's claim that the arrangement is nothing more than an equitable mortgage.

Pursuant to the sale and lease back scheme, CCCC executed two deeds of sale over its equipment in favor of MLFC, which were then leased back to CCCC.[11] To facilitate payment of the rentals, MLFC required CCCC to execute a deed of assignment of its collectibles from the Ministry of Public Highways.[12] In addition, CCCC was also required to execute a chattel mortgage over its other properties as a security.

CCCC's position is that it is no longer indebted to MLFC because the total amounts collected by the latter from the Ministry of Public Highways, by virtue of the deed of assignment, and from the proceeds of the foreclosed chattels were more than enough to cover CCCC's liabilities. Finally, CCCC submits that, in any event, the deed of assignment itself already freed CCCC from its obligation to MLFC.

The trial court rendered a decision[13] upholding the lease agreement and finding CCCC liable to MLFC for

P1,067,861.79 in lease rentals plus 25% attorney's fees and P486,442.28 in litigation expenses.[14] On appeal[15] by CCCC, the appellate court affirmed the trial court's decision but reduced the attorney's fees to 10% and totally eliminated the awarded litigation expenses.[16] CCCC is now before this Court seeking to reverse the decision of the Court of Appeals.[17]

CCCC presents the following assigned errors:

- WITH DUE RESPECT, THE RESPONDENT COURT ERRED IN UPHOLDING THE SO-CALLED SALE-LEASE BACK SCHEME OF THE PRIVATE RESPONDENT WHEN THE SAME IS IN REALITY NOTHING BUT AN EQUITABLE MORTGAGE.
- WITH DUE RESPECT, THE RESPONDENT COURT ERRED IN [NOT] HOLDING THAT THE DEED OF ASSIGNMENT EXECUTED BY PETITIONER IN FAVOR OF PRIVATE RESPONDENT FOR THE LATTER TO COLLECT FROM THE MINISTRY OF HIGHWAYS COMPLETELY FREED PETITIONER OF ITS OBLIGATION TO THE PRIVATE RESPONDENT.
- WITH DUE RESPECT, THE RESPONDENT COURT ERRED IN FINDING PETITIONER STILL LIABLE TO THE PRIVATE RESPONDENT DESPITE THE FACT THAT PETITIONER HAD ALREADY OVER-PAID SAID RESPONDENT.
- WITH DUE RESPECT, THE RESPONDENT COURT ERRED IN NOT GRANTING PETITIONER'S CLAIM FOR DAMAGES AGAINST THE PRIVATE RESPONDENT.

With respect to the first assigned error, this Court finds in favor of CCCC.

It is clear that the transaction between CCCC and MLFC is what is popularly known as a "financial leasing" or "financing lease." Transactions of this sort are not new to the commercial world and have been recognized as genuine or legitimate contracts, accorded with statutory and administrative recognition.[18]

In *Beltran v. PAIC Finance Corporation*,[19] this Court had occasion to discuss the nature of a financing lease:

A financing lease may be seen to be a contract *sui generis*, possessing some but not necessarily all the elements of an ordinary or civil law lease. Thus, legal title to the equipment leased is lodged in the financial lessor. The financial lessee is entitled to the possession and use of the leased equipment. At the same time, the financial lessee is obligated to make periodic payments denominated as lease rentals, which enable the financial lessor to recover the purchase price of the equipment which had been paid to the supplier thereof....

MLFC's own evidence discloses that it offers two types of financing lease: a direct lease and a sale-lease back. A direct lease is one where the client buys equipment through a financing company. MLFC would, in effect, initially purchase equipment that is needed by the client and then lease it to the latter. In a sale-lease back, the client already has the equipment but needs working capital. The client sells to MLFC equipment that it owns, which will be leased back to him. The transaction between CCCC and MLFC involved the second type of financing lease.[20]

CCCC argues that the sale and lease back scheme is nothing more than an equitable mortgage and, consequently, asks for its reformation.

Section 3 (d) of Republic Act No. 5980,[21] otherwise known as the "Financing Company Act", defines "Financial leasing" as:

"a mode of extending credit through a non-cancelable lease contract under which the lessor purchases or acquires, at the instance of the lessee, machinery, equipment, motor vehicles, appliances, business and office machines, and other movable or immovable property in consideration of the periodic payment by the lessee of a fixed amount of money sufficient to amortize at least seventy percent (70%) of the purchase price or

acquisition cost, including any incidental expenses and a margin of profit over an obligatory period of not less than two (2) years during which the lessee has the right to hold and use the leased property with the right to expense the lease rentals paid to the lessor and bears the cost of repairs, maintenance, insurance and preservation thereof, but with no obligation or option on his part to purchase the leased property from the owner-lessor at the end of the lease contract.”[22]

The above definition was originally found in Section 1 (i) of the Revised Rules and Regulations implementing the original Republic Act No. 5980. When Republic Act No. 8556 was enacted, amending Republic Act No. 5980, the definition was given a statutory nature.

In *Investors Finance Corporation v. Court of Appeals*,[23] the Court, applying the definition of financial leasing, differentiated between a true financial leasing and an ordinary loan with mortgage in the guise of a lease. It was explained that the definition contemplates the extension of credit to assist a buyer in acquiring movable property which he can use and eventually own. Thus, in a true "financial leasing," a finance company purchases on behalf of or at the instance of the lessee the equipment which the latter is interested to buy but has insufficient funds for the purpose. The finance company therefore leases the equipment to the lessee in consideration of the periodic payment by the lessee of a fixed amount of "rental." However, where the client already owns the equipment but needs additional working capital and the finance company purchases such equipment with the intention of leasing it back to him, the lease agreement is simulated to disguise the true transaction that is a loan with security. In that instance, it is clear that the intention of the parties was not to enable the client to acquire and use the equipment, but to extend to him a loan.

Going back to the case at bar, MLFC admits that the transaction with CCCC involved the purchase of already-owned equipment. Consequently, there can be no doubt that the transaction between the parties is not one of financial leasing, as defined by law, but simply a loan secured by a chattel mortgage over CCCC's equipment.

When the true intention of the parties to a contract is not expressed in the instrument purporting to embody their agreement by reason of mistake, fraud, inequitable conduct or accident, the remedy of the aggrieved party is to ask for reformation of the instrument under Articles 1359 and 1362 of the Civil Code, to the end that their true agreement may be expressed therein.[24] Under Article 1144 of the Civil Code, the prescriptive period for actions based upon a written contract and for reformation of an instrument is ten years.[25] The right of action for reformation accrued from the date of execution of the contract of lease in 1976.[26] This was properly exercised by CCCC when it filed its answer with counterclaim to MLFC's complaint in 1978 and asked for the reformation of the lease contract.[27]

Moving on to the second assigned error, CCCC claims that it had assigned to MLFC its collectibles from the Ministry of Public Highways, amounting to P2,469,142.50. The assignment was duly approved by the Ministry of Public Highways. Consequently, CCCC argues that MLFC should be barred from suing because the obligation had been transferred to and assumed by the Ministry of Public Highways.

This Court finds that the execution of the deed of assignment in favor of MLFC did not completely free CCCC from its obligations to MLFC under the lease agreement. On its face, the deed speaks of an assignment. However, in light of the circumstances obtaining at the time of the execution of said deed of assignment, this Court cannot regard the transaction as an absolute conveyance. In the interpretation of contracts, if the terms are clear and leave no doubt as to the intention of the contracting parties, the literal meaning of the stipulations shall control. But when the words appear contrary to the evident intention of the parties, the latter shall prevail over the former. In order to judge the intention of the parties, their contemporaneous and subsequent acts shall principally be considered.[28]

The deed of assignment was dated August 27, 1976. CCCC, by its own evidence,[29] was shown to have made partial payments on the obligation, apart from those obtained by MLFC from the Ministry of Public Highways. These partial payments were made after the execution of the deed of assignment. Since subsequent payments were made by CCCC itself, it follows that the execution of the deed of assignment did not extinguish its obligation.

In addition, the fact that a chattel mortgage was executed after the execution of the deed of assignment further confirms the existence of CCCC's obligation under the lease agreement. If indeed the deed of assignment extinguished the obligation, there was no reason to execute a chattel mortgage. Evidently, the only conceivable reason for the execution of a chattel mortgage was because the obligation under the lease agreement subsisted.

In *Citizens Surety and Insurance Co., Inc. v. Court of Appeals*,[30] this Court was faced with the same issue. Petitioner in that case, a surety company, issued two surety bonds in behalf of respondent therein to guaranty the fulfillment of an obligation under a contract of sale the latter had entered into with the Singer Sewing Machine Company. In consideration of the bonds, two indemnity agreements were executed by said respondent followed by a deed of assignment executed on the same date. After respondent's failure to comply with its obligation under the contract of sale, petitioner was compelled to pay under the surety bonds. When respondent failed to reimburse it, petitioner filed a collection suit. Respondent opposed the money claim, and asserted that the surety bonds and the indemnity agreements had been extinguished by the execution of the deed of assignment.

The Court held therein that the deed of assignment cannot be regarded as an absolute conveyance whereby the obligation under the surety bonds was automatically extinguished. Respondent's subsequent acts showed that the deed of assignment was intended merely as a security for the issuance of the two bonds. The Court found that partial payments were made after the execution of the deed of assignment to satisfy the obligation under the two surety bonds. Moreover, a second real estate mortgage in favor of petitioner was executed by respondent. These circumstances showed that no debt was extinguished upon the execution of the deed of assignment, which was intended merely as another security for the issuance of the surety bonds.

This Court now comes to the issue of overpayment. While the lease agreement is in reality an equitable mortgage, the records show that the equipment have already been sold by MLFC,[31] and that the proceeds from the sale were credited to CCCC's account.

The Court of Appeals ruled that CCCC is indebted to MLFC in the amount of P1,048,655.00 and disregarded CCCC's own computation showing an alleged overpayment. This Court agrees with this finding. CCCC's computation proved to be incomplete and unreliable. Noticeably absent from the computation are the penalties incurred by CCCC, when it defaulted on the lease rentals, which would have the effect of substantially increasing CCCC's debt.[32] Moreover, the Court of Appeal's computation is part of the findings of fact made by the appellate court. Such findings and conclusions should not be disturbed on appeal, in the absence of any showing that these are unfounded or arbitrarily arrived at or that the Court of Appeals had failed to consider an important evidence to the contrary.[33]

Finding that CCCC is still indebted to MLFC, the former's claim for damages must also fail.

WHEREFORE, the decision appealed from is hereby AFFIRMED. No costs.

SO ORDERED.

Davide, Jr., C.J., Vitug, Ynares-Santiago, and Carpio, JJ., concur.

[1] Civil Case No. 5450.

- [2] Branch 58.
- [3] Lease Agreement No. 211 (Exhibit A), Records, pp. 8-10.
- [4] Lease Schedules Nos. 797 and 931 (Exhibits A-1 and A-2), Records, pp. 10-16.
- [5] Chattel Mortgage and its Amendment (Exhibits B and C), Records pp. 17-19.
- [6] Statement of Account (Exhibit D), Records, p. 20.
- [7] Trial court decision, p. 2, Records, p. 777.
- [8] Complaint, Records, pp. 1-24.
- [9] Appellant's brief, Rollo, pp. 13-14.
- [10] Now the Department of Public Works and Highways.
- [11] Exhibits 1 and 2, Records, pp. 89-95.
- [12] Petition, p. 6; Rollo, p. 16.
- [13] Records, pp. 776-779.
- [14] Trial court decision, Records, p. 779.
- [15] The appeal was docketed as CA-G.R. No. 30000.
- [16] Court of Appeals decision, Rollo, p. 43.
- [17] Dated May 27, 1992.
- [18] BA Finance Corporation v. Court of Appeals, 228 SCRA 530 (1993).

[19] 209 SCRA 105 (1992).

- [20] TSN, Rolando Palma, December 3, 1984, p. 16.
- [21] As amended by Presidential Decree Nos. 1454 and 1793 and Republic Act 8556.
- [22] Italics supplied.

[23] 193 SCRA 701 (1991).

- [24] Ibid.
- [25] Ramos v. Court of Appeals, 180 SCRA 635 (1989).
- [26] Rosello-Bentir v. Leanda, 330 SCRA 591 (2000).
- [27] Records, pp. 75-88.
- [28] Sy v. Court of Appeals, 131 SCRA 116 (1984).
- [29] Exhibit 8, Records, p. 604.

[30] 162 SCRA 738 (1988).

[31] TSN, Amado Briones, February 1, 1985, p. 8.

[32] See Section 17 of the Lease Agreement on Default; Records, p. 9.

[33] Coconut Cooperative Marketing Association, Inc. v. Court of Appeals, 164 SCRA 568 (1988).

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