

## FIRST DIVISION

[ G.R. No. 169576, October 17, 2008 ]

**LEONIDES MERCADO, REPRESENTED BY HIS HEIRS: RACQUEL D. MERCADO, JIMMY D. MERCADO, HENRY D. MERCADO, LOURICAR D. MERCADO AND VIRGILIO D. MERCADO, PETITIONERS, VS. COURT OF APPEALS AND SAN MIGUEL CORPORATION, RESPONDENTS.**

### R E S O L U T I O N

**CORONA, J.:**

Leonides Mercado had been distributing respondent San Miguel Corporation's (SMC's) beer products in Quiapo, Manila since 1967. In 1991, SMC extended to him a P7.5 million credit line allowing him to withdraw goods on credit. To secure his purchases, Mercado assigned three China Banking Corporation (CBC) certificates of deposit amounting to P5 million<sup>[1]</sup> to SMC and executed a continuing hold-out agreement stating:

Any demand made by [SMC] on [CBC], claiming default on my/our part shall be conclusive on [CBC] and shall serve as absolute authority for [CBC] to encash the [CBC certificates of deposit] in accordance with the third paragraph of this Hold-Out Agreement, whether or not I/we have in fact defaulted on any of my/our obligations with [SMC], it being understood that the issue of whether or not there was factual default must be threshed out solely between me/us and [SMC]

He also submitted three surety bonds from Eastern Assurance and Surety Corporation (EASCO) totaling P2.6 million.<sup>[2]</sup>

On February 10, 1992, SMC notified CBC that Mercado failed to pay for the items he withdrew on credit. Consequently, citing the continuing hold-out agreement, it asked CBC to release the proceeds of the assigned certificates of deposit. CBC approved SMB's request and informed Mercado.

On March 2, 1992, Mercado filed an action to annul the continuing hold-out agreement and deed of assignment in the Regional Trial Court (RTC) of Manila, Branch 55.<sup>[3]</sup> He claimed that the continuing hold-out agreement allowed forfeiture without the benefit of foreclosure. It was therefore void pursuant to Article 2088 of the Civil Code.<sup>[4]</sup> Moreover, Mercado argued that he had already settled his recent purchases on credit but SMC erroneously applied the said payments to his old accounts not covered by the continuing hold-out agreement (*i.e.*, purchases made prior to the extension of the credit line).

On March 18, 1992, SMC filed its answer with counterclaim against Mercado. It contended that Mercado delivered only two CBC certificates of deposit amounting to

P4.5 million<sup>[5]</sup> and asserted that the execution of the continuing hold-out agreement and deed of assignment was a recognized business practice. Furthermore, because Mercado admitted his outstanding liabilities, SMC sought payment of the lees products he withdrew (or purchased on credit) worth P7,468,153.75.<sup>[6]</sup>

On April 23, 1992, SMC filed a third-party complaint against EASCO.<sup>[7]</sup> It sought to collect the proceeds of the surety bonds submitted by Mercado.

On September 14, 1994, Mercado filed an urgent manifestation and motion seeking the dismissal of the complaint. He claimed that he was no longer interested in annulling the continuing hold-out agreement and deed of assignment. The RTC, however, denied the motion.<sup>[8]</sup> Instead, it set the case for pre-trial. Thereafter, trial ensued.

During trial, Mercado acknowledged the accuracy of SMC's computation of his outstanding liability as of August 15, 1991. Thus, the RTC dismissed the complaint and ordered Mercado and EASCO (to the extent of P2.6 million or the value of its bonds) to jointly and severally pay SMC the amount of P7,468,153.75.<sup>[9]</sup>

Aggrieved, Mercado and EASCO appealed to the Court of Appeals (CA)<sup>[10]</sup> insisting that Mercado did not default in the payment of his obligations to SMC.

On December 14, 2004, the CA affirmed the RTC decision *in toto*.<sup>[11]</sup> Mercado and EASCO both moved for reconsideration but their respective motions were denied.<sup>[12]</sup>

On October 28, 2005, EASCO filed a petition for review on certiorari in this Court<sup>[13]</sup> but eventually agreed to settle its liability with SMC.<sup>[14]</sup> The petition was terminated on September 19, 2007.<sup>[15]</sup>

Meanwhile, Mercado passed away and was substituted by his heirs, petitioners Racquel D. Mercado, Jimmy D. Mercado, Henry D. Mercado, Louricar D. Mercado and Virgilio D. Mercado.

Petitioners subsequently filed this petition asserting that the CA erred in affirming the RTC decision *in toto*. The said decision (insofar as it ordered Mercado to pay SMC P7,468,153.75) was void. SMC's counterclaim was permissive in nature. Inasmuch as SMC did not pay docket fees, the RTC never acquired jurisdiction over the counterclaim.

We deny the petition.

A counterclaim (or a claim which a defending party may have against any party)<sup>[16]</sup> may be compulsory<sup>[17]</sup> or permissive. A counterclaim that (1) arises out of (or is necessarily connected with) the transaction or occurrence that is the subject matter of the opposing party's claim; (2) falls within the jurisdiction of the court and (3) does not require for its adjudication the presence of third parties over whom the court cannot acquire jurisdiction, is compulsory.<sup>[18]</sup> Otherwise, a counterclaim is merely permissive.