

FIRST DIVISION

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

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

D E C I S I O N

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:

- I. 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.
- II. 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.
- III. 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.
- IV. 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