

## FIRST DIVISION

[ G.R. No. 164791, June 29, 2010 ]

**SELWYN F. LAO AND EDGAR MANANSALA, PETITIONERS,  
SPECIAL PLANS, INC., RESPONDENT.**

### D E C I S I O N

**DEL CASTILLO, J.:**

In Roman Law, compensation was the reciprocal extinction of claims between mutual debtors. In the earlier stages of that system the practice did not exist as a matter of right but its application was discretionary with the *judex*. Later the praetor applied it by incorporating into the formula, which he prepared for the *judex*, an exception *doli*, that is, an authorization to take into account any circumstances which would render inequitable the enforcement of the claim. The effect was to cause a dismissal of the claim, however large, if a counterclaim, however small, was proven and the indirect result was to compel the actor (plaintiff) to deduct the counterclaim in advance.<sup>[1]</sup>

#### ***Factual Antecedents***

Petitioners Selwyn F. Lao (Lao) and Edgar Manansala (Manansala), together with Benjamin Jim (Jim), entered into a Contract of Lease<sup>[2]</sup> with respondent Special Plans, Inc. (SPI) for the period January 16, 1993 to January 15, 1995 over SPI's building at No. 354 Quezon Avenue, Quezon City. Petitioners intended to use the premises for their karaoke and restaurant business known as "Saporro Restaurant".

Upon expiration of the lease contract, it was renewed for a period of eight months at a rental rate of P23,000.00 per month.

On June 3, 1996, SPI sent a Demand Letter<sup>[3]</sup> to the petitioners asking for full payment of rentals in arrears.

Receiving no payment, SPI filed on July 23, 1996 a Complaint<sup>[4]</sup> for sum of money with the Metropolitan Trial Court (MeTC) of Quezon City, claiming that Jim and petitioners have accumulated unpaid rentals of P118,000.00 covering the period March 16, 1996 to August 16, 1996.

After service of summons, petitioners filed their Verified Answer<sup>[5]</sup> faulting SPI for making them believe that it owns the leased property. They likewise asserted that SPI did not deliver the leased premises in a condition fit for petitioners' intended use. Thus, petitioners claimed that they were constrained to incur expenses for necessary repairs as well as expenses for the repair of structural defects, which SPI failed and refused to reimburse. Petitioners prayed that the complaint be dismissed and judgment on their counterclaims be rendered ordering SPI to pay them the sum

of P422,920.40 as actual damages, as well as moral damages, attorney's fees and exemplary damages.

After the issues were joined, trial on the merits ensued. As culled from the MeTC Decision, the following account was presented by SPI:

Delfin Cruz, president of Special Plans, Inc. testified that on January 7, 1993, plaintiff-corporation and herein defendants entered into a two-year Contract of Lease (Exhibit "A" inclusive, with sub-markings) starting January 16, 1993 until January 15, 1995, involving a portion of said plaintiff-corporation's office building which used to be the Bahay Namin Food and Drinks at 354 Quezon Avenue, Quezon City. Defendants used the leased premises for their karaoke and restaurant business known as Saporro Restaurant. Upon [expiration of the lease], defendants, through defendant Lao requested in writing (Exhibit "B") for a renewal of the contract of lease, but plaintiff-corporation agreed only for an eight-month extension of [the] contract with all its terms and conditions on a month-to-month basis at a monthly rental of P23,000.00.

This witness further testified that while defendants paid the sum of P23,000.00 in August 1996 they nevertheless failed to pay the agreed rental since March 16, 1996, thus the accumulated unpaid rentals shot up to P118,000.00. Plaintiff-corporation demanded upon defendants payment therefor in a letter dated June 3, 1996 (Exhibit "D" inclusive with sub-markings).

On cross, Delfin Cruz admitted that plaintiff-corporation did not inform defendants that it was not the owner of the leased premises during the signing of the contract of lease and that said defendants did not inform him of the structural defects of the subject premises, including the repair works conducted thereon.

Antonio San Mateo, vice-president for legal affairs of plaintiff-corporation, averred that he made the demand to pay upon defendants for their failure to settle their agreed monthly rentals starting March 16, 1996 to August 15, 1996; and that for the period covering September 16, 1995 to October 15, 1995, defendants paid only P20,000.00, hence, the balance of P3,000.00 (Exhibit "E").<sup>[6]</sup>

In their defense, Jim and petitioners proffered the following:

Meanwhile, defendant Benjamin Jim testified that he was one of the signatories [to] the original contract of lease involving the subject premises whose facilities, including the roof, were already dilapidated: thus prompting the group to renovate the same. After a year of operation, Saporro lost so he decided to back out but defendant Lao convinced him to stay with the group for another x x x year. But the business lost even more so he finally called it quits with the consent of the group. He pulled out his audio-video equipment, refrigerator, and air-

conditioning unit on January 2, 1995, thirteen (13) days before the expiration of the contract of lease. He further denied having signed the request for the extension of the contract.

On cross, he stated that he did not sign documents for and in behalf of Saporro; and, that he allowed defendant Lao and Victor San Luis to sign for the group.

Testifying for defendant Jim, Atty. Maria Rosario Carmela Nova declared that defendant Jim sought her services on August 30, 1996 for the recovery of his money invested at Mount Fuji and Saporro but Atty. Cesa, who acted as counsel for defendants Lao and Manansala, refused to return the same in a letter-reply dated September 23, 1996 (Exhibit "1-Jim" inclusive with sub-markings).

Defendant Selwyn Lao testified that the group was not able to inspect the leased premises since Delfin Cruz had no key thereon during the signing of the contract of lease on January 7, 1993. He stated that paragraph 6 of the said contract provides that the LESSEE shall maintain the leased premises, including the parking lot, in good, clean and sanitary condition and shall make all necessary repairs thereon at his own expense except repairs of structural defects which shall be the responsibility of the LESSOR (Exhibit "1-Lao and Manansala"). When the group took possession of the leased premises on January 16, 1993, the equipment and furniture, among others, were found to be not in good condition. The trusses, roof and ceiling of the premises were already dilapidated. Rain seeped through the floor. When the group talked with Delfin Cruz about the condition of the leased property, the latter would just tell the former not to worry about it.

The group conducted structural and necessary repairs thereon, thus incurring the sum of P545,000.00 (Exhibit "2-Lao and Manansala" inclusive, with sub-markings), P125,000.00 of which was spent on structural defects, as follows:

|                 |   |                             |
|-----------------|---|-----------------------------|
| Roofing repair  | - | P 45,000.00 (Exhibit "2-A") |
| Ceiling repair  | - | 50,000.00 (Exhibit "2-B")   |
| Flooring repair | - | 20,000.00 (Exhibit "2-C")   |
| Waterproofing   | - | 10,000.00 (Exhibit "2-D")   |

Defendant Lao further testified that Delfin Cruz told him to proceed with the repair work without informing him (Lao) that plaintiff-corporation was not the owner of the leased premises. The witness added that the group paid the sum of P23,000.00 on July 21, 1996 for the period March 16, 1996 to April 15, 1996.

On cross, he averred that he sought the expertise of Gregorio Tamayo to repair the premises for P545,000.00; and that he had a verbal authority to sign for and in behalf of defendant Jim who took his audio-video equipment on January 2, 1996.

Presented at the witness stand to testify for defendant Lao and

Manansala, Gregorio Tamayo admitted that defendant Lao sought his services to undertake both structural and finishing works on the subject property at a cost of P545,00.00.

On cross, he declared that he was the subcontractor of defendant Lao.<sup>[7]</sup>

### ***Ruling of the Metropolitan Trial Court***

On December 15, 1999, the MeTC rendered its Decision<sup>[8]</sup> finding that the unpaid rentals stood at only P95,000.00. It also found that SPI is solely responsible for repairing the structural defects of the leased premises, for which the petitioners spent P125,000.00. It held that even assuming that petitioners did not notify SPI about the structural defects and the urgency to repair the same, Article 1663 of the Civil Code allows the lessee to make urgent repairs in order to avoid an imminent danger at the lessor's cost. Hence, the MeTC dismissed the complaint for lack of cause of action. The dispositive portion of the Decision reads:

Wherefore, in view of the foregoing considerations, let this case be, as it is, hereby ordered DISMISSED for lack of cause of action. No costs.

The counterclaim and cross-claim of the defendants are likewise DENIED for lack of merit.

SO ORDERED.<sup>[9]</sup>

### ***Ruling of the Regional Trial Court***

Aggrieved, SPI filed an appeal before the RTC of Quezon City. Both parties filed their respective memoranda.<sup>[10]</sup> However, on November 24, 2000, counsel for SPI filed his Withdrawal of Appearance<sup>[11]</sup> with the conformity of SPI, through its Vice President Antonio L. San Mateo.<sup>[12]</sup> In an Order<sup>[13]</sup> dated January 5, 2001, the RTC granted the Withdrawal of Appearance and ordered that all notices, orders and other court processes in the case be forwarded to SPI at its address at 354 Quezon Avenue, Quezon City.

On March 12, 2001, the RTC rendered a Decision<sup>[14]</sup> affirming with modification the MeTC Decision by ordering petitioners to pay SPI the amount of P95,000.00 for unpaid rentals.<sup>[15]</sup> The RTC disagreed with the MeTC on the aspect of off-setting the amount allegedly spent by petitioners for the repairs of the structural defects of subject property with their unpaid rentals. The dispositive portion of the RTC Decision reads:

FROM THE GOING MILLIEU, premises considered, the lower court's (Branch 38) decision dated December 15, 1999 is modified to the effect that Defendants Selwyn Lao and Edgar Manansala are ordered to pay to the plaintiff-corporation the amount of Ninety Five Thousand (P95,000.00) pesos for unpaid rentals. With respect to the other aspect

of the decision, there being no cogent reason to disturb the lower court's ruling, the same stands.

SO ORDERED.<sup>[16]</sup>

### **Ruling of the Court of Appeals**

On April 25, 2003, petitioners Lao and Manansala filed a Petition for Review with the CA.<sup>[17]</sup> Jim did not join them. Hence, the appealed Decision of the RTC had become final insofar as Jim is concerned.

On June 30, 2003, the CA rendered a Decision<sup>[18]</sup> affirming *in toto* the RTC Decision. Petitioners moved for reconsideration, but it was denied in a Resolution<sup>[19]</sup> dated August 9, 2004.

### **Issues**

Petitioners do not take issue that the unpaid rentals amount to P95,000.00.<sup>[20]</sup>

Nonetheless, they assert that the amount of P545,000.00 they spent for repairs, P125,000.00 of which was spent on structural repairs, should be judicially compensated against the said unpaid rentals amounting to P95,000.00.<sup>[21]</sup> On the other hand, SPI avers that petitioners have not shown proof that they spent these amounts.<sup>[22]</sup>

### **Our Ruling**

The petition is without merit.

The Civil Code provides that compensation shall take place when two persons, in their own right, are creditors and debtors of each other.<sup>[23]</sup> In order for compensation to be proper, it is necessary that:

1. Each one of the obligors be bound principally and that he be at the same time a principal creditor of the other;
2. Both debts consist in a sum of money, or if the things due are consumable, they be of the same kind, and also of the same quality if the latter has been stated;
3. The two debts are due;
4. The **debts are liquidated and demandable**;
5. Over neither of them be any retention or controversy, commenced by third parties and communicated in due time to the debtor. <sup>[24]</sup>

Petitioners failed to properly discharge their burden to show that the debts are