

THIRD DIVISION

[G.R. No. 180439, December 23, 2009]

**RESORT HOTELS CORPORATION, RODOLFO M. CUENCA AND
CUENCA INVESTMENT CORPORATION, PETITIONERS, VS.
DEVELOPMENT BANK OF THE PHILIPPINES AND SM
INVESTMENT CORPORATION, RESPONDENTS.**

D E C I S I O N

NACHURA, J.:

Before us is a petition for review on *certiorari* under Rule 45 of the Rules of Court, assailing the Court of Appeals (CA) Decision^[1] in CA-G.R. CV No. 81363, which reversed and set aside the Decision of the Regional Trial Court (RTC), Branch 134, Makati City, in Civil Case Nos. 6342, 269-R, TG-799 and 9497.^[2]

The long and arduous facts, as found by the CA, follow:

[Petitioner] Resort Hotel[s] Corporation (RHC for brevity), a corporation duly organized and existing in accordance with Philippine laws, was the previous owner and operator of several hotels located outside Metro Manila; namely Baguio Pines Hotel in Baguio City, Taal Vista Lodge Hotel in Tagaytay City, and Hotel Mindanao in Cagayan de Oro City. Among RHC's stockholders were [petitioners] Cuenca Investment Corporation and Rodolfo Cuenca, who was the erstwhile President and Chairman of the Board of Directors of the said Corporation. On the other hand, [respondent] Development Bank of the Philippines (DBP), a government financial institution, was RHC's major creditor that eventually foreclosed the disputed hotels upon the latter's default. [Respondent] SM Investment Corporation (SMIC) was the subsequent owner of Taal Vista Lodge Hotel and Baguio Pines Hotel.

It appears that from 1969 up to 1981, RHC obtained from DBP several loans, aggregating approximately P157 million, for the purpose of expanding hotel capacities, operations and services nationwide. To secure the payment of these loans, RHC executed real estate mortgages in favor of DBP covering the following properties of RHC: a) two (2) parcels of land situated in Baguio City, covered by Transfer Certificate of Title (TCT) No. T-15880 and Original Certificate of Title No. P-1316, which included Baguio Pines Hotel x x x; b) six (6) parcels of land located in Tagaytay City, covered by TCT Nos. T-8085, T-10801, T-10802, T-10803, T-10804 and T-10805, which included Taal Vista Lodge Hotel x x x; and c) two (2) parcels of land situated in Cagayan de Oro, covered by TCT Nos. T-34777 and T-34778, which included Hotel Mindanao x x x. Likewise, RHC executed chattel mortgages additionally securing the loans with all the

personal properties located inside its head office in Makati.

When the loans became due and demandable, RHC failed to pay. Sometime in the early '80S, RHC proposed to DBP that part of its obligations be converted into equity inasmuch as it was experiencing financial difficulties. DBP subsequently acceded. With the approval of the Board of Directors of RHC, which was then headed by its Chairman, Rodolfo Cuenca, DBP obtained shareholdings, equivalent to 55% of RHC's total stockholders' equity, in exchange for the reduction of RHC's obligation to DBP by [as] much as P47 million. As a result of the debt-to-equity conversion, DBP acquired two (2) board seats in the eleven-member Board of Directors of RHC.

As of January 10, 1984, RHC's outstanding obligation was pegged at P114,005,404.02 while its total arrearages was P56,134,819.52 which was about 49% of its total outstanding obligation. Consequently, DBP applied for the extrajudicial foreclosure of the real estate and chattel mortgages pursuant to Presidential Decree No. 385, also known as "*The Law on Mandatory Foreclosure*," mandating government financial institutions to foreclose mandatorily loans with arrearages amounting to at least 20% of the total outstanding obligation.

Intending to block the impending foreclosure of the mortgaged personal properties, RHC filed on February 6, 1984 a Complaint x x x against DBP and the Sheriff of Rizal or Makati before Branch 148 of Regional Trial Court (RTC) of Makati, docketed therein as Civil Case No. 6342. With respect to the mortgaged real properties, RHC filed similar Complaints before Branch 7 of RTC of Baguio City x x x, Branch 18 of RTC of Tagaytay City x x x, and Branch 18 of RTC of Misamis Oriental

x x x, docketed as therein Civil Case Nos. 269-R, TG-799 and 9497, respectively. In Civil Case Nos. 6342 and 269-R, RHC specifically prayed for the issuance of restraining orders or preliminary injunctive writs to stop or enjoin the Sheriffs from conducting foreclosure proceedings.

By the Orders dated March 6, 1984 and March 21, 1984, the applications for restraining orders or preliminary injunctive writ were denied by the RTC of Makati x x x and Baguio City, respectively. Unsatisfied therewith, RHC filed separate petitions for certiorari, docketed as AC-G.R. Nos. SP-02939 and SP-03103 assailing the Orders of the lower courts with the then Intermediate Appellate Court. On both occasions, the then Intermediate Appellate Court sustained the Orders of denial of the two (2) lower court x x x.

As there were no restraining orders or injunctive writs whatsoever issued by the lower courts, the foreclosure sale of the mortgaged properties went through as scheduled. The auction sale of the mortgaged chattels was conducted on May 28, 1984 by the Sheriff of Makati. As regards the mortgaged real properties, the auction sale of those located in Cagayan de Oro was conducted on February 27, 1984 by the Office of the Provincial Sheriff of Misamis Oriental, while the auction sale of those located in Baguio City was held on March 22, 1984 by the Office of the

City and Provincial Sheriff of Baguio City. With respect to those located in Tagaytay City, the auction sale was conducted on June 11, 1984 by the Office of the Provincial Sheriff.

In all the foreclosure sales, DBP emerged and was declared the highest and winning bidder. With regard to the foreclosed chattels, DBP posted a bid price of P117,500.00 x x x. With regard to the foreclosed real properties, DBP bought the Cagayan de Oro properties for P7,440,565.00, the Baguio City properties for P32,158,515.00, and the Tagaytay City properties for P26,450,560.00. Subsequently, three (3) Certificates of Sale were issued to evidence sale of the mortgaged real properties to DBP x x x.

Meanwhile, on October 23, 1984, Baguio Pines Hotel was gutted by fire. A total sum of about P64,566,000.00 representing fire insurance proceeds was collected by DBP and applied to the obligation of RHC x x x. Thereafter, the one-year statutory period of redemption expired without RHC exercising the right of redemption. Consequently, title[s] to the foreclosed properties were consolidated in the name of DBP.

By Resolution dated April 16, 1985 issued by the Supreme Court *en banc*, Civil Case Nos. 269-R, 9497 and TG-799 were consolidated with Civil Case No. 6342 which was then pending before Branch 148 of the RTC of Makati. Later on, the four (4) consolidated cases were transferred to Branch 134 of the same court.

On April 23, 1985, RHC filed the first Amended and Supplemental Complaint x x x pleading new and additional causes of action and enabling Rodolfo Cuenca to join the suit as co-plaintiff.

On May 26, 1988, DBP sold the Baguio City properties to SMIC x x x. Likewise on July 11, 1988, DBP sold the Tagaytay City properties, which included the Taal Vista Lodge Hotel, to Tagaytay and Taal Management Corporation (TTMC) x x x, which in turn sold the same to SMIC for P38,000,000.00 x x x.

On June 23, 1992, RHC and Rodolfo Cuenca filed their Second Amended and Supplemental Complaint x x x enabling Rodolfo Cuenca and CIC to prosecute the action as a derivative stockholder's suit in behalf of RHC. On April 7, 1995, RHC, Rodolfo Cuenca and CIC x x x filed their Third Amended and Supplemental Complaint x x x impleading additional defendants; namely, SMIC in Civil Case No. 269-R, TTMC in Civil Case No. TG-799.

On February 5, 1996, [petitioners] filed their Fourth Amended Complaint x x x asserting nine (9) causes of action against DBP, SMIC and the Sheriffs responsible for the foreclosure proceedings, with TTMC being dropped as defendant. In their first cause of action, which was to declare the obligation extinguished, they alleged, *inter alia*, that DBP had no right to foreclose the mortgages since RHC's obligation to DBP had been extinguished by confusion or merger which occurred when shareholdings in RHC were acquired by DBP in accordance with debt-to-equity

conversion agreement. In their second cause of action, which was to restructure the obligation, they asserted, *inter alia*, that assuming RHC's obligation to DBP had not been extinguished, RHC was entitled to loan restructuring at the very least. In their third cause of action, which was to ascertain and fix the amount of obligation, they insisted that DBP had no right to foreclose the mortgages as the amount of the outstanding obligation had not yet been liquidated or ascertained. In their fourth cause of action, which was to annul the mortgages, the plaintiffs-appellees claimed that DBP had no right to foreclose the mortgages considering that DBP was in fact and in effect lending to itself to accompany and carry into effect the Government's purpose and policy, and that some of the mortgages sought to be foreclosed` were not registered. In their fifth cause of action, which was to annul the foreclosure sales, they insisted, *inter alia*, that the required posting and publication of notices of extrajudicial foreclosures had not been complied with, and there was gross inadequacy in the purchase prices of the foreclosed properties. In their sixth cause of action, which was to declare the Baguio Pines Hotel effectively redeemed and the amount of refund due, they alleged that DBP acquired Baguio Pines Hotel at the foreclosure sale for P32,158,515.00. While Baguio Pines Hotel was in the possession of DBP, it was destroyed by fire. However, DBP collected the insurance proceeds despite the fact that they were more than the amount of the purchase price. In their seventh cause of action, they alleged that in the event that judgment was not rendered declaring the Baguio Pines Hotel redeemed, RHC's total obligation to DBP should be declared to be fully satisfied and DBP should be ordered to refund the difference between the insurance proceeds and the correct outstanding obligation of RHC to DBP. In their eighth cause of action, which was to declare Rodolfo Cuenca released or discharged from his joint and several undertaking, they asseverated, *inter alia*, that any joint and several undertaking of Rodolfo Cuenca to answer for the obligation of RHC to DBP should be reformed on the ground of mistake, fraud, inequitable conduct or accident since it was merely a formality to ensure the payment of RHC's obligations. Finally, in their ninth cause of action, the plaintiffs-appellees alleged that they were entitled to exemplary damages and attorney's fees.

In its Answer thereto, DBP maintained that the [petitioners] had no cause of action considering that: a) there was no confusion or merger because the equity of the original stockholders was unimpaired, and control of the said corporation remained with the original stockholders; b) restructuring was not a matter of right for one party, but could arise only from the mutual agreement of the parties, restructuring in effect a novation of the loan contract; c) the obligations of RHC had been properly computed, and the computation already took into account the debt-to-equity conversion; d) DBP was an entity distinct and separate from RHC, and therefore, could not have possibly lent to itself; e) non-registration of mortgages did not render them invalid as between the parties; f) all requirements of the law regarding foreclosure were complied with; g) the insurance proceeds collected by DBP were credited to the account of RHC, but the said proceeds were still insufficient to discharge the obligation; h) the proceeds from the foreclosure sales did not even amount to one-half of the total obligations of RHC; i) Rodolfo

Cuenca's undertaking to be bound jointly and severally liable with RHC was not a mere formality but a contract defining his obligation in case RHC failed to pay; j) there was no legal ground to discharge Rodolfo Cuenca from his obligation; and k) DBP was not liable for any damages since it was RHC, Rodolfo Cuenca and CIC that had acted in bad faith x x x.

For its part, SMIC filed its Answer to Fourth Amended Complaint x x x averring that a) RHC, Rodolfo Cuenca and CIC had no cause of action against it; b) the RTC had no jurisdiction over the nature of the action or suit, it involving an intra-corporate; and c) it was a buyer in good faith in connection with its acquisition of Taal Vista Lodge Hotel and Baguio Pines Hotel.

On March 27, 1998, RHC, [CIC and Cuenca] filed their Fifth Amended Complaint x x x deleting the ninth cause of action praying for the payment of exemplary damages and attorney's fees. On February 15, 2000, they made a Manifestation x x x that they were withdrawing their Fifth Amended Complaint. With the withdrawal of the said Complaint, the RTC conducted the pre-trial of the consolidated cases on the basis of the Fourth Amended and Supplemental Complaint x x x.

On March 13, 2000, [petitioners] filed a Motion to Drop as Defendants x x x on the ground that the Sheriffs of Rizal or Makati, Baguio City, Cavite and Misamis Oriental were not indispensable to resolution of the consolidated cases. There being no objection interposed by DBP and SMIC, the RTC, in its Order dated May 17, 2000 x x x dropped the said Sheriffs as defendants in the consolidated cases.

Thereafter, trial of the consolidated cases ensued.

During the hearing, [petitioners] presented as witnesses Bayani Santos, the Senior Manager of DBP, Roberto Cuenca and his father, Rodolfo Cuenca. Their testimonies were aptly summarized by the RTC, thus:

Bayani Santos, senior manager of defendant DBP testified that he has been employed therein since November 14, 1974. His functions include the handling of special accounts or non-performing accounts of the bank. He said that he brought with him notices of foreclosure for the Hotel Mindanao on February 27, 1984[,] for the Pines Hotel on March 22, 1984 and for Taal Vista Lodge on June 11, 1984. When asked about proofs of posting and publication, witness Santos showed a Xerox copy of affidavit of publication for the extrajudicial sale of Tagaytay property. Witness Santos likewise presented letters dated March 2 and May 23, 1984 addressed to plaintiff RHC about the auction sale of the Tagaytay and Baguio properties on March 22, 27 and June 11, 1984. He explained that there were two (2) dates set for auction of the Baguio properties because the first date was postponed. About the total loan obligation of plaintiff RHC, witness Santos merely pointed to