

SECOND DIVISION

[G.R. No. 141316, November 20, 2003]

**CLARA REYES PASTOR AND OTHER STOCKHOLDERS OF C & C
COMMERCIAL CORPORATION AND C & C COMMERCIAL CORPORATION,
PETITIONERS, VS. PHILIPPINE NATIONAL BANK AND NATIONAL
INVESTMENT & DEVELOPMENT CORPORATION, RESPONDENTS.**

DECISION

TINGA, J.:

This is the third time that a controversy arising from Civil Case No. RQ-18176 has reached this Court. The first was *C & C Commercial Corporation, et. al. v. Philippine National Bank, et. al.*, docketed as G.R. No. 42449, ^[1] while the second was *Philippine National Bank and National Investment Development Corporation v. Court of Appeals, et.al.*, docketed as G.R. No. 108870. ^[2] Both cases form part of the factual backdrop of the present petition which is summarized below.

On various dates between the period February 27, 1957 and December 20, 1960, petitioner C&C Commercial Corporation^[3] (hereafter, C & C) opened seven (7) letters of credit with the respondent Philippine National Bank (hereafter, PNB) to import machines and equipment for its plants. Since C & C's obligations under the letters of credit totaling P5,451,851.83 as of January 31, 1968 were not paid, PNB instituted on March 13, 1968 a case for collection with a prayer for preliminary attachment before the then Court of First Instance of Manila against C & C, impleading petitioner Clara Pastor, the controlling stockholder of C & C, as joint and solidary debtor.^[4]

However, instead of proceeding with the collection case, the PNB and its subsidiary, the National Investment Development Corporation (hereafter, NIDC) as *Trustees*, and Clara Pastor as *Trustor*, entered into a *Voting Trust Agreement*^[5] (hereafter, VTA) dated March 5, 1969. The VTA gave PNB and NIDC full authority "to manage the affairs and the accounts and properties of the C & C Commercial Corporation, Inc.; to choose its directors and key officers; to safeguard its interest and those of its creditors; and, in general, to exercise all such powers and discharge such functions as inherently pertain to the ownership and/or management of the corporation"^[6] for a period of five (5) years, renewable for another five (5) years in case an unpaid balance remains at the end of the original period.^[7] Also included in the VTA was an immunity clause in favor of PNB and NIDC.^[8]

The PNB and NIDC immediately took over the management of C & C pursuant to the agreement. On September 6, 1971, C & C executed a chattel mortgage over its personal properties in favor of NIDC as a security for the loan of Seven Hundred Thousand Pesos (P700,000.00) intended to finance the production of asbestos cement products and their exportation to Brunei and to repair/rehabilitate its plant building which had been damaged by typhoon "Yoling."^[9]

Meanwhile, the accounting firm of Sycip, Gorres and Velayo (hereafter, SGV) examined the management and operations of C & C for the first three (3) years under the Voting Trust Agreement. On August 27, 1973, SGV submitted a report^[10] finding that the C & C was in a

serious financial position. The SGV made the following observations relative to the company's financial difficulty:

- Even in 1969, it would appear that the Company had required inflow of funds to support its operations since at that time it had already incurred a 3.4 million capital deficiency. This figure eventually reached P11.5 million by 1972. Exhibit IX shows an analysis of capital deficiency from 1969 to 1972.
- Total assets decreased by 15% from P5.1 million in 1969 to P4.3 million in 1972 mainly due to decreases in current assets amounting to P6 million; although additional investments were made in fixed assets, depreciation more than offset this resulting in a P2 million decrease in the net book values of fixed assets.
- Total current liabilities increased by P6.3 million in 1972 due mainly to the increase in accounts payable amounting to P1.1 million and new liabilities due to banks of P5.2 million which include interests accrued as follows:

Additional Liabilities Due to Banks Incurred in 1970-1972

| | PNB | NIDC | DBP | Total |
|----------------------------|-------|-------|-------|-------|
| Principal | P1.3M | P1.0M | | P2.3M |
| Interest and other charges | 1.6 | .1 | P1.2M | 2.9 |
| | <hr/> | <hr/> | <hr/> | <hr/> |
| Total | P2.9M | P1.1M | P1.2M | P5.2M |
| | ===== | ===== | ===== | ===== |

- Collections from sales generated from 1969 to 1972 have gone into operations resulting in the non-movement on the Company's liabilities to banks. As a result, interest expense amounted to P.7 million in 1972 compared to P.07 million in 1969. Accrued interest alone increased by 113% from P2.4 million in 1969 to P5.1 million in 1972. (Please refer to Exhibit X for the Funds Flow Analysis for the three (3) years ended December 31, 1972.)

The level of sales that the Company achieved in 1972 after three years of operation accounted only for about 5% utilization of plant capacity. This is traceable to the fact that operations are off and on due not only to lack of raw materials but also to natural calamities like floods and typhoons which have affected sales and operations.

Over the three-year period 1970-1972, the Company generated funds of about P6.3 million from bank loans and other current liabilities. Of this, P2.9 million represented interest. Assuming the 1969 base figures are correct and that no major investment in fixed assets remain unrecorded (as the Company keeps no fixed asset records), the balance could be attributed to cash operating losses, averaging P1.13 million per year. Using 1972 figures which reflect a cash operating deficit of P1.41 million, this conclusion appears to be reasonable.

Reacting to the foregoing report, the petitioners filed on October 16, 1973 before the then Court of First Instance of Rizal, Quezon City Branch, a *Complaint*^[11] for Termination of Voting Trust Agreement, Accounting, and Damages With Injunction and Receivership. The *Complaint* recited the following alleged causes of action: (1) breach of VTA by mismanagement, negligent management, and/or incompetence; (2) failure to render accounting of management, submit annual financial statements and follow generally accepted accounting procedures; (3) compensatory damages for losses and unrealized profits, and; (4) litigation expenses and attorney's fees.

In their *Answer*,^[12] PNB and NIDC denied the charge of mismanagement and argued that: (1) their competence to manage the corporation could not be questioned as they stood to benefit from normalization of operations; (2) the plaintiffs were not entitled to accounting as the VTA had not yet been terminated but they nevertheless submitted annual financial statements to the plaintiffs and religiously followed accepted accounting procedures in recording transactions; (3) the plaintiffs' claim for damages had no basis; and, (4) the damages suffered by the plaintiffs were due to their own making. They further alleged that C & C's indebtedness to PNB had reached the amount of P11,538,029.63 as of August 31, 1973, excluding daily interest, and to NIDC, P1,219,982.00 as of April 15, 1973, excluding daily interest.

On January 22, 1974, the lower court issued an *Order* ^[13] granting C & C's application for receivership, appointing Bayani Barzaga as receiver. This one-man receivership was subsequently converted into a joint receivership composed of three (3) members, pursuant to an agreement reached between C & C, PNB and NIDC to provide a mutually acceptable mechanism for the management of C & C pending the settlement negotiations between them.
^[14]

In the meantime, during the pendency of the case or on December 19, 1973, the Development Bank of the Philippines (DBP) executed a *Deed of Assignment*^[15] in favor of PNB, assigning to the latter Promissory Notes ^[16] and Real Estate Mortgage^[17] executed by C & C on May 16, 1960 and May 8, 1961, in the principal amounts of P490,000.00 and P796,000.00, respectively.

On March 11, 1974, PNB filed a *Petition for Sale Under Act 3135 as Amended*^[18] before the Provincial Sheriff of Pasig to foreclose the land covered by OCT No. 2224 together with the improvements, buildings, machinery and equipment thereon, on account of the assigned loans of C & C from DBP. The PNB pegged the total amount of the loans at P2,693,325.18 as of January 18, 1974. It also included the amount of P11,878,411.69 on the account of seven Letters of Credit plaintiffs had opened with it, computed as of January 31, 1974, which brought the total mortgage debt to P14, 571,736. 87.

On September 22, 1975, C & C filed a *Complaint* ^[19] docketed as Civil Case No. 22047, for nullification of the extrajudicial foreclosure proceedings with prayer for a writ of injunction against PNB and the Provincial Sheriff of Rizal, contesting PNB's foreclosure of the mortgage and the scheduled auction sale. On September 30, 1975, an *Order* ^[20] was issued by the then Court of First Instance (CFI) of Pasig ordering the maintenance of the *status quo* and restraining the scheduled foreclosure sale.

On the other hand, NIDC filed on September 25, 1975, a *Petition* ^[21] for the auction sale of the chattels covered by a *Deed of Chattel Mortgage*, this time with the Sheriff of the City of Manila. This was pursued on the basis of the P700,000.00 loan under the loan agreement dated September 10, 1971, the balance of which stood at P658, 493.15, inclusive of 10% attorney's fees, as of August 31, 1975. Since the chattel mortgage deed contains an all-embracing mortgage clause,^[22] NIDC also sought to collect through the foreclosure sale other accounts which as of August 31, 1975 amounted as follows: (1) accounts receivables pegged at P1,159,272.80; (2) additional advances of P23,943.63; and, (3) guaranty accommodation charges of P3,399.64, leading to a total of P1,845,109.22.

Subsequently, or on October 3, 1975, petitioners filed before the then CFI of Pasig another *Complaint*^[23] for Nullification of the Extrajudicial Foreclosure Proceedings against NIDC. The Complaint was docketed as Civil Case No. 22133. The court issued a similar *Order* dated October 15, 1975, restraining the scheduled sale and directing the maintenance of the *status quo*.

On September 17, 1975, on separate *Motions to Dismiss* filed by PNB and NIDC as defendants in Civil Case Nos. 22047 and 22133, respectively, the CFI of Pasig dismissed both cases in separate decisions for violation of the rule against splitting cause of action and for lack of capacity of C & C to sue, it being under receivership.

On January 5, 1976, the petitioners moved for leave to file a *Supplemental Complaint*, [24] with an application for the issuance of a writ of preliminary injunction to restrain the threatened foreclosure sale of their properties.

In an *Order* [25] dated January 15, 1976, the lower court admitted the *Supplemental Complaint* but denied the application for injunction on account of Presidential Decree No. 385 which prohibited the issuance of restraining orders or injunctions against government financial institutions in any foreclosure action taken by such institutions, in compliance with the mandatory foreclosure provided in said Decree.[26]

Undaunted, the petitioners filed before this Court a *Petition for Certiorari* docketed as G.R. No. 42449,[27] contesting the denial of their application for injunction. In its decision of July 5, 1989, the Court granted the petition, ruling that petition for the foreclosure sale was "materially defective in that it included in the amount of the total indebtedness to be satisfied by the sale previously incurred unsecured obligations." The decision was "without prejudice however to the right of PNB to petition for an extrajudicial foreclosure sale to satisfy the obligations specifically secured by the DBP- assigned mortgage," so the Court stated.

Accordingly, on January 25, 1990, the defendant PNB once more instituted extrajudicial foreclosure proceedings against the petitioners before the Pasig Sheriff, this time for the reduced mortgage debt of P7,789,193.20, including interest, penalty charges and attorney's fees. On February 15, 1990, petitioners filed a *Motion for Issuance of Injunction*, [28] arguing that the mortgage debt of P7,789,193. 20 stated in the *Notice of Foreclosure* was beyond the amount of P1,286,000.00 approved for foreclosure by the Supreme Court as a secured obligation.

On February 19, 1990, the trial court issued an *Order* [29] temporarily restraining the foreclosure sale to make way for the reception of evidence on the disputed amount of the mortgage debt. Subsequently, on March 9, 1990, it ordered the issuance, upon the filing of an injunction bond, of a writ of preliminary injunction enjoining PNB and the Pasig Sheriff from foreclosing the petitioner's properties. In the same *Order*, the trial court directed PNB to seek clarification from this Court whether the obligation approved for satisfaction through the foreclosure sale shall include interest and other charges. The record reveals that no such clarification was sought from this Court.

Trial on the merits ensued. Finally, on January 20, 1992, the lower court rendered its *Decision*[30] finding PNB & NIDC responsible for the serious financial difficulties of C & C, allegedly on account of their mismanagement, characterized by extravagance, dishonesty, bad faith and incompetence. The trial court drew this conclusion from the massive operational losses, capital deficiency and reduction of corporate assets suffered by C & C during the PNB and NIDC's management under the VTA, as presented in the SGV report. It likewise considered the testimony of Pastor specifying acts of dishonesty and recklessness as follows: "payroll padding to accommodate ghost workers; . . . theft of spare parts which were later sold to NIDC Managers of (C & C); . . . no board meetings in 1972 and 1973; . . . no infusion of capital by PNB and NIDC in 1972 and 1973; . . . no audited financial statements to record ACPPI operations for the years 1970, 1971, and 1972; purchase of raw materials and supplies for maintenance of the machinery and equipment were slow and niggardly; . . . misdelivery of pipes purchased by customers, heavy automatic losses to (C & C); and the supposed samples of asbestos sheets worth of P30,000.00 were actually appropriated for the personal use of PNB Vice President."

The trial court concluded that since PNB and NIDC violated the trust as ordained in the VTA, rescission of the VTA is proper. Corollarilly, it granted damages and attorney's fees in favor of C & C in the total amount of P21,485,848.00. It likewise ruled that aside from the DBP-assigned secured obligation of C & C, all the unsecured obligations of C & C to PNB and NIDC were not sufficiently established. The dispositive portion of the RTC decision reads:

ACCORDINGLY, judgment is hereby rendered as follows:

1. Rescinding the Voting Trust Agreement executed on March 5, 1969, by plaintiff Clara Reyes Pastor, a majority stockholder of C & C Commercial Corporation, as Trustor, in favor of the defendants, Philippine National Bank and National Investment Development Corporation, as Trustees;
2. Declaring that the secured loan of P490,000.00 and P796,000.00 of the plaintiffs from the Development Bank of the Philippines (DBP), under the promissory notes dated May 16, 1960 and May 8, 1961, secured by real estate mortgages on the same dates, executed by plaintiffs C & C Commercial Corporation and plaintiff Clara Reyes Pastor for herself and as attorney-in-fact of her husband, Antonio Pastor, in favor of DBP, which were assigned by the DBP to defendant PNB are already considered fully paid by the plaintiffs by reason of set off/compensation with the damages and attorney's fees awarded to plaintiffs in this judgment, and, the secured loans are, therefore, no longer payable to defendant PNB from the plaintiffs;
3. Canceling thereby the aforesaid real estate mortgages covering the mortgaged twenty (20) parcels of land described therein, together with all the buildings and other improvements existing or which may hereafter be created or constructed thereon, situated at Barrio Napindan, Municipality of Taguig, Province of Rizal (now of Metro Manila), under Original Certificate of Title No. 2224 of the Registry of Deeds of the Province of Rizal (now of Pasig, Metro Manila);
4. Making permanent the writ of preliminary injunction issued on March 23, 1990;
5. Ordering, as consequence, the Register of Deeds of the Province of Rizal (now of Pasig, Metro Manila) to cancel the mortgage annotations, pertaining to the said real estate mortgages, made at the back of Original Certificate of Title No. 2224 of the Registry of Deeds of the Province of Rizal (now of Pasig, Metro Manila);
6. Ordering, as well, the Register of Deeds of the Province of Rizal (now of Pasig, metro Manila) to return and deliver to the plaintiffs the owner's duplicate copy of Original Certificate of Title No. 2224 of the Registry of Deeds of the Province of Rizal (now of Pasig, Metro Manila);
7. Ordering the defendants to pay to plaintiffs C & C Commercial Corporation, jointly and severally, actual damages in the amounts of : (a) P4,520,000.00, as business losses; (b) P6,599,224.00, as unrealized profits; (c) P8,084,631.00, as capital deficiency; and (d) P781,993.00, representing decrease in assets, including the sum of P1,000,000.00 as exemplary damages as well as P500,000.00, in reasonable attorney's fees, or for the total net amount of P20,199,848.00, in damages and attorney's fees, after deducting from the gross total of the aforesaid awarded damages and attorney's fees, the total secured loans of P1,286,000.00 by way of set off/compensation;
8. Ordering the defendants to pay to plaintiff C & C Commercial Corporation, also jointly and severally, interests on the total actual damages of P19,985,848.00, at the rate of 8% per annum from the date of this judgment until fully paid;