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**FIRST DIVISION**

[G.R. No. 199420. August 27, 2014]

**PHILNICO INDUSTRIAL CORPORATION,** *petitioner*, *vs.* **PRIVATIZATION AND MANAGEMENT OFFICE,** *respondent.*

[G.R. No. 199432. August 27, 2014]

**PRIVATIZATION AND MANAGEMENT OFFICE,** *petitioner*, *vs.* **PHILNICO INDUSTRIAL CORPORATION,** *respondent.*

**SYLLABUS**

**1. CIVIL LAW; CIVIL CODE; PLEDGE; SECTION 8.02 OF THE AMENDED AND RESTATED DEFINITIVE AGREEMENT (ARDA) CONSTITUTES *PACTUM COMMISSORIUM* AND, THUS, NULL AND VOID FOR BEING CONTRARY TO ARTICLE 2088 OF THE CIVIL CODE.—** Article 1305 of the Civil Code allows contracting parties to establish such stipulation, clauses, terms, and conditions as they may deem convenient, provided, however, that they are not contrary to law, morals, good customs, public order, or public policy. *Pactum commissorium* is among the contractual stipulations that are deemed contrary to law. It is defined as "a stipulation empowering the creditor to appropriate the thing given as guaranty for the fulfillment of the obligation in the event the obligor fails to live up to his undertakings, without further formality, such as foreclosure proceedings, and a public sale." It is explicitly prohibited under Article 2088 of the Civil Code which provides: ART. 2088. The creditor cannot appropriate the things given by way of pledge or mortgage, or dispose of them. Any stipulation to the contrary is null and void. There are two elements for *pactum commissorium* to exist: (1) that there should be a pledge or mortgage wherein a property is pledged or mortgaged by way of security for the payment of the principal obligation; and (2) that there should be a stipulation for an automatic appropriation by the creditor of the thing pledged or mortgaged in the event of nonpayment of the principal obligation within the stipulated period. Both elements of *pactum commissorium*

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are present in the instant case: (1) By virtue of the Pledge Agreement dated May 2, 1997, PIC pledged its PPC shares of stock in favor of PMO as security for the fulfillment of the former's obligations under the ARDA dated May 10, 1996 and the Pledge Agreement itself; and (2) There is automatic appropriation as under Section 8.02 of the ARDA, in the event of default by PIC, title to the PPC shares of stock shall *ipso facto* revert from PIC to PMO without need of demand.

**2. ID.; ID.; ID.; IN DETERMINING THE EXISTENCE OF *PACTUM COMMISSORIUM*, THE COURT, HAD FOCUSED MORE ON THE EVIDENT INTENTION OF THE PARTIES, RATHER THAN THE FORMAL OR WRITTEN FORM.—** In *Blas v. Angeles-Hutalla*, the Court recognized that the agreement of the parties may be embodied in only one contract or in two or more separate writings. In case of the latter, the writings of the parties should be read and interpreted together in such a way as to render their intention effective. The agreement between PMO and PIC is the sale of the PPC shares of stock by the former to the latter, to be secured by a pledge on the very same shares of stock. The ARDA and the Pledge Agreement herein, although executed in separate written instruments, are integral to one another. On one hand, Section 2.04 of the ARDA explicitly requires the execution of a pledge agreement as security for the payment by PIC of the purchase price for the PPC shares of stock and receivables, and even provides the form for said pledge agreement in Annex A thereof. Section 2.07 of the ARDA also states that the closing of the sale and purchase of the PPC shares of stock and receivables shall take place on the same date that PIC shall execute and deliver the pledge agreement, together with the certificates of shares of stock, to PMO. On the other hand, the "Whereas Clauses" of the Pledge Agreement expressly mentions the ARDA and explains that the Pledge Agreement is being executed to secure payment by PIC of the purchase price and all other amounts due to PMO under the ARDA, as well as the performance by PIC of its other obligations under the ARDA and the Pledge Agreement itself. Clearly, it was the intention of the parties to enter into and execute both contracts for a complete effectuation of their agreement. To reiterate, the Pledge Agreement secures, for the benefit of PMO, the performance by PIC of its obligations under both the ARDA and the Pledge Agreement itself. It is with the execution of

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the Pledge Agreement that PIC turned over possession of its certificates of shares of stock in PPC to PMO. As the RTC pertinently observed in its Order dated June 19, 2003, there had already been a shift in the relations of PMO and PIC, from mere seller and buyer, to creditor-pledgee and debtor-pledgor. Having enjoyed the security and benefits of the Pledge Agreement, PMO cannot now insist on applying Section 8.02 of the ARDA and conveniently and arbitrarily exclude and/or ignore the Pledge Agreement so as to evade the prohibition against *pactum commissorium*. More importantly, the Court, in determining the existence of *pactum commissorium*, had focused more on the evident intention of the parties, rather than the formal or written form. In *A. Francisco Realty and Development Corporation v. Court of Appeals*, therein petitioner similarly denied the existence of *pactum commissorium* because the proscribed stipulation was found in the promissory note and not in the mortgage deed.

**3. ID.; ID.; ID.; CONTRACT OF PLEDGE IS VALID SINCE OWNERSHIP OF THE SUBJECT SHARES OF STOCK HAD PASSED ON TO PETITIONER.—** Among the requirements of a contract of pledge is that the pledgor is the absolute owner of the thing pledged. Based on the provisions of the ARDA, ownership of the PPC shares of stock had passed on to PIC, hence, enabling PIC to pledge the very same shares to PMO. In accordance with Section 2.07(a)(1) and 2.07(a)(2) of the ARDA, PMO had transferred to PIC all rights, title, and interests in and to the PPC shares of stock, and delivered to PIC the certificates for said shares for cancellation and replacement of new certificates already in the name of PIC. In addition, Section 2.07(b) of the ARDA explicitly declares that PIC as buyer shall exercise all the rights, including the right to vote, of a shareholder in respect of the PPC shares of stock. PMO cannot maintain that the ownership of the PPC shares of stock did not pass on to PIC, but in the same breath claim that non-payment by PIC of the installments due on the purchase price is a resolutory condition for the contract of sale – these two arguments are actually contradictory. As the Court clearly explained in *Heirs of Paulino Atienza v. Espidol*: Regarding the **right to cancel the contract for nonpayment of an installment**, there is need to initially determine if what the parties had was a contract of sale or a contract to sell. **In a contract of sale, the title to the property passes to the buyer**

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**upon the delivery of the thing sold.** In a contract to sell, on the other hand, the ownership is, by agreement, retained by the seller and is not to pass to the vendee until full payment of the purchase price**. In the contract of sale, the buyer's nonpayment of the price is a negative resolutory condition;** in the contract to sell, the buyer's full payment of the price is a positive suspensive condition to the coming into effect of the agreement. **In the first case, the seller has lost and cannot recover the ownership of the property unless he takes action to set aside the contract of sale.** In the second case, the title simply remains in the seller if the buyer does not comply with the condition precedent of making payment at the time specified in the contract. x x x. So that it could invoke the resolutory condition of nonpayment of an installment, PMO must necessarily concede that its contract with PIC was a one of sale and that ownership of the PPC shares of stock had indeed passed on to PIC. And even then, having lost ownership of the shares, PMO cannot automatically recover the same without taking steps to set aside the contract of sale.

**4. ID.; OBLIGATIONS AND CONTRACTS; IN THE ABSENCE OF A STIPULATION, A PARTY CANNOT UNILATERALLY AND EXTRAJUDICIALLY RESCIND A CONTRACT; A PARTY MUST INVOKE THE RIGHT TO RESCIND A CONTRACT JUDICIALLY.—** The general rule is that in the absence of a stipulation, a party cannot unilaterally and extrajudicially rescind a contract. A party must invoke the right to rescind a contract judicially. It is also settled that the rescission of a contract based on Article 1191 of the Civil Code requires mutual restitution to bring back the parties to their original situation prior to the inception of the contract. Rescission creates the obligation to return the object of the contract. It can be carried out only when the one who demands rescission can return whatever he may be obliged to restore. Even though PMO had previously acknowledged the need for restitution or restoration following rescission, it also qualified that such restitution or restoration shall still be "subject x x x to the fair determination of the amount to be restored as may be deemed reasonable and substantiated." Section 8.02 of the ARDA provides for the *ipso facto* reversion of the pledged shares of PIC to PMO in case of default on the part of the former, which as explained above, is prohibited by Article 2088 of the Civil Code. The said Section does not

mention the broader concept of rescission of the entire ARDA. In its Petition in G.R. No. 199432, PMO is asking the Court, among other things, to already declare the ARDA rescinded. The Court cannot grant or deny such prayer at this point for there are questions of fact and law which are still under litigation before the RTC.

**5. REMEDIAL LAW; PROVISIONAL REMEDIES; NO BASIS FOR DISSOLVING THE WRIT OF PRELIMINARY INJUNCTION.—** The Court emphasizes that the Writ of Preliminary Injunction was granted in the RTC Order dated February 27, 2003; and the Motion for Reconsideration of the issuance of said Writ filed by the PMO was denied in the RTC Order dated June 19, 2003 – both of which are interlocutory orders. Under Rule 65 of the Rules of Court, the PMO only had 60 days from notice to file with the Court of Appeals a petition for *certiorari* assailing said orders. However, PMO did not file such a petition and lost the right to avail itself of the remedy. PMO, in challenging the RTC Order dated August 25, 2009, cannot be allowed to revive the issues of *pactum commissorium* and the arbitration clause, together with its opposition to the Writ of Preliminary Injunction, which were already settled and ruled upon six years before in the RTC Orders dated February 27, 2003 and June 19, 2003. The removal of said issues from those submitted for trial before the RTC is thus justified. That the RTC issued the aforementioned Orders of 2003 based only on initial and incomplete evidence is incorrect. The issues of *pactum commissorium* and arbitration clause are questions of law that do not require the review or evaluation of evidence. The RTC, before issuing said Orders of 2003, conducted hearings and required the submission of pleadings, so the parties were given the opportunity to present their arguments on said questions of law. In particular, the ruling of the RTC that Section 8.02 of the ARDA constitutes *pactum commissorium*, cannot be set aside and the Writ of Injunction issued based on such ruling cannot be dissolved, even if there be changes in the factual circumstances of the parties, for as long as the applicable law remains the same. There are still several remaining issues in the Pre-Trial Order dated February 6, 2009 that the RTC needs to resolve, among others, the alleged default under the ARDA. They involve both questions of fact and law, so their resolution requires further hearings for presentation of evidence by the parties. Hence,

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PMO cannot claim pre-judgment of its case with the issuance by the RTC of the Orders dated February 27, 2003 and June 19, 2003. Despite the declaration that Section 8.02 of the ARDA is null and void as it constitutes *pactum commissorium*, PMO and PIC shall have the opportunity to thresh-out other issues between them which are not resolved in these cases, such as the issue of default, during the trial on the merits before the RTC.

**APPEARANCES OF COUNSEL**

*Agabin Verzola & Layaoen Law Offices and See* and *Herrera Law Firm* for Philnico Industrial Corp.

*The Solicitor General* for Privatization and Mgn't. Office.

**D E C I S I O N**

**LEONARDO-DE CASTRO, *J.*:**

Before the Court are the consolidated Petitions for Review on *Certiorari* under Rule 45 of the Rules of Court involving the Decision[1] dated January 31, 2011 and Resolution[2] dated November 18, 2011 of the Court of Appeals in CA-G.R. SP. No. 111108, which affirmed the Order[3] dated August 25, 2009 of the Regional Trial Court (RTC), Branch 64 of Makati City in Civil Case No. 03-114.

**THE PARTIES**

The Petition in G.R. No. 199420 was filed by Philnico Industrial Corporation (PIC). It is a corporation duly organized under the laws of the Philippines and which, together with Philnico Processing Corporation (PPC) and Pacific Nickel Philippines,

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[1] *Rollo* (G.R. No. 199420), pp. 49-59; penned by Associate Justice Samuel H. Gaerlan with Associate Justices Hakim S. Abdulwahid and Ricardo R. Rosario, concurring.

[2] *Id.* at 60-61.

[3] *Id.* at 69-71; penned by Judge Gina M. Bibat-Palamos.

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Inc. (PNPI), form the Philnico Group. The Philnico Group is engaged in nickel mining and refining business. PIC and PNPI hold a Mineral Production Sharing Agreement over nickel mining areas in Nonoc and Dinagat Islands in Surigao, while PPC owns a nickel refinery complex also in Nonoc Island.[4]

The Petition in G.R. No. 199432 was filed by the Privatization and Management Office (PMO), an attached agency of the Department of Finance. PMO succeeded the Asset Privatization Trust (APT), when the latter's life ended on December 31, 2000.[5] The PMO serves as the marketing arm of the Government with respect to Transferred Assets, Government Corporations and other properties assigned to it by the Privatization Council (PrC) for disposition. Together, the mission of the PMO and PrC is to take title to and possession of, conserve, provisionally manage, and dispose of assets previously identified for privatization; and, in the process, reduce the Government's maintenance expense on non-performing assets, generating maximum cash recovery for the National Government.[6]

## ANTECEDENT FACTS

The Development Bank of the Philippines and Philippine National Bank, by virtue of foreclosure proceedings, became the holders of all the shares of stock in PPC (then still the Nonoc Mining and Industrial Corporation). The banks eventually transferred their PPC shares of stock to PMO (then still the APT) in 1987.

On May 10, 1996, PMO, PIC (then still the Philnico Mining and Industrial Corporation), and PPC executed a contract, denominated as the Amended and Restated Definitive Agreement (ARDA), which laid down the terms and conditions of the

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[4] *Id.* at 16.

[5] Executive Order No. 323; Republic Act No. 7661, as amended by Republic Act No. 8758; and Proclamation No. 50.

[6] Citizens Charter (Anti Red Tape Act of 2007 in accordance with Republic Act No. 9485 and pursuant to Civil Service Commission-Memorandum Circular No. 12-2008) http://www.pmo.gov.ph/transparency/charter.pdf (last opened August 19, 2014).

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purchase and acquisition by PIC from PMO of 22,500,000 shares of stock of PPC (representing 90% of ownership of PPC), as well as receivables of PMO from PPC. Under the ARDA, PIC agreed to pay PMO the peso equivalent of US$333,762,000.00 as purchase price, payable in installments and in accordance with the schedule also set out in the ARDA.[7]

Among the provisions of the ARDA relevant to the instant cases are Sections 2.04 and 2.07, which govern the rights and obligations of the parties as regards the PPC shares of stock, *viz*:

> 2.04 Security
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> (a) As security for the payment of the Purchase Price in accordance with the terms of this Agreement, the Buyer shall pledge the Shares to the Seller and execute a pledge agreement (the "Pledge Agreement") in favor of the Seller in substantially the form of Annex A. The Buyer shall also pledge to the Seller the Converted Shares and the New Shares as security for the payment of the Purchase Price upon the issuance of such shares in the name of the Buyer.
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> 2.07 Closing
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> (a) The closing of the sale and purchase of the Shares and the Tranche B Receivables under this Agreement shall take place on the Closing Date and at such place as may be agreed between the Buyer and the Seller upon the fulfillment of all of the conditions precedent specified in Sections 4.01 and 4.02 (unless any such condition precedent shall have been waived by the Buyer or the Seller, as the case may be). At the closing, the following transactions shall take place:
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> (1) the Seller shall execute and deliver to the Buyer the necessary deed of sale transferring to the Buyer all of the Seller's right, title and interest in and to the Shares and deliver to the Buyer the stock certificates representing such shares, each duly

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[7] *Rollo* (G.R. No. 199432), pp. 161-193.

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endorsed, or with separate stock transfer powers attached, in favor of the Buyer together with the duly executed resignations of the directors of the Company named in Schedule 6;

(2) the Company shall issue in the name of, and deliver to, the Buyer new stock certificates representing the Shares;

(3) the Buyer shall execute and deliver the Pledge Agreement covering the Shares and deliver to the Seller the stock certificates representing such shares;

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(b) From and after the Closing Date, the Buyer shall exercise all the rights (including the right to vote) of a shareholder in respect of the Shares (subject to the negative covenants contained in the Pledge Agreement).[8]

Also worthy of note herein is Section 8 of the ARDA on default, which states:

SECTION 8. DEFAULT AND DEFAULT REMEDIES

8.01 Events of Default

Subject to any applicable curing period, each of the following events shall constitute an Event of Default hereunder:

(a) The Buyer shall, subject to the provisions of Section 2.03(b), fail to pay any two consecutive installments on the Purchase Price in accordance with the terms of Section 2.03.

(b) The Buyer shall fail to comply with or observe any other material term, obligation or covenant contained in this Agreement or in the Pledge Agreement.

(c) The Buyer shall commit any act of bankruptcy or insolvency, or shall file any petition or action for relief under any bankruptcy, reorganization, insolvency or moratorium law or other law or laws for the relief of debtors.

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[8] *Id.* at 170-172.

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8.02 Consequence of Default

At any time after the happening of an Event of Default, and provided that the same shall not have been remedied within ninety (90) days from receipt by the Buyer of written notice from the Seller, the Seller may declare the buyer in default and, as a consequence thereof, exercise such rights and remedies as it may have under this Agreement and applicable laws (including the cancellation of these Agreement); **provided that in case of default under Section 8.01(a), the title to the Existing Shares and the Converted Shares shall *ipso facto* revert to the Seller without need of demand in case such payment default is not remedied by the Buyer within ninety (90) days from the due date of the second installment.** (Emphasis supplied.)[9]

In accordance with the ARDA, PMO executed and delivered to PIC the necessary documents to transfer the former's rights, title, and interests to and in the PPC shares of stock to the latter; and PPC issued new certificates for the same shares of stock in the name of PIC and/or its nominees.

On May 2, 1997, PIC and PNPI as pledgors and PMO as pledgee executed a Pledge Agreement[10] which began with "Whereas Clauses" that read:

WHEREAS, [PIC] and the [PMO] have entered into an Amended and Restated Definitive Agreement, dated May 10, 1996, involving the purchase by the [PIC] from the [PMO] of 22,500,000 shares of common stock of [PPC] and certain receivables of the [PMO] from said corporation; and

WHEREAS, to secure the obligation of [PIC] to pay the purchase price and all other amounts due the [PMO] under the aforesaid Definitive Agreement and the performance by [PIC] of its other obligations thereunder and under this Pledge Agreement, the [PIC and PNPI] have agreed to execute and deliver this Pledge Agreement, giving unto the [PMO] a good and valid pledge over the pledge[d] shares[.][11]

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[9] *Id.* at 189-190.

[10] *Id.* at 247-258.

[11] *Id.* at 247.

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Sections 3.01 and 3.02 of the Pledge Agreement expressly acknowledged that PIC delivered its certificates of shares of stock in PPC and that PMO received said certificates.[12] Section 5 of the same Agreement covered default and the available remedies in case thereof, thus:

SECTION [5]. DEFAULT REMEDIES, *ETC.*

5.01 Events of Default

The following shall be considered Events of Default under this Pledge Agreement:

(a) [PIC] shall fail to pay when due the obligations after giving effect to any applicable period of grace; or

(b) [PIC] or PNPI shall fail to comply with or observe any other material term, obligation or covenant contained in this Pledge Agreement or the Definitive Agreement; or

(c) [PIC] or PNPI shall commit any act of bankruptcy or insolvency, or shall file any petition or action for relief under any bankruptcy, reorganization, insolvency or moratorium law or other x x x laws for the relief of debtors; or

(d) The priority of the lien of or the security interest granted by this Pledge Agreement shall be impaired, or this Pledge Agreement shall cease to be a first and preferred lien upon the Pledged Shares.

5.02 Consequences of Default

If an Event of Default shall have occurred, then at any time thereafter, if any such event shall then be continuing after the applicable grace period, if any, the [PMO] is hereby authorized:

(a) To sell in one or more sales, either public or private, at any time the whole or any part of the Pledged Shares in such order and number as the [PMO] may elect at its place of business or elsewhere and the [PMO] may, in all allowable cases, be the purchaser of any or all Pledged Shares so sold and hold the same thereafter in its own right free from any claim of [PIC] or any right of redemption;

(b) To issue receipts and to execute and deliver any instrument or document or do any act necessary for the transfer and assignment

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[12] *Id*. at 250.

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of all rights, title and interest of [PIC] in the Pledged Shares to the purchaser or purchasers thereof; and

(c) To apply, at the [PMO's] option, the proceeds of any said sale, as well as all sums received or collected by the [PMO] from or on account of such Pledged Shares to (i) the payment of expenses incurred or paid by the [PMO] in connection with any sale, transfer or delivery of the Pledged Shares and (ii) the payment of the Obligations or any part thereof.[13]

In the meantime, the nickel refinery complex of PPC, which last operated in the 1980s, had become obsolete and much of the facilities therein were already scrap. The estimated cost in 2003 for building an entirely new refinery plant based on new technology was about US$1 Billion. The Philnico Group, which had already invested at least US$60 Million, was inviting and negotiating with prospective foreign investors who could assist in its business.

On account of the huge financial cost of building a new nickel refinery plant, coupled with the economic problems then affecting the Asia-Pacific Region, PMO, PIC, and PPC executed an Amendment Agreement[14] on September 27, 1999 which provided for the restructuring of the payment terms of the entire obligation under the ARDA, the repayment of advances, the conditions for borrowings or financing, a new cash break-even formula, and the adoption of an investment plan.

Three years later, in a letter dated November 6, 2002, PMO notified PIC that the latter had defaulted in the payment of its obligations and demanded that PIC settle its unpaid amortizations in the total amount of US$275,000.00 within 90 days, or on or about February 5, 2003, or else the PMO would enforce the automatic reversion of the PPC shares of stock under Section 8.02 of the ARDA. PIC replied in a letter dated January 7, 2003 requesting PMO to set aside its notice of default; to not rescind the sale of the PPC shares of stock; and to give PIC an

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[13] *Id*. at 254-255.

[14] *Id*. at 224-238.

opportunity to conclude its fund-raising efforts for its business, particularly with a group of investors from China. In another letter dated January 22, 2003 to PIC, PMO clearly indicated its intention to enforce Section 8.02 of the ARDA should PIC fail to settle its outstanding obligations after February 5, 2003.

On February 4, 2003, a day before the deadline for payment set by PMO in its letters, PIC filed before the RTC a Complaint for Prohibition against Reversion of Shares with Prayer for Writ of Preliminary Injunction and/or Temporary Restraining Order, Suspension of Payment and Fixing of Period of Payment, against PMO, PPC, and the PPC Corporate Secretary. On February 7, 2003, PIC filed an Amended Complaint raising, among other arguments, the need for mutual restitution in case the ARDA is rescinded by the RTC. Ultimately, PIC prayed of the RTC that:

(a) Upon the filing of this complaint, a temporary restraining order be issued under Sec. 5 of Rule 58 of [the] 1997 Rules of Civil Procedure prohibiting [PMO, PPC, and the PPC Corporate Secretary] from reverting the 22,500,000 shares covered by Stock Certificate Nos. 018, 022, 024, 025, 026, 027, 028, 030 and 031 x x x in the name of [PIC] to defendant PMO.

(b) After hearing –

(i) A writ of preliminary injunction be issued prohibiting [PMO, PPC, and the PPC Corporate Secretary] from effecting the reversion of the aforementioned shares in favor of defendant PMO until further orders from the Court; and thereafter,

(c) Judgment issue –

(i) Making the injunction permanent and ordering the suspension of the payment of the amortizations as provided for in the ARDA and fixing a reasonable period within which said payment should be due; and

(d) Or in the alternative, in the remote possibility that the ARDA x x x be considered rescinded, mutual restitution be ordered by the Honorable Court as provided by the Civil Code relative to reciprocal obligations.

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[PIC] prays for such further and equitable relief as may be just and equitable in the premises.[15]

After the summary hearing held on February 7, 2003, the RTC issued a temporary restraining order (TRO), effective for 20 days, restraining PMO, PPC, and the PPC Corporate Secretary from effecting the reversion of the 22,500,000 shares of stock of PPC.

The RTC then conducted hearings on the prayer of PIC for the issuance of a writ of preliminary injunction. The RTC subsequently issued an Order[16] on February 27, 2003 finding PIC entitled to the issuance of such a writ for the following reasons:

> While the failure of [PIC] to meet its amortization with respect to the smaller portion of the purchase price cannot be denied, said default cannot automatically result in the reversion of the shares of stocks to PMO. The provision in the ARDA providing for *ipso facto* reversion of the shares of stock is null and void for being a *pactum commissorium*. x x x.
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> The automatic reversion of the shares of stock is by itself automatic appropriation of the thing pledged, which is contrary to good morals and public policy. It would also result in unjust enrichment on the part of defendant PMO. Even in case of rescission, mutual restitution is allowed so as not to enrich one party to the prejudice of the other. It would be tantamount to confiscation of property without due process. The seller had the option of foreclosing the property pledged. The seller cannot automatically appropriate the same to himself when the ownership is already transferred to [PIC]. Thus, even for the time being when foreclosure of the shares pledge[d] is being considered, and the question of rescission is being deliberated, [PIC] has a right to be protected and therefore entitled to the relief of preliminary injunction.

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[15] *Id.* at 157-158.

[16] *Rollo* (G.R. No. 199420), pp. 62-68; penned by Judge Delia H. Panganiban.

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Regarding the provision on referral to arbitration, granting that the case is proper for arbitration, [PIC] is nonetheless entitled to the writ of preliminary injunction pending the arbitration proceeding.

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One of the requirements for the issuance of the writ of preliminary injunction is when there is an urgent and paramount necessity for the writ to prevent an irreparable damage. Irreparable means one that can not be rectified. [PIC] is in danger of losing its investment in the project without any recourse if PMO will be allowed the automatic reversion of the ownership of the 22,500,000 shares. The right of [PIC] will be prejudiced if the writ of preliminary injunction will not be issued in the meantime.[17]

The RTC thus decreed:

WHEREFORE, premises considered, the Writ of Preliminary Injunction is GRANTED.

Until further Order from this Court, and subject to [PIC's] filing of a bond in the amount of ₱100,000,000.00 to pay for all the damages which [PMO, PPC, and the PPC Corporate Secretary] may sustain by reason of the injunction if the Court will finally decide that [PIC] is not entitled thereto, defendants Privatization and Management Office (PMO), Philnico Processing Corporation (PPC), and the Corporation Secretary of PPC are enjoined from effecting the reversion to PMO of the 22,500,000 shares purchased by plaintiff Philnico Industrial Corporation and from selling the same to any third party.[18]

PMO filed a Motion for Reconsideration of the RTC Order dated February 27, 2003, insisting that the provision on *ipso facto* reversion in the ARDA did not constitute *pactum commissorium* and would not result in unjust enrichment on the part of PMO. PMO likewise filed a Motion to Dismiss on the ground that the complaint of PIC did not state a cause of action. In its Order[19] dated June 19, 2003, the RTC found no merit in both Motions and held that:

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[17] *Id*. at 65-67.

[18] *Id*. at 67-68.

[19] *Rollo* (G.R. No. 199432), pp. 343-344B; penned by Judge Delia H. Panganiban.

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1. The Motion for Reconsideration is DENIED. This Court maintains that [PIC] is entitled to the issuance of the Writ of Preliminary Injunction.

[PIC] has already acquired ownership of the 22,500,000 shares when the ARDA was executed between the parties. The ARDA merely provides for the transfer of the subject shares to [PIC]. As a matter of fact, [PIC] has executed a Pledge Agreement as a security for the payment of [PIC's] obligation with defendant PMO.

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Under the ARDA, the relationship of [PIC] and defendant PMO is that of a pledgor and pledgee and no longer as a buyer and seller. As such, the *ipso facto* reversion of the shares in the ARDA constitutes *pactum commissorium*. The execution of the Pledge Agreement is precisely made to secure the payment of [PIC's] obligation with defendant PMO. The automatic reversion of the shares if allowed will in fact constitute automatic appropriation of the thing pledged which is proscribed being *pactum commissorium*. The automatic appropriation itself will prejudice the investment made by [PIC] in the said project and all improvements will inure to defendant PMO which the law abhors. Even in case of rescission, mutual restitution is allowed so as not to enrich one party at the expense of the other. This forfeiture clause in the ARDA is contrary to law, good morals and public policy.

2. With respect to the Motion To Dismiss, the same is DENIED.

Cause of action is the act or omission by which a party violates a right of another (Sec. 2, Rule 2 of the 1997 Rules on Civil Procedure). As already stated in the resolution of the motion for reconsideration, the *ipso facto* reversion of the shares pursuant to Section 8.02 of the ARDA constitute[s] *pactum commissorium*, and therefore null and void being contrary to morals, law and public policy. As such, the *ipso facto* reversion of the shares will result in unjust enrichment on the part of defendant PMO for the reason that all investment of [PIC] with the said project will inure to the benefit of defendant PMO with [PIC] getting nothing.

The present case does not violate the principles of autonomy of contract[s]. [PIC] seeks to prohibit the implementation of the *ipso facto* reversion clause in the ARDA, which is contrary to law being a *pactum commissorium*. This is a limitation imposed by law, which is considered to be part of a contract. Contracts must respect the

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law, for the law forms part of the contract. While the contract is the law between the parties, the Court may stop its enforcement if it is contrary to law, morals, good customs or public policy (San Andres *vs*. Rodriguez, 332 SCRA 69).

While the ARDA provides for arbitration as mode of settlement of the dispute (Section 9.05), the present complaint involves interpretation of the provisions of the ARDA. Interpretation of contracts is within the domain of the Court. The *ipso facto* reversion of the shares in the ARDA can never be subject of arbitration but it is within the domain of the court to declare whether or not the same is valid or null and void.[20]

In the same Order, the RTC directed PMO, PPC, and the PPC Secretary to file their answer to the complaint of PIC. PMO no longer challenged the RTC Orders dated February 27, 2003 and June 19, 2003 before the appellate courts. Instead, PMO complied with the RTC directive and already filed with the said trial court its Answer and Amended Answer to the complaint of PIC.

The RTC proceeded to pre-trial when the parties failed to arrive at an amicable settlement. On February 6, 2009, the RTC issued its Pre-trial Order[21] in which it enumerated the respective issues for resolution submitted by PIC and PMO, to wit:

ISSUES ([PIC])

1. **Whether or not the *ipso facto* reversion clause in the ARDA is valid, and, whether or not it is a specie[s] of *pactum commissorium* which is outlawed.**
2. Whether or not [PIC] is in default under the terms of the ARDA which clearly contemplates the actual operation of the plant before the subsequent installments after the third year will be due, as it even recognizes deferment of payment of installment if the Nonoc mining plant and refinery is not yet in full operation and has not produced sufficient cash equivalent for payment to seller.

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[20] *Id*. at 344-344B.

[21] *Id*. at 345-351; penned by Presiding Judge Gina M. Bibat-Palamos.

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3. Even assuming that the schedule of payment is not modified by the other terms of the ARDA (as actual operation of the plant and refinery), whether or not [PIC] may be considered as in default considering the fortuitous events which are unforeseen and beyond the control of [PIC] which had prevented [PIC] from complying with its obligation under the scheduled amortization.

4. Whether or not [PIC] is entitled to be reimbursed what it had already paid and spent to implement the contract, in the remote event that APT/PMO may be allowed to exercise right [of] rescission.

5. **Whether or not plaintiff [PIC] is required to resort to arbitration to enforce its cause of action in the complaint.**

ISSUES ([PMO])

1. Whether or not defendant PMO may be prohibited from *ipso facto* reverting the shares pursuant to the ARDA considering that [PIC] defaulted in its payment and there is an express provision in the ARDA providing for the said provision.

2. Whether or not the terms and modes of payments as provided in the ARDA may be suspended or fixed anew by reason of unforeseen events cited by [PIC].

3. Whether or not defendant PMO may be enjoined by this Honorable Court in the performance of its functions and duties in connection with the sale or disposition of assets transferred to it pursuant to Proclamation No. 50-A.[22] (Emphases supplied.)

PIC filed a Manifestation and Motion praying for the modification of the foregoing Pre-trial Order dated February 6, 2009 of the RTC by deleting Issue Nos. 1 and 5 in the Statement of Issues of PIC. PIC posited that these two issues were already resolved by the RTC in the Order dated June 19, 2003 and should no longer be among the issues to be tried in the course of subsequent proceedings.

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[22] *Id*. at 349-350.

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PMO countered in its Comment/Opposition that the RTC Orders dated February 27, 2003 and June 19, 2003 concerned only the issuance of the Writ of Preliminary Injunction; and the findings and conclusions of the trial court on the propriety of the issuance of the injunctive writ are premised on initial and incomplete evidence, which should be considered merely as provisional. Said RTC Orders should not bind the trial court in its determination of the merits of the case and to hold otherwise would result in the prejudgment of the case or disposition of the main case without a full-blown trial. Consequently, PMO prayed that the RTC deny the Manifestation and Motion of PIC.

PMO also successively filed an Omnibus Motion and a Supplement to Omnibus Motion, asserting that: (1) the Writ of Preliminary Injunction was issued in 2003 by the RTC without jurisdiction and was therefore void, because there was no compliance with the arbitration clause in the ARDA; (2) the continuance of the Writ of Preliminary Injunction is causing irreparable damage to the National Government; (3) since the issuance of the Writ of Preliminary Injunction six years before, PIC had effectively achieved and obtained the reliefs it had prayed for in its complaint as it was able to suspend the payment of monthly amortization and prevent the reversion, or even the selling, of the PPC shares of stock in the event of default; (4) the amount of injunction bond is insufficient and grossly disproportionate to the enormity of the damages that PMO stands to suffer; (5) the injunctive writ is supposed to be a "strong arm of equity" and should not be used as an instrument of perpetrating injustice against the National Government; (6) in accordance with Rule 58, Section 6 of the Rules of Court, PMO is signifying its intention to post a counterbond that would answer for the damages PIC might suffer by the dissolution of the Writ of Preliminary Injunction; and (7) PMO thought it prudent to no longer assail the RTC Orders dated February 27, 2003 and June 19, 2003 before the appellate courts believing that such a move would only cause further delay in the resolution of the case and cause more irreparable damage to the National Government. PMO sought several reliefs from the RTC in its Omnibus Motion, quoted as follows:

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(1) That the Writ of Preliminary Injunction be dissolved;

(2) That a representative of defendant PMO be appointed to the PPC's and PNPI's board of directors or management; and

(3) That [PIC] be required to submit an accounting of its books and financial reports from the year 2003 to 2008.

Other just and equitable reliefs are also prayed for.[23]

Following hearings and exchange of pleadings by the parties, the RTC collectively resolved the pending motions of PIC and PMO in its Order dated August 25, 2009.

The RTC determined that there was sufficient basis to grant the Manifestation and Motion of PIC to delete two issues from the Pre-Trial Order dated February 6, 2009:

The Court will not disturb the earlier findings of the previous judge that the *ipso facto* reversion clause in the ARDA is invalid and that it constitute[s] *pactum commissorium*. The Court finds no legal and factual reasons to change the previous findings of the Honorable Delia H. Panganiban that [PIC] has already acquired ownership of the 22,500,000 shares sold to it and that the ARDA is merely a scheme for the transfer of the said share to the latter. As such, the relation between [PIC] and defendant PMO has become that of a mortgagor and mortgagee. Accordingly, the proviso in the ARDA for the *ipso facto* reversion constitutes *pactum commissorium*.

The Court disagrees with [PMO] that the said finding is merely initiatory as it was a finding on a legal issue. No other evidence is needed to change the same. In fact, said issue was extensively and exhaustively argued by the parties in their respective pleadings in relation thereto. It is presumed that the previous Presiding Judge of this Court has considered all the arguments raised by the parties. Section 3(o) of Rule 131 of the Revised Rules of Court provides: that all matters within an issue raised in a case were laid before the court and passed upon by it. In addition, based on the personal analysis of its new Presiding Judge, the Court is judiciously convinced of the soundness of its earlier findings. More importantly, it appears from the records that defendant PMO never challenged such finding

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[23] *Id.* at 505-506.

in a higher judicial arena. Thus, this Court deems its resolution to be incontestable at this stage. Consequently, since the said finding has attained finality, any error that this Court may have committed in resolving the said issue may only be raised in an appeal to be made by the adverse party.

This Court also finds merit [i]n plaintiff's prayer for the deletion of the fifth issue raised during the pre-trial of this case. The denial of the motion to dismiss previously filed by defendant PMO also [constitutes] as an adjudication on the issue as to whether or not the subject matter of this case is a proper subject of arbitration proceedings as provided for in ARDA. The Court reached the said conclusion based on jurisprudential law which up to this date is unchanged. Said conclusion has also become immutable when [PMO, PPC, and the PPC Corporate Secretary] similarly failed to challenge the same.[24]

As for the Omnibus Motion and Supplement to Omnibus Motion of PMO, the RTC only conceded to requiring PIC to submit accounting and financial reports to PMO:

On defendant PMO's omnibus motion and its supplemental thereto, the Court resolves the first motion in the negative. As stated above[,] this instant case does not involve matters which can be adjudicated through arbitration. It involves the interpretation of contract which falls within the jurisdiction of this Court. This Court agrees with [PIC] that there can be no damage when what is being restrained is an illegal act. It need not be said that no right can emanate from an illegal act. In this instant case, what is being restrained by the Writ is the enforcement by defendant PMO of the reversion clause in the ARDA. Having unequivocally declared such reversion clause illegal, the Court has no reason to terminate the efficacy of the Writ it issued. The Court notes that defendant PMO did not lift a finger during the time that it should have done so. Thus, the delay, if there be any, is not solely attributable to [PIC]. Having impliedly consented thereto, defendant PMO must suffer the consequences of its inaction. The same is true on the allegation of insufficiency of the injunction bond filed by [PIC]. The defendant PMO's failure to question the same within reasonable time the amount of the injunction bond posted by [PIC] is fatal to its cause as it galvanized the resolution of the Court on the matter.

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[24] *Rollo* (G.R. No. 199420), p. 70.

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The Court will not act on defendant PMO's prayer for the appointment of a representative in [PIC's] Board of Director[s]. As stated by [PIC] in its opposition to the pending incident, that it is not preventing defendant PMO to appoint a representative [in the] former, the Court will no longer discuss the said motion. The parties, however, are directed to notify this Court of the appointment by [PMO] of a representative in [PIC's] Board of Director[s]. On defendant PMO's motion to submit accounting report, while it may be true that [PIC] is submitting its financial statements to the Bureau of Internal Revenue and the Securities and Exchange Commission, the Court finds no legal obstacle not to direct [PIC] to submit a copy of the said documents to [PMO].

Lastly, on the motion of [PMO] to post counter bond, the Court finds the same to [be] without merit. The Court cannot allow, even if a bond is posted, [PMO] to commit an act which it has declared to be illegal. There is no premium for an illegal act.[25]

The dispositive portion of the RTC Order dated August 25, 2009 reads:

**WHEREFORE,** premises considered, the Court **GRANTS** the following motion:

1. Manifestation [and] Motion filed by [PIC] and hereby DELETES issues numbers 1 and 5 in pages 5 and 6 of its Pre-Trial Order of February 6, 2009.

2. The Omnibus Motion on requiring [PIC] to submit an accounting and financial report to the defendant [PMO], and submit to this Court a manifestation of its compliance thereto;

and **DENIES** the following:

1. The dissolution of the Writ of Preliminary Injunction for lack of merit.

2. The appointment of a representative of [PMO to the] Board of Directors for lack of merit.

3. The posting of counter bond for lack of merit.[26]

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[25] *Id*. at 70-71.

[26] *Id*. at 71.

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PMO assailed the RTC Order dated August 25, 2009 before the Court of Appeals *via* a Petition for *Certiorari*, averring that:

I.

PUBLIC RESPONDENT COMMITTED GRAVE ABUSE OF DISCRETION AMOUNTING TO LACK OR EXCESS OF JURISDICTION IN HOLDING THAT THE *IPSO FACTO* REVERSION CLAUSE IN THE ARDA IS A SPECIE[S] OF *PACTUM COMMISSORIUM* AND SUCH DISPOSITION IS A FINAL DETERMINATION OF THE COURT WHICH CAN ONLY BE QUESTIONED ON APPEAL; AND

II.

PUBLIC RESPONDENT COMMITTED GRAVE ABUSE OF DISCRETION AMOUNTING TO LACK OR EXCESS OF JURISDICTION IN DENYING [PMO'S] MOTION TO DISSOLVE THE WRIT OF PRELIMINARY INJUNCTION AND MOTION TO FILE A COUNTERBOND FOR THE DISSOLUTION THEREOF.[27]

The Court of Appeals, in its Decision dated January 31, 2011, disagreed with the finding of the RTC that the instant case involves a *pactum commissorium*, but still affirmed the denial by the RTC of the motion of PMO to dissolve the Writ of Preliminary Injunction issued in 2003.

According to the Court of Appeals, Section 8.02 of the ARDA does not constitute *pactum commissorium*:

> The elements of *pactum commissorium* are: (1) that there should be a pledge or mortgage wherein a property is pledged or mortgaged by way of security for the payment of the principal obligation; and (2) that there should be a stipulation for an automatic appropriation by the creditor of the thing pledged or mortgaged in the event of nonpayment of the principal obligation within the stipulated period.
>
> In the instant case, the subject ARDA basically pertains to the contract of sale of shares of stock. There was nothing given by way of pledge or mortgage in said contract, through which [PMO] could

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[27] *Id*. at 54-55.

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have appropriated the shares to itself should default in the payment thereof arise.

At this point, We have to agree with [PMO] that the ARDA is separate and distinct from the Pledge Agreement. The two agreements have separate terms and conditions, especially concerning the consequences of default. Under the ARDA, [PMO] may effect the *ipso facto* reversion of the title over the shares of stock of [PIC], without need of demand. On the other hand, under the Pledge Agreement, [PMO] may conduct a public or private sale of the shares of stock of [PIC], wherein it may opt to buy the same.

Furthermore, the first element of *pactum commissorium* only holds true under the Pledge Agreement while the second element with respect to the stipulation for automatic appropriation can be found under the ARDA. Thus, it is plainly irreconcilable how *pactum commissorium* can be made to apply in the present case, absent the two elements concurring in one contract.[28]

Notwithstanding its aforequoted pronouncements, the Court of Appeals still declared the *ipso facto* reversion clause in the ARDA invalid:

Nevertheless, the questioned provision on automatic reversion of shares still cannot be held valid. While the contracting parties may establish such stipulations, clauses, terms and conditions as they may deem convenient, they should, however, be not contrary to law, morals, good customs, public order, or public policy.

In a contract of sale involving shares of stock, ownership is deemed transferred upon the issuance of certificate of stock. Section 63 of the Corporation Code provides that "shares of stock so issued are personal property and may be transferred by delivery of the certificate or certificates indorsed by the owner or his attorney-in-fact or other person legally authorized to make the transfer."

The word "transfer," as contemplated in that particular section of the Corporation Code, means any act by which the share of stock of one person is vested in another, that is, he is divested and another acquires ownership of such stock.

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[28] *Id*. at 57.

Applying these principles, ownership over the stock of shares was already transferred to [PIC] when it was issued new certificates of stock. [PMO] cannot oblige [PIC] to automatically part with its ownership over the shares in favor of the former on the occasion of default or nonpayment, even if they have previously agreed upon the same. Such stipulation contained in the ARDA is contrary to law, hence, null and void.

It bears stressing that what is being declared null and void here is the "automatic reversion of shares" clause and not the provision for the rescission/cancellation of ARDA, as what has been impressed by [PMO] in its arguments.

Accordingly, [PIC] is entitled to be protected of his rights through the issuance of the Writ of Preliminary Injunction. And it is but proper to deny the dissolution of said writ. It should be of no moment that it has been in effect for several years now. Until the matter has been settled on whether [PIC] has substantially breached its obligation as to constitute default, then, the shares of stock cannot as yet be foreclosed and sold, in accordance with the terms and conditions of the Pledge Agreement, to satisfy [PMO's] alleged claims.[29] (Citations omitted.)

The Court of Appeals accordingly ruled in the end:

In view of all the foregoing, We simply cannot ascribe grave abuse of discretion to public respondent. While We may have a different take on the matter at hand, it is axiomatic that not every erroneous conclusion of law or fact is abuse of discretion.

**WHEREFORE,** premises considered, the instant petition is **DENIED**. The assailed Order dated 25 August 2009 issued by public respondent, Hon. Judge Gina M. Bibat-Palamos of RTC Makati, Branch 64, in Civil Case No. 03-114 is hereby **AFFIRMED**.[30] (Citation omitted.)

PIC filed a Motion for Partial Reconsideration, while PMO filed a Motion for Reconsideration of the Decision dated January 31, 2011 of the Court of Appeals, which the appellate court both denied in its Resolution dated November 18, 2011.

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[29] *Id*. at 57-58.

[30] *Id*. at 58-59.

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Hence, the instant Petitions.

In its Petition in G.R. No. 199420, PIC assigned the following errors on the part of the Court of Appeals:

I

THE HONORABLE COURT OF APPEALS COMMITTED GROSS ERROR, ACTED WITH GRAVE ABUSE OF DISCRETION WHEN IT DECIDED A QUESTION OF SUBSTANCE NOT IN ACCORD WITH LAW AND ESTABLISHED JURISPRUDENCE BY HOLDING THAT THE ESSENTIAL ELEMENTS OF *PACTUM COMMISSORIUM*, NAMELY, 1) THAT THERE SHOULD BE A [PLEDGE] OR [MORTGAGE] WHEREIN A PROPERTY PLEDGED OR MORTGAGED BY WAY OF SECURITY FOR THE PAYMENT OF THE PRINCIPAL OBLIGATION; AND 2) THAT THERE SHOULD BE A STIPULATION FOR AN AUTOMATIC APPROPRIATION BY THE CREDITOR OF THE THING PLEDGED OR MORTGAGED IN THE EVENT OF NONPAYMENT OF THE PRINCIPAL OBLIGATION WITHIN THE STIPULATED PERIOD, MUST CONCUR OR BE PRESENT IN ONE CONTRACT UNLIKE IN THE CASE AT BENCH WHERE ONE ELEMENT PURPORTEDLY APPEARS IN THE ARDA WHILE THE OTHER APPEARS IN THE PLEDGE AGREEMENT.

II

THE HONORABLE COURT OF APPEALS COMMITTED GROSS ERROR, ACTED WITH GRAVE ABUSE OF DISCRETION AND NOT IN ACCORD WITH LAW AND ESTABLISHED JURISPRUDENCE WHEN IT GAVE DUE COURSE AND RULED ON [PMO'S] PETITION FOR *CERTIORARI* ASSAILING THE ORDER ISSUED BY THE TRIAL COURT ON FEBRUARY 27, 2003 HOLDING THAT THE *IPSO FACTO* OR AUTOMATIC REVERSION TO PMO OF THE PLEDGED SHARES OF STOCK UNDER SECTION 8.02 OF THE ARDA IS *PACTUM COMMISSORIUM* WHEN SAID ORDER HAD LONG BECOME FINAL AND THEREFORE THE PETITION ASSAILING IT IS TIME-BARRED AND SHOULD HAVE BEEN DISMISSED OUTRIGHT.[31]

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[31] *Id*. at 24-25.

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On the other hand, PMO raised the following arguments in its Petition in G.R. No. 199432:

I

THE HONORABLE COURT OF APPEALS ERRED IN RULING THAT THE *IPSO FACTO* REVERSION CLAUSE OF THE ARDA IS CONTRARY TO LAW IN THE ABSENCE OF ANY LAW ALLEGEDLY VIOLATED BY THE SAID CLAUSE.

II

THE HONORABLE COURT OF APPEALS ERRED IN DENYING [PMO'S] PRAYER FOR THE DISSOLUTION OF THE WRIT OF PRELIMINARY INJUNCTION EVEN IF THE PURPOSE FOR WHICH IT WAS ISSUED HAD ALREADY BEEN MET AND ITS CONTINUED IMPLEMENTATION DEPRIVED [PMO] OF REMEDIES UNDER THE LAW AND THE ARDA.

III

THE DISSOLUTION OF THE WRIT AFTER THE LAPSE OF ALMOST NINE (9) YEARS IS IN ORDER AND IN THE INTEREST OF EQUITABLE JUSTICE.[32]

## RULING OF THE COURT

The allegations and arguments of PIC and PMO in their respective Petitions essentially boil down to two fundamental issues: (1) Whether Section 8.02 of the ARDA on *ipso facto* or automatic reversion of the PPC shares of stock to PMO in case of default by PIC constitutes *pactum commissorium*; and (2) Whether the Writ of Preliminary Injunction should be dissolved.

The Court resolves the first issue in the positive and the second issue in the negative.

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[32] *Rollo* (G.R. No. 199432), pp. 42-43.

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**Section 8.02 of the ARDA constitutes *pactum commissorium* and, thus, null and void for being contrary to Article 2088 of the Civil Code.**

Article 1305 of the Civil Code allows contracting parties to establish such stipulation, clauses, terms, and conditions as they may deem convenient, provided, however, that they are not contrary to law, morals, good customs, public order, or public policy.

*Pactum commissorium* is among the contractual stipulations that are deemed contrary to law. It is defined as "a stipulation empowering the creditor to appropriate the thing given as guaranty for the fulfillment of the obligation in the event the obligor fails to live up to his undertakings, without further formality, such as foreclosure proceedings, and a public sale."[33] It is explicitly prohibited under Article 2088 of the Civil Code which provides:

> ART. 2088. The creditor cannot appropriate the things given by way of pledge or mortgage, or dispose of them. Any stipulation to the contrary is null and void.

There are two elements for *pactum commissorium* to exist: (1) that there should be a pledge or mortgage wherein a property is pledged or mortgaged by way of security for the payment of the principal obligation; and (2) that there should be a stipulation for an automatic appropriation by the creditor of the thing pledged or mortgaged in the event of nonpayment of the principal obligation within the stipulated period.[34]

Both elements of *pactum commissorium* are present in the instant case: (1) By virtue of the Pledge Agreement dated May 2, 1997, PIC pledged its PPC shares of stock in favor of PMO as security for the fulfillment of the former's obligations under

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[33] *Edralin v. Philippine Veterans Bank*, G.R. No. 168523, March 9, 2011, 645 SCRA 75, 89.

[34] *Spouses Uy Tong and Kho Po Giok vs. CA*, 244 Phil. 403, 408 (1988).

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the ARDA dated May 10, 1996 and the Pledge Agreement itself; and (2) There is automatic appropriation as under Section 8.02 of the ARDA, in the event of default by PIC, title to the PPC shares of stock shall *ipso facto* revert from PIC to PMO without need of demand.

The Court of Appeals, in ruling that there is no *pactum commissorium*, adopted the position of PMO that the ARDA and the Pledge Agreement are entirely separate and distinct contracts. Neither contract contains both elements of *pactum commissorium*: the ARDA solely has the second element, while the Pledge Agreement only has the first element.

The Court disagrees.

In *Blas v. Angeles-Hutalla*,[35] the Court recognized that the agreement of the parties may be embodied in only one contract or in two or more separate writings. In case of the latter, the writings of the parties should be read and interpreted together in such a way as to render their intention effective.

The agreement between PMO and PIC is the sale of the PPC shares of stock by the former to the latter, to be secured by a pledge on the very same shares of stock. The ARDA and the Pledge Agreement herein, although executed in separate written instruments, are integral to one another. On one hand, Section 2.04 of the ARDA explicitly requires the execution of a pledge agreement as security for the payment by PIC of the purchase price for the PPC shares of stock and receivables, and even provides the form for said pledge agreement in Annex A thereof. Section 2.07 of the ARDA also states that the closing of the sale and purchase of the PPC shares of stock and receivables shall take place on the same date that PIC shall execute and deliver the pledge agreement, together with the certificates of shares of stock, to PMO. On the other hand, the "Whereas Clauses" of the Pledge Agreement expressly mentions the ARDA and explains that the Pledge Agreement is being executed to secure payment by PIC of the purchase price and all other amounts due to PMO under the ARDA, as well as the performance by

[35] 482 Phil. 485, 505 (2004).

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PIC of its other obligations under the ARDA and the Pledge Agreement itself. Clearly, it was the intention of the parties to enter into and execute both contracts for a complete effectuation of their agreement.

To reiterate, the Pledge Agreement secures, for the benefit of PMO, the performance by PIC of its obligations under both the ARDA and the Pledge Agreement itself. It is with the execution of the Pledge Agreement that PIC turned over possession of its certificates of shares of stock in PPC to PMO. As the RTC pertinently observed in its Order dated June 19, 2003, there had already been a shift in the relations of PMO and PIC, from mere seller and buyer, to creditor-pledgee and debtor-pledgor. Having enjoyed the security and benefits of the Pledge Agreement, PMO cannot now insist on applying Section 8.02 of the ARDA and conveniently and arbitrarily exclude and/or ignore the Pledge Agreement so as to evade the prohibition against *pactum commissorium*.

More importantly, the Court, in determining the existence of *pactum commissorium*, had focused more on the evident intention of the parties, rather than the formal or written form. In *A. Francisco Realty and Development Corporation v. Court of Appeals*,[36] therein petitioner similarly denied the existence of *pactum commissorium* because the proscribed stipulation was found in the promissory note and not in the mortgage deed. The Court held that:

> The contention is patently without merit. To sustain the theory of petitioner would be to allow a subversion of the prohibition in Art. 2088.
>
> In *Nakpil v. Intermediate Appellate Court*, which involved the violation of a constructive trust, no deed of mortgage was expressly executed between the parties in that case. Nevertheless, this Court ruled that an agreement whereby property held in trust was ceded to the trustee upon failure of the beneficiary to pay his debt to the former as secured by the said property was void for being a *pactum commissorium*. It was there held:

[36] 358 Phil. 833, 845-847 (1998).

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> The arrangement entered into between the parties, whereby Pulong Maulap was to be "considered sold to him (respondent) x x x" in case petitioner fails to reimburse Valdes, must then be construed as tantamount to a *pactum commissorium* which is expressly prohibited by Art. 2088 of the Civil Code. For, there was to be automatic appropriation of the property by Valdez in the event of failure of petitioner to pay the value of the advances. Thus, contrary to respondent's manifestations, all the elements of a *pactum commissorium* were present: there was a creditor-debtor relationship between the parties; the property was used as security for the loan; and, there was automatic appropriation by respondent of Pulong Maulap in case of default of petitioner.

Similarly, the Court has struck down such stipulations as contained in deeds of sale purporting to be *pacto de retro* sales but found actually to be equitable mortgages.

> It has been consistently held that the presence of even one of the circumstances enumerated in Art. 1602 of the New Civil Code is sufficient to declare a contract of sale with right to repurchase an equitable mortgage. This is so because *pacto de retro* sales with the stringent and onerous effects that accompany them are not favored. In case of doubt, a contract purporting to be a sale with right to repurchase shall be construed as an equitable mortgage.
>
> Petitioner, to prove her claim, cannot rely on the stipulation in the contract providing that complete and absolute title shall be vested on the vendee should the vendors fail to redeem the property on the specified date. Such stipulation that the ownership of the property would automatically pass to the vendee in case no redemption was effected within the stipulated period is void for being a *pactum commissorium* which enables the mortgagee to acquire ownership of the mortgaged property without need of foreclosure. Its insertion in the contract is an avowal of the intention to mortgage rather that to sell the property.

Indeed, in *Reyes v. Sierra*, this Court categorically ruled that a mortgagee's mere act of registering the mortgaged property in his own name upon the mortgagor's failure to redeem the property

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amounted to the exercise of the privilege of a mortgagee in a *pactum commissorium*.

> Obviously, from the nature of the transaction, applicant's predecessor-in-interest is a mere mortgagee, and ownership of the thing mortgaged is retained by Basilia Beltran, the mortgagor. The mortgagee, however, may recover the loan, although the mortgage document evidencing the loan was nonregistrable being a purely private instrument. Failure of mortgagor to redeem the property does not automatically vest ownership of the property to the mortgagee, which would grant the latter the right to appropriate the thing mortgaged or dispose of it. This violates the provision of Article 2088 of the New Civil Code, which reads:
>
> > The creditor cannot appropriate the things given by way of pledge or mortgage, or dispose by them. Any stipulation to the contrary is null and void.
>
> The act of applicant in registering the property in his own name upon mortgagor's failure to redeem the property would amount to a *pactum commissorium* which is against good morals and public policy.

Thus, in the case at bar, the stipulations in the promissory notes providing that, upon failure of respondent spouses to pay interest, ownership of the property would be automatically transferred to petitioner A. Francisco Realty and the deed of sale in its favor would be registered, are in substance a *pactum commissorium*. They embody the two elements of *pactum commissorium* as laid down in *Uy Tong v. Court of Appeals*, x x x. (Citations omitted.)

Appreciating the ARDA together with the Pledge Agreement, the Court can only conclude that Section 8.02 of the ARDA constitutes *pactum commissorium* and, therefore, null and void.

PMO though insists that there is no valid Pledge Agreement, arguing that PIC could not have validly pledged the PPC shares of stock because it is not yet the absolute owner of said shares. According to PMO, the sale of the PPC shares of stock to PIC is subject to the resolutory condition of nonpayment by PIC of the installments due on the purchase price.

Again, the Court is unconvinced.

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Among the requirements of a contract of pledge is that the pledgor is the absolute owner of the thing pledged.[37] Based on the provisions of the ARDA, ownership of the PPC shares of stock had passed on to PIC, hence, enabling PIC to pledge the very same shares to PMO. In accordance with Section 2.07(a)(1) and 2.07(a)(2) of the ARDA, PMO had transferred to PIC all rights, title, and interests in and to the PPC shares of stock, and delivered to PIC the certificates for said shares for cancellation and replacement of new certificates already in the name of PIC. In addition, Section 2.07(b) of the ARDA explicitly declares that PIC as buyer shall exercise all the rights, including the right to vote, of a shareholder in respect of the PPC shares of stock.

PMO cannot maintain that the ownership of the PPC shares of stock did not pass on to PIC, but in the same breath claim that non-payment by PIC of the installments due on the purchase price is a resolutory condition for the contract of sale – these two arguments are actually contradictory. As the Court clearly explained in *Heirs of Paulino Atienza v. Espidol*[38]:

> Regarding the **right to cancel the contract for nonpayment of an installment**, there is need to initially determine if what the parties had was a contract of sale or a contract to sell. **In a contract of sale, the title to the property passes to the buyer upon the delivery of the thing sold.** In a contract to sell, on the other hand, the ownership is, by agreement, retained by the seller and is not to pass to the vendee until full payment of the purchase price**. In the contract of sale, the buyer's nonpayment of the price is a negative resolutory condition;** in the contract to sell, the buyer's full payment of the price is a positive suspensive condition to the coming into effect of the agreement. **In the first case, the seller has lost and cannot recover the ownership of the property unless he takes action to set aside the contract of sale.** In the second case, the title simply remains in the seller if the buyer does not comply with the condition precedent of making payment at the time specified in the contract. x x x. (Emphases supplied, citation omitted.)

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[37] *Calibo, Jr. v. Court of Appeals*, 403 Phil. 340, 344 (2001).

[38] G.R. No. 180665, August 11, 2010, 628 SCRA 256, 262.

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So that it could invoke the resolutory condition of nonpayment of an installment, PMO must necessarily concede that its contract with PIC was a one of sale and that ownership of the PPC shares of stock had indeed passed on to PIC. And even then, having lost ownership of the shares, PMO cannot automatically recover the same without taking steps to set aside the contract of sale.

Moreover, the general rule is that in the absence of a stipulation, a party cannot unilaterally and extrajudicially rescind a contract. A party must invoke the right to rescind a contract judicially.[39] It is also settled that the rescission of a contract based on Article 1191 of the Civil Code requires mutual restitution to bring back the parties to their original situation prior to the inception of the contract. Rescission creates the obligation to return the object of the contract. It can be carried out only when the one who demands rescission can return whatever he may be obliged to restore.[40]

Even though PMO had previously acknowledged the need for restitution or restoration following rescission, it also qualified that such restitution or restoration shall still be "subject x x x to the fair determination of the amount to be restored as may be deemed reasonable and substantiated."[41]

Section 8.02 of the ARDA provides for the *ipso facto* reversion of the pledged shares of PIC to PMO in case of default on the part of the former, which as explained above, is prohibited by Article 2088 of the Civil Code. The said Section does not mention the broader concept of rescission of the entire ARDA.

In its Petition in G.R. No. 199432, PMO is asking the Court, among other things, to already declare the ARDA rescinded. The Court cannot grant or deny such prayer at this point for there are questions of fact and law which are still under litigation before the RTC.

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[39] *EDS Manufacturing, Inc. v. Healthcheck International, Inc.*, G.R. No. 162802, October 9, 2013, 707 SCRA 133, 143.

[40] *Spouses Velarde v. Court of Appeals*, 413 Phil. 360, 375 (2001).

[41] *Rollo* (G.R. No. 199432), p. 285, Motion for Reconsideration (Re: Order dated February 27, 2003) of PMO.

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**There is no basis for dissolving the Writ of Preliminary Injunction.**

The Court emphasizes that the Writ of Preliminary Injunction was granted in the RTC Order dated February 27, 2003; and the Motion for Reconsideration of the issuance of said Writ filed by the PMO was denied in the RTC Order dated June 19, 2003 – both of which are interlocutory orders. Under Rule 65 of the Rules of Court, the PMO only had 60 days from notice to file with the Court of Appeals a petition for *certiorari* assailing said orders. However, PMO did not file such a petition and lost the right to avail itself of the remedy.

PMO, in challenging the RTC Order dated August 25, 2009, cannot be allowed to revive the issues of *pactum commissorium* and the arbitration clause, together with its opposition to the Writ of Preliminary Injunction, which were already settled and ruled upon six years before in the RTC Orders dated February 27, 2003 and June 19, 2003. The removal of said issues from those submitted for trial before the RTC is thus justified. That the RTC issued the aforementioned Orders of 2003 based only on initial and incomplete evidence is incorrect. The issues of *pactum commissorium* and arbitration clause are questions of law that do not require the review or evaluation of evidence. The RTC, before issuing said Orders of 2003, conducted hearings and required the submission of pleadings, so the parties were given the opportunity to present their arguments on said questions of law. In particular, the ruling of the RTC that Section 8.02 of the ARDA constitutes *pactum commissorium*, cannot be set aside and the Writ of Injunction issued based on such ruling cannot be dissolved, even if there be changes in the factual circumstances of the parties, for as long as the applicable law remains the same.

There are still several remaining issues in the Pre-Trial Order dated February 6, 2009 that the RTC needs to resolve, among others, the alleged default under the ARDA. They involve both questions of fact and law, so their resolution requires further hearings for presentation of evidence by the parties. Hence, PMO cannot claim pre-judgment of its case with the issuance

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by the RTC of the Orders dated February 27, 2003 and June 19, 2003. Despite the declaration that Section 8.02 of the ARDA is null and void as it constitutes *pactum commissorium*, PMO and PIC shall have the opportunity to thresh-out other issues between them which are not resolved in these cases, such as the issue of default, during the trial on the merits before the RTC.

**WHEREFORE,** premises considered, the Court:

(1) **GRANTS** the Petition for Review of PIC in G.R. No. 199420 by declaring that Section 8.02 of the ARDA constitutes *pactum commissorium* and, thus, null and void;

(2) **DENIES** the Petition for Review of PMO in G.R. No. 199432 for lack of merit; and

(3) **DIRECTS** the RTC to resolve Civil Case No. 03-114 with utmost dispatch.

**SO ORDERED.**

*Sereno, C.J. (Chairperson), Bersamin*, *Perez*, and *Mendoza*,[*] *JJ.*, concur.

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**THIRD DIVISION**

[G.R. Nos. 212536-37. August 27, 2014]

**COMMISSIONER OF INTERNAL REVENUE and COMMISSIONER OF CUSTOMS,** *petitioners, vs.* **PHILIPPINE AIRLINES, INC.,** *respondent.*

**SYLLABUS**

**1. STATUTORY CONSTRUCTION; A LATER LAW, GENERAL IN TERMS AND NOT EXPRESSLY REPEALING OR AMENDING A PRIOR SPECIAL LAW,**

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[*] Per Special Order No. 1754 dated August 18, 2014.