Republic of the Philippines
Supreme Court
Manila

SECOND DIVISION

THE WELLEX GROUP, INC., Petitioner,	**G.R. No. 167519**
	Present:
- versus -	CARPIO, *J., Chairperson,* VELASCO, JR.,* DEL CASTILLO, MENDOZA, and LEONEN, *JJ.*
U-LAND AIRLINES, CO., LTD., Respondent.	**Promulgated:** 14 JAN 2015

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DECISION

LEONEN, *J.*:

This is a Petition[1] for Review on Certiorari under Rule 45 of the Rules of Court. The Wellex Group, Inc. (Wellex) prays that the Decision[2] dated July 30, 2004 of the Court of Appeals in CA-G.R. CV No. 74850 be reversed and set aside.[3]

The Court of Appeals affirmed the Decision[4] of the Regional Trial Court, Branch 62 of Makati City in Civil Case No. 99-1407. The Regional Trial Court rendered judgment in favor of U-Land Airlines, Co., Ltd. (U-Land) and ordered the rescission of the Memorandum of Agreement[5] between Wellex and U-Land.[6]

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* Designated acting member per S.O. No. 1910 dated January 12, 2015.
1 *Rollo*, pp. 12–43.
2 Id. at 46–54.
3 Id. at 40.
4 Id. at 89–102.
5 Id. at 59–62.
6 Id. at 102.

Wellex is a corporation established under Philippine law and it maintains airline operations in the Philippines.[7] It owns shares of stock in several corporations including Air Philippines International Corporation (APIC), Philippine Estates Corporation (PEC), and Express Savings Bank (ESB).[8] Wellex alleges that it owns all shares of stock of Air Philippines Corporation (APC).[9]

U-Land Airlines Co. Ltd. (U-Land) "is a corporation duly organized and existing under the laws of Taiwan, registered to do business . . . in the Philippines."[10] It is engaged in the business of air transportation in Taiwan and in other Asian countries.[11]

On May 16, 1998, Wellex and U-Land entered into a Memorandum of Agreement[12] (First Memorandum of Agreement) to expand their respective airline operations in Asia.[13]

Terms of the First Memorandum of Agreement

The preambular clauses of the First Memorandum of Agreement state:

> WHEREAS, U-LAND is engaged in the business of airline transportation in Taiwan, Philippines and/or in other countries in the Asian region, and desires to expand its operation and increase its market share by, among others, pursuing a long-term involvement in the growing Philippine airline industry;
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> WHEREAS, WELLEX, on the other hand, has current airline operation in the Philippines through its majority-owned subsidiary Air Philippines International Corporation and the latter's subsidiary, Air Philippines Corporation, and in like manner also desires to expand its operation in the Asian regional markets, a Memorandum of Agreement on _____, a certified copy of which is attached hereto as Annex "A" and is hereby made an integral part hereof, which sets forth, among others, the basis for WELLEX's present ownership of shares in Air Philippines International Corporation.
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> WHEREAS, the parties recognize the opportunity to develop a long-term profitable relationship by combining such of their respective resources in an expanded airline operation as well as in property

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7 Id. at 59.
8 Id. at 59-60.
9 Id. at 63.
10 Id. at 14.
11 Id. at 15.
12 There are two memoranda of agreement. We refer to the Memorandum of Agreement between Wellex and U-Land as the First Memorandum of Agreement. We then refer to Annex "A" or the Memorandum of Agreement among Wellex, APIC, and APC as the Second Memorandum of Agreement.
13 Id. at 59.

> development and in other allied business activities in the Philippines, and desire to set forth herein the basic premises and their understanding with respect to their joint cooperation and undertakings.[14]

In the First Memorandum of Agreement, Wellex and U-Land agreed to develop a long-term business relationship through the creation of joint interest in airline operations and property development projects in the Philippines.[15] This long-term business relationship would be implemented through the following transactions, stated in Section 1 of the First Memorandum of Agreement:

> (a) U-LAND shall acquire from WELLEX, shares of stock of AIR PHILIPPINES INTERNATIONAL CORPORATION ("APIC") equivalent to at least 35% of the outstanding capital stock of APIC, but in any case, not less than 1,050,000,000 shares . . . [;]
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> (b) U-LAND shall acquire from WELLEX, shares of stock of PHILIPPINE ESTATES CORPORATION ("PEC") equivalent to at least 35% of the outstanding capital stock of PEC, but in any case, not less than 490,000,000 shares . . . [;]
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> (c) U-LAND shall enter into a joint development agreement with PEC . . . [; and]
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> (d) U-LAND shall be given the option to acquire from WELLEX shares of stock of EXPRESS SAVINGS BANK ("ESB") up to 40% of the outstanding capital stock of ESB . . . under terms to be mutually agreed.[16]

I. Acquisition of APIC and PEC shares

The First Memorandum of Agreement stated that within 40 days from its execution date, Wellex and U-Land would execute a share purchase agreement covering U-Land's acquisition of the shares of stock of both APIC (APIC shares) and PEC (PEC shares).[17] In this share purchase agreement, U-Land would purchase from Wellex its APIC shares and PEC shares.[18]

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14 Id.
15 Id.
16 Id. at 59–60.
17 Id. at 60.
18 Id at 59–60. In the First Memorandum of Agreement, the second preambular clause states that Wellex has a "majority-owned subsidiary Air Philippines International Corporation and the latter's subsidiary, Air Philippines Corporation[.]"
Section 1 of the First Memorandum of Agreement reads:
1. Basic Agreement. - The parties agree to develop a long-term business relationship initially through the creation of joint interest in airline operations as well as in property development projects in the Philippines to be implemented as follows:
(a) U-LAND shall acquire from WELLEX, shares of stock of AIR PHILIPPINES INTERNATIONAL CORPORATION ("APIC") equivalent to at least 35% of the outstanding capital stock of APIC, but in any case, not less than 1,050,000,000 shares (the "APIC Shares").
(b) U-LAND shall acquire from WELLEX, shares of stock of PHILIPPINE ESTATES CORPORATION ("PEC") equivalent to at least 35% of the outstanding capital stock of PEC, but in

Wellex and U-Land agreed to an initial purchase price of □0.30 per share of APIC and □0.65 per share of PEC. However, they likewise agreed that the final price of the shares of stock would be reflected in the actual share purchase agreement.[19]

Both parties agreed that the purchase price of APIC shares and PEC shares would be paid upon the execution of the share purchase agreement and Wellex's delivery of the stock certificates covering the shares of stock. The transfer of APIC shares and PEC shares to U-Land was conditioned on the full remittance of the final purchase price as reflected in the share purchase agreement. Further, the transfer was conditioned on the approval of the Securities and Exchange Commission of the issuance of the shares of stock and the approval by the Taiwanese government of U-Land's acquisition of these shares of stock.[20]

Thus, Section 2 of the First Memorandum of Agreement reads:

> 2. Acquisition of APIC and PEC Shares. - Within forty (40) days from date hereof (unless extended by mutual agreement), U-LAND and WELLEX shall execute a Share Purchase Agreement ("SHPA") covering the acquisition by U-LAND of the APIC Shares and PEC Shares (collectively, the "Subject Shares"). Without prejudice to any subsequent agreement between the parties, the purchase price for the APIC Shares to be reflected in the SHPA shall be THIRTY CENTAVOS (P0.30) per share and that for the PEC Shares at SIXTY FIVE CENTAVOS (P0.65) per share.
>
> The purchase price for the Subject Shares as reflected in the SHPA shall be paid in full upon execution of the SHPA against delivery of the Subject Shares. The parties may agree on such other terms and conditions governing the acquisition of the Subject Shares to be provided in a separate instrument.
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> The transfer of the Subject Shares shall be effected to U-LAND provided that: (i) the purchase price reflected in the SHPA has been fully paid; (ii) the Philippine Securities & Exchange Commission (SEC) shall have approved the issuance of the Subject Shares; and (iii) any required approval by the Taiwanese government of the acquisition by U-LAND of the Subject Shares shall likewise have been obtained.[21]

II. Operation and management of APIC/PEC/APC

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any case, not less than 490,000,000 shares (the "PEC Shares").

19 Id. at 60.

20 Id.

21 Id.

U-Land was "entitled to a proportionate representation in the Board of Directors of APIC and PEC in accordance with Philippine law."[22] Operational control of APIC and APC would be exercised jointly by Wellex and U-Land "on the basis of mutual agreement and consultations."[23] The parties intended that U-Land would gain primary control and responsibility for the international operations of APC.[24] Wellex manifested that APC is a subsidiary of APIC in the second preambular clause of the First Memorandum of Agreement.[25]

Section 3 of the First Memorandum of Agreement reads:

> 3. Operation/Management of APIC/APC. - U-LAND shall be entitled to a proportionate representation in the Board of Directors of APIC and PEC in accordance with Philippine law. For this purpose, WELLEX shall cause the resignation of its nominated Directors in APIC and PEC to accommodate U-LAND's pro rata number of Directors. Subject to applicable Philippine law and regulations, operational control of APIC and Air Philippines Corporation ("APC") shall be lodged jointly to WELLEX and U-LAND on the basis of mutual agreement and consultations. Further, U-LAND may second technical and other consultants into APIC and/or APC with the view to increasing service, productivity and efficiency, identifying and implementing profit-service opportunities, developing technical capability and resources, and installing adequate safety systems and procedures. In addition, U-LAND shall arrange for the lease by APC of at least three (3) aircrafts owned by U-LAND under such terms as the parties shall mutually agree upon. It is the intent of the parties that U-LAND shall have primary control and responsibility for APC's international operations.[26]

III. Entering into and funding a joint development agreement

Wellex and U-Land also agreed to enter into a joint development agreement simultaneous with the execution of the share purchase agreement. The joint development agreement shall cover housing and other real estate development projects.[27]

U-Land agreed to remit the sum of US$3 million not later than May 22, 1998. This sum was to serve as initial funding for the development projects that Wellex and U-Land were to undertake pursuant to the joint

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22 Id.
23 Id.
24 Id. at 61.
25 Id. at 59.
26 Id. at 60–61. First Memorandum of Agreement, sec. 4 provides:
U-LAND shall, not later than May 22, 1998 remit the sum of US$3.0 million as initial funding for the aforesaid development projects against delivery by WELLEX of 57,000,000 shares of PEC as security for said amount in accordance with Section 9 below. (*Rollo*, p. 61.)
27 Id. at 61.

development agreement. In exchange for the US$3 million, Wellex would deliver stock certificates covering 57,000,000 PEC shares to U-Land.[28]

The execution of a joint development agreement was also conditioned on the execution of a share purchase agreement.[29]

Section 4 of the First Memorandum of Agreement reads:

> 4. Joint Development Agreement with PEC. – Simultaneous with the execution of the SHPA, U-LAND and PEC shall execute a joint development agreement ("JDA") to pursue property development projects in the Philippines. The JDA shall cover specific housing and other real estate development projects as the parties shall agree. All profits derived from the projects covered by the JDA shall be shared equally between U-LAND and PEC. U-LAND shall, not later than May 22, 1998, remit the sum of US$3.0 million as initial funding for the aforesaid development projects against delivery by WELLEX of 57,000,000 shares of PEC as security for said amount in accordance with Section 9 below.[30]

In case of conflict between the provisions of the First Memorandum of Agreement and the provisions of the share purchase agreement or its implementing agreements, the terms of the First Memorandum of Agreement would prevail, unless the parties specifically stated otherwise or the context of any agreement between the parties would reveal a different intent.[31] Thus, in Section 6 of the First Memorandum of Agreement:

> 6. Primacy of Agreement. – It is agreed that in case of conflict between the provisions of this Agreement and those of the SHPA and the implementing agreements of the SHPA, the provisions of this Agreement shall prevail, unless the parties specifically state otherwise, or the context clearly reveal a contrary intent.[32]

Finally, Wellex and U-Land agreed that if they were unable to agree on the terms of the share purchase agreement and the joint development agreement within 40 days from signing, then the First Memorandum of Agreement would cease to be effective.[33]

In case no agreements were executed, the parties would be released from their respective undertakings, except that Wellex would be required to refund within three (3) days the US$3 million given as initial funding by U-Land for the development projects. If Wellex was unable to refund the

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28 Id.
29 Id.
30 Id.
31 Id.
32 Id.
33 Id.

US$3 million to U-Land, U-Land would have the right to recover on the 57,000,000 PEC shares that would be delivered to it.[34] Section 9 of the First Memorandum of Agreement reads:

> 9. Validity. - In the event the parties are unable to agree on the terms of the SHPA and/or the JDA within forty (40) days from date hereof (or such period as the parties shall mutually agree), this Memorandum of Agreement shall cease to be effective and the parties released from their respective undertakings herein, except that WELLEX shall refund the US$3.0 million provided under Section 4 within three (3) days therefrom, otherwise U-LAND shall have the right to recover on the 57,000,000 PEC shares delivered to U-LAND under Section 4.[35]

The First Memorandum of Agreement was signed by Wellex Chairman and President William T. Gatchalian (Mr. Gatchalian) and U-Land Chairman Ker Gee Wang (Mr. Wang) on May 16, 1998.[36]

Annex "A" or the Second Memorandum of Agreement

Attached and made an integral part of the First Memorandum of Agreement was Annex "A," as stated in the second preambular clause. It is a document denoted as a "Memorandum of Agreement" entered into by Wellex, APIC, and APC.[37]

The Second Memorandum of Agreement states:

> This Memorandum of Agreement, made and executed this ___th day of _____ at Makati City, by and between:
>
> **THE WELLEX GROUP, INC.,** a corporation duly organized and existing under the laws of the Philippines, with offices at 22F Citibank Tower, 8741 Paseo de Roxas, Makati City (hereinafter referred to as "TWGI"),
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> **AIR PHILIPPINES INTERNATIONAL CORPORATION** (formerly **FORUM PACIFIC, INC.**), likewise a corporation duly organized and existing under the laws of the Philippines, with offices at 8F Rufino Towers, Ayala Avenue, Makati City (hereinafter referred to as "APIC"),
>
> - and -

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34 Id.
35 Id.
36 Id. at 59 and 61.
37 Id. at 63.

AIR PHILIPPINES CORPORATION, corporation duly organized and existing under the laws of the Philippines, with offices at Multinational Building, Ayala Avenue, Makati City (hereinafter referred to as "APC").

W I T N E S S E T H: That -

WHEREAS, TWGI is the registered and beneficial owner, or has otherwise acquired _____ (illegible in *rollo*) *rights to the entire issued and outstanding capital stock (the "APC SHARES") of AIR PHILIPPINES CORPORATION ("APC") and has made stockholder advances to APC for the* _____ (illegible in *rollo*) *of aircraft, equipment and for working capital used in the latter's operations (the "*_____ (illegible in *rollo*) *ADVANCES").*

WHEREAS, APIC desires to obtain full ownership and control of APC, including all of _____ (illegible in *rollo*) *assets, franchise, goodwill and operations, and for this purpose has offered to acquire the* _____ (illegible in *rollo*) *SHARES of TWGI in APC, including the APC ADVANCES due to TWGI from APC, with* _____ (illegible in *rollo*) *of acquiring all the assets, franchise, goodwill and operations of APC; and TWGI has* _____ (illegible in *rollo*) *to the same in consideration of the conveyance by APIC to TWGI of certain investments,* _____ (illegible in *rollo*) *issuance of TWGI of shares of stock of APIC in exchange for said APC SHARES and the* _____ (illegible in *rollo*) *ADVANCES, as more particularly described hereunder.*

NOW, THEREFORE, the parties agree as follows:

1. TWGI agrees to transfer the APC ADVANCES in APIC in exchange for the _____ (illegible in *rollo*) by APIC to TWGI of investment shares of APIC in Express Bank, PetroChemical _____ (illegible in *rollo*) of Asia Pacific, Republic Resources & Development Corporation and Philippine _____ (illegible in *rollo*) Corporation (the "APIC INVESTMENTS").

2. TWGI likewise agrees to transfer the APC SHARES to APIC in exchange solely _____ (illegible in *rollo*) the issuance by APIC of One Billion Seven Hundred Ninety Seven Million Eight Hundred Fifty Seven Thousand Three Hundred Sixty Four (1,797,857,364) shares of its capital stock of a _____ (illegible in *rollo*) value of P1.00 per share (the "APIC SHARES"), taken from the currently authorized but _____ (illegible in *rollo*) shares of the capital stock of APIC, as well as from the increase in the authorized capital _____ (illegible in *rollo*) of APIC from P2.0 billion to P3.5 billion.

3. It is the basic understanding of the parties hereto that the transfer of the APC _____ (illegible in *rollo*) as well as the APC ADVANCES to APIC shall be intended to enable APIC to obtain _____ (illegible in *rollo*) and control of APC, including all of APC's assets, franchise, goodwill and _____ (illegible in *rollo*).

4. Unless the parties agree otherwise, the effectivity of this Agreement and transfers _____ (illegible in *rollo*) APC ADVANCES in

> exchange for the APIC INVESTMENTS, and the transfer of the _____ (illegible in *rollo*) SHARES in exchange for the issuance of new APIC SHARES, shall be subject to _____ (illegible in *rollo*) due diligence as the parties shall see fit, and the condition subsequent that the _____ (illegible in *rollo*) for increase in the authorized capital stock of the APIC from P2.0 billion to P3.5 _____ (illegible in *rollo*) shall have been approved by the Securities and Exchange Commission.
>
> IN WITNESS WHEREOF, the parties have caused these presents to be signed on the date _____ (illegible in *rollo*) first above written.[38] (Emphasis supplied)

This Second Memorandum of Agreement was allegedly incorporated into the First Memorandum of Agreement as a "disclosure to [U-Land] [that] . . . [Wellex] was still in the process of acquiring and consolidating its title to shares of stock of APIC."[39] It "included the terms of a share swap whereby [Wellex] agreed to transfer to APIC its shareholdings and advances to APC in exchange for the issuance by APIC of shares of stock to [Wellex]."[40]

The Second Memorandum of Agreement was signed by Mr. Gatchalian, APIC President Salud,[41] and APC President Augustus C. Paiso.[42] It was not dated, and no place was indicated as the place of signing.[43] It was not notarized either, and no other witnesses signed the document.[44]

The 40-day period lapsed on June 25, 1998.[45] Wellex and U-Land were not able to enter into any share purchase agreement although drafts were exchanged between the two.

Despite the absence of a share purchase agreement, U-Land remitted to Wellex a total of US$7,499,945.00.[46] These were made in varying amounts and through the issuance of post-dated checks.[47] The dates of remittances were the following:

Date	Amount (in US$)
June 30, 1998	990,000.00
July 2, 1998	990,000.00
	20,000.00
July 30, 1998	990,000.00

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38 Id. at 63–64.
39 Id. at 222.
40 Id.
41 First name is illegible in *rollo*.
42 Id. at 64.
43 Id. at 63–65.
44 Id. at 65.
45 Id. at 80.
46 Id. at 49.
47 Id. at 97.

	490,000.00
	490,000.00
August 1, 1998	990,000.00
	490,000.00
	490,000.00
August 3, 1998	990,000.00
	70,000.00
September 25, 1998	399,972.50
	99, 972.50
Total	US$7,499,945.00[48]

Wellex acknowledged the receipt of these remittances in a confirmation letter addressed to U-Land dated September 30, 1998.[49]

According to Wellex, the parties agreed to enter into a security arrangement. If the sale of the shares of stock failed to push through, the partial payments or remittances U-Land made were to be secured by these shares of stock and parcels of land.[50] This meant that U-Land could recover the amount it paid to Wellex by selling these shares of stock and land titles or using them to generate income.

Thus, after the receipt of US$7,499,945.00, Wellex delivered to U-Land stock certificates representing 60,770,000 PEC shares and 72,601,000 APIC shares.[51] These were delivered to U-Land on July 1, 1998, September 1, 1998, and October 1, 1998.[52]

In addition, Wellex delivered to U-Land Transfer Certificates of Title (TCT) Nos. T-216769, T-216771, T-228231, T-228227, T-211250, and T-216775 covering properties owned by Westland Pacific Properties Corporation in Bulacan; and TCT Nos. T-107306, T-115667, T-105910, T-120250, T-1114398, and T-120772 covering properties owned by Rexlon Realty Group, Inc.[53] On October 1, 1998,[54] U-Land received a letter from Wellex, indicating a list of stock certificates that the latter was giving to the former by way of "security."[55]

Despite these transactions, Wellex and U-Land still failed to enter into the share purchase agreement and the joint development agreement.

In the letter[56] dated July 22, 1999, 10 months[57] after the last formal

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48 Id. at 324.
49 Id. at 96 and 147.
50 Id. at 412.
51 Id. at 49.
52 Id. at 90.
53 Id. at 49.
54 Id. at 90.
55 Id. at 90–91 and 96.
56 Id. at 66–67.

communication between the two parties, U-Land, through counsel, demanded the return of the US$7,499,945.00.[58] This letter was sent 14 months after the signing of the First Memorandum of Agreement.

Counsel for U-Land claimed that "[Wellex] ha[d] unjustifiably refused to enter into the. . . Share Purchase Agreement."[59] As far as U-Land was concerned, the First Memorandum of Agreement was no longer in effect, pursuant to Section 9.[60] As such, U-Land offered to return all the stock certificates covering APIC shares and PEC shares as well as the titles to real property given by Wellex as security for the amount remitted by U-Land.[61]

Wellex sent U-Land a letter[62] dated August 2, 1999, which refuted U-Land's claims. Counsel for Wellex stated that the two parties carried out several negotiations that included finalizing the terms of the share purchase agreement and the terms of the joint development agreement. Wellex asserted that under the joint development agreement, U-Land agreed to remit the sum of US$3 million by May 22, 1998 as initial funding for the development projects.[63]

Wellex further asserted that it conducted extended discussions with U-Land in the hope of arriving at the final terms of the agreement despite the failure of the remittance of the US$3 million on May 22, 1998.[64] That remittance pursuant to the joint development agreement "would have demonstrated [U-Land's] good faith in finalizing the agreements."[65]

Wellex averred that, "[s]ave for a few items, [Wellex and U-Land] virtually agreed on the terms of both [the share purchase agreement and the joint development agreement.]"[66] Wellex believed that the parties had already "gone beyond the 'intent' stage of the [First Memorandum of Agreement] and [had already] effected partial implementation of an over-all agreement."[67] U-Land even delivered a total of 12 post-dated checks to Wellex as payment for the APIC shares and PEC shares.[68] "[Wellex] on the other hand, had [already] delivered to [U-Land] certificates of stock of APEC [sic] and PEC as well as various land titles to cover actual remittances."[69] Wellex alleged that the agreements were not finalized because U-Land was "forced to suspend operations because of financial

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57 Id. at 226.
58 Id. at 66.
59 Id.
60 Id. at 66–67.
61 Id. at 67.
62 Id. at 68–69.
63 Id. at 68.
64 Id.
65 Id.
66 Id. at 69.
67 Id.
68 Id.
69 Id.

problems spawned by the regional economic turmoil."[70]

Thus, Wellex maintained that "the inability of the parties to execute the [share purchase agreement] and the [joint development agreement] principally arose from problems at [U-Land's] side, and not due to [Wellex's] 'unjustified refusal to enter into [the] [share purchase agreement][.]'"[71]

On July 30, 1999, U-Land filed a Complaint[72] praying for rescission of the First Memorandum of Agreement and damages against Wellex and for the issuance of a Writ of Preliminary Attachment.[73] From U-Land's point of view, its primary reason for purchasing APIC shares from Wellex was APIC's majority ownership of shares of stock in APC (APC shares).[74] After verification with the Securities and Exchange Commission, U-Land discovered that "APIC did not own a single share of stock in APC."[75] U-Land alleged that it repeatedly requested that the parties enter into the share purchase agreement.[76] U-Land attached the demand letter dated July 22, 1999 to the Complaint.[77] However, the 40-day period lapsed, and no share purchase agreement was finalized.[78]

U-Land alleged that, as of the date of filing of the Complaint, Wellex still refused to return the amount of US$7,499,945.00 while refusing to enter into the share purchase agreement.[79] U-Land stated that it was induced by Wellex to enter into and execute the First Memorandum of Agreement, as well as release the amount of US$7,499,945.00.[80]

In its Answer with Compulsory Counterclaim,[81] Wellex countered that U-Land had no cause of action.[82] Wellex maintained that under the First Memorandum of Agreement, the parties agreed to enter into a share purchase agreement and a joint development agreement.[83] Wellex alleged that to bring the share purchase agreement to fruition, it would have to acquire the corresponding shares in APIC.[84] It claimed that U-Land was fully aware that the former "still ha[d] to consolidate its title over these shares."[85] This was the reason for Wellex's attachment of the Second

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70 Id.
71 Id.
72 Id. at 70–75.
73 Id. at 73.
74 Id. at 322.
75 Id. at 72.
76 Id.
77 Id.
78 Id. at 71.
79 Id. at 72.
80 Id. at 91.
81 Id. at 76–88.
82 Id. at 78.
83 Id. at 92.
84 Id. at 92–93.
85 Id. at 93.

Memorandum of Agreement to the First Memorandum of Agreement. Wellex attached the Second Memorandum of Agreement as evidence to refute U-Land's claim of misrepresentation.[86]

Wellex further alleged that U-Land breached the First Memorandum of Agreement since the payment for the shares was to begin during the 40-day period, which began on May 16, 1998.[87] In addition, U-Land failed to remit the US$3 million by May 22, 1998 that would serve as initial funding for the development projects.[88] Wellex claimed that the remittance of the US$3 million on May 22, 1998 was a mandatory obligation on the part of U-Land.[89]

Wellex averred that it presented draft versions of the share purchase agreement, which were never finalized.[90] Thus, it believed that there was an implied extension of the 40-day period within which to enter into the share purchase agreement and the joint development agreement since U-Land began remitting sums of money in partial payment for the purchase of the shares of stock.[91]

In its counterclaim against U-Land, Wellex alleged that it had already set in motion building and development of real estate projects on four (4) major sites in Cavite, Iloilo, and Davao. It started initial construction on the basis of its agreement with U-Land to pursue real estate development projects.[92]

Wellex claims that, had the development projects pushed through, the parties would have shared equally in the profits of these projects.[93] These projects would have yielded an income of □2,404,948,000.00, as per the study Wellex conducted, which was duly recognized by U-Land.[94] Half of that amount, □1,202,474,000.00, would have redounded to Wellex.[95] Wellex, thus, prayed for the rescission of the First Memorandum of Agreement and the payment of □1,202,474,000 in damages for loss of profit.[96] It prayed for the payment of moral damages, exemplary damages, attorney's fees, and costs of suit.[97]

In its Reply,[98] U-Land denied that there was an extension of the 40-

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86 Id. at 78.
87 Id. at 80.
88 Id.
89 Id. at 95.
90 Id. at 77.
91 Id. at 80.
92 Id. at 83.
93 Id. at 84.
94 Id.
95 Id.
96 Id. at 86.
97 Id. at 87.
98 Id. at 363–367.

day period within which to enter into the share purchase agreement and the joint development agreement. It also denied requesting for an extension of the 40-day period. It further raised that there was no provision in the First Memorandum of Agreement that required it to remit payments for Wellex's shares of stock in APIC and PEC within the 40-day period. Rather, the remittances were supposed to begin upon the execution of the share purchase agreement.[99]

As for the remittance of the US$3 million, U-Land stated that the issuance of this amount on May 22, 1998 was supposed to be simultaneously made with Wellex's delivery of the stock certificates for 57,000,000 PEC shares. These stock certificates were not delivered on that date.[100]

With regard to the drafting of the share purchase agreement, U-Land denied that it was Wellex that presented versions of the agreement. U-Land averred that it was its own counsel who drafted versions of the share purchase agreement and the joint development agreement, which Wellex refused to sign.[101]

U-Land specifically denied that it had any knowledge prior to or during the execution of the First Memorandum of Agreement that Wellex still had to "consolidate its title over" its shares in APIC. U-Land averred that it relied on Wellex's representation that it was a majority owner of APIC shares and that APIC owned a majority of APC shares.[102]

Moreover, U-Land denied any knowledge of the initial steps that Wellex undertook to pursue the development projects and denied any awareness of a study conducted by Wellex regarding the potential profit of these projects.[103]

The case proceeded to trial.

U-Land presented Mr. David Tseng (Mr. Tseng), its President and Chief Executive Officer, as its sole witness.[104] Mr. Tseng testified that "[s]ometime in 1997, Mr. William Gatchalian who was in Taiwan invited [U-Land] to join in the operation of his airline company[.]"[105] U-Land did not accept the offer at that time.[106] During the first quarter of 1998, Mr. Gatchalian "went to Taiwan and invited [U-Land] to invest in Air

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99 Id. at 363.
100 Id. at 363–364.
101 Id. at 364–365.
102 Id. at 365.
103 Id. at 366.
104 Id. at 96.
105 Id.
106 Id.

Philippines[.]"[107] This time, U-Land alleged that subsequent meetings were held where Mr. Gatchalian, representing Wellex, "claimed ownership of a majority of the shares of APIC and ownership by APIC of a majority of the shares of [APC,] a domestic carrier in the Philippines."[108] Wellex, through Mr. Gatchalian, offered to sell to U-Land PEC shares as well.[109]

According to Mr. Tseng, the parties agreed to enter into the First Memorandum of Agreement after their second meeting.[110] Mr. Tseng testified that under this memorandum of agreement, the parties would enter into a share purchase agreement "within forty (40) days from its execution which [would] put into effect the sale of the shares [of stock] of APIC and PEC[.]"[111] However, the "[s]hare [p]urchase [a]greement was not executed within the forty-day period despite the draft . . . given [by U-Land to Wellex]."[112]

Mr. Tseng further testified that it was only after the lapse of the 40-day period that U-Land discovered that Wellex needed money for the transfer of APC shares to APIC. This allegedly shocked U-Land since under the First Memorandum of Agreement, APIC was supposed to own a majority of APC shares. Thus, U-Land remitted to Wellex a total of US$7,499,945.00 because of its intent to become involved in the aviation business in the Philippines. These remittances were confirmed by Wellex through a confirmation letter. Despite the remittance of this amount, no share purchase agreement was entered into by the parties.[113]

Wellex presented its sole witness, Ms. Elvira Ting (Ms. Ting), Vice President of Wellex. She admitted her knowledge of the First Memorandum of Agreement as she was involved in its drafting. She testified that the First Memorandum of Agreement made reference, under its second preambular clause, to the Second Memorandum of Agreement entered into by Wellex, APIC, and APC. She testified that under the First Memorandum of Agreement, U-Land's purchase of APIC shares and PEC shares from Wellex would take place within 40 days, with the execution of a share purchase agreement.[114]

According to Ms. Ting, after the 40-day period lapsed, U-Land Chairman Mr. Wang requested sometime in June of 1998 for an extension for the execution of the share purchase agreement and the remittance of the US$3 million. As proof that Mr. Wang made this request, Ms. Ting

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107 Id.
108 Id.
109 Id.
110 Id.
111 Id.
112 Id.
113 Id.
114 Id. at 96–97.

testified that Mr. Wang sent several post-dated checks to cover the payment of the APIC shares and PEC shares and the initial funding of US$3 million for the joint development agreement. She testified that Mr. Wang presented a draft of the share purchase agreement, which Wellex rejected. Wellex drafted a new version of the share purchase agreement.[115] However, the share purchase agreement was not executed because during the period of negotiation, Wellex learned from other sources that U-Land "encountered difficulties starting October of 1998."[116] Ms. Ting admitted that U-Land made the remittances to Wellex in the amount of US$7,499,945.00.[117]

Ms. Ting testified that U-Land was supposed to make an initial payment of US$19 million under the First Memorandum of Agreement. However, U-Land only paid US$7,499,945.00. The total payments should have amounted to US$41 million.[118]

Finally, Ms. Ting testified that Wellex tried to contact U-Land to have a meeting to thresh out the problems of the First Memorandum of Agreement, but U-Land did not reply. Instead, Wellex only received communication from U-Land regarding their subsequent negotiations through the latter's demand letter dated July 22, 1999. In response, Wellex wrote to U-Land requesting another meeting to discuss the demands. However, U-Land already filed the Complaint for rescission and caused the attachment against the properties of Wellex, causing embarrassment to Wellex.[119]

In the Decision dated April 10, 2001, the Regional Trial Court of Makati City held that rescission of the First Memorandum of Agreement was proper:

> The first issue must be resolved in the negative. Preponderance of evidence leans in favor of plaintiff that it is entitled to the issuance of the writ of preliminary attachment. Plaintiff's evidence establishes the facts that it is engaged in the airline business in Taiwan, was approached by defendant, through its Chairman William Gatchalian, and was invited by the latter to invest in an airline business in the Philippines, Air Philippines Corporation (APC); that plaintiff became interested in the invitation of defendant; that during the negotiations between plaintiff and defendant, defendant induced plaintiff to buy shares in Air Philippines International Corporation (APIC) since it owns majority of the shares of APC; that defendant also induced plaintiff to buy shares of APIC in Philippine Estates Corporation (PEC); that the negotiations between plaintiff and defendant culminated into the parties executing a MOA (Exhs. "C" to "C-3", also Exh. "1"); that in the second "Whereas" clause of the MOA, defendant represented that it has a current airline operation

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115 Id.
116 Id. at 97.
117 Id.
118 Id.
119 Id.

through its majority-owned subsidiary APIC, that under the MOA, the parties were supposed to enter into a Share Purchase Agreement (SPA) within forty (40) days from May 16, 1998, the date the MOA in order to effect the transfer of APIC and PEC shares of defendant to plaintiff; that plaintiff learned from defendant that APIC does not actually own a single share in APC; that plaintiff verified with the Securities and Exchange Commission (SEC), by obtaining a General Information Sheet therefrom (Exh. "C-Attachment"); that APIC does not in fact own APC; that defendant induced plaintiff to still remit its investment to defendant, which plaintiff did as admitted by defendant per its Confirmation Letter (Exh. "D") in order that APC shares could be transferred to APIC; that plaintiff remitted a total of US$7,499,945.00 to defendant; and that during the forty-day period stipulated in the MOA and even after the lapse of the said period, defendant has not entered into the SPA, nor has defendant caused the transfer of APC shares to APIC.

In the second "Whereas" clause of the MOA (Exh. "C"), defendant's misrepresentation that APIC owns APC is made clear, as follows:

> "WHEREAS, WELLEX, on the other hand, has current airline operation in the Philippines through its majority-owned subsidiary Air Philippines International Corporation (Exh. "C") and the latter's subsidiary, Air Philippines Corporation, and in like manner also desires to expand its operation in the Asian regional markets; x x x" (Second Whereas of Exh. "C")

On the other hand, defendant's evidence failed to disprove plaintiff's evidence. The testimony of defendant's sole witness Elvira Ting, that plaintiff knew at the time of the signing of the MOA that APIC does not own a majority of the shares of APC because another Memorandum of Agreement was attached to the MOA (Exh "1") pertaining to the purchase of APC shares by APIC is unavailing. The second "Whereas" clause of the MOA leaves no room for interpretation. . . . The second MOA purportedly attached as Annex "A" of this MOA merely enlightens the parties on the manner by which APIC acquired the shares of APC. Besides, . . . the second MOA was not a certified copy and did not contain a marking that it is an Annex "A" when it was supposed to be an Annex "A" and a certified copy per the MOA between plaintiff and defendant. As can be also gathered from her testimony, Ms. Ting does not have personal knowledge that plaintiff was not informed that APIC did not own shares of APC during the negotiations as she was not present during the negotiations between plaintiff and defendant's William Gatchalian. Her participation in the agreement between the parties [was] merely limited to the preparation of the documents to be signed. Ms. Ting testified, as follows:

> "Q During the negotiation, you did not know anything about that?"
>
> A I was not involved in the negotiation, sir.
>
> Q And you are just making your statement that U-Land knew about the intended transfer of shares from APC to APIC because of

this WHEREAS CLAUSE and the Annex to this Memorandum of Agreement?

A Yes, it was part of the contract."
(TSN, Elvira Ting, June 6, 2000, pp. 8-10)

Defendant's fraud in the performance of its obligation under the MOA is further revealed when Ms. Ting testified on cross-examination that notwithstanding the remittances made by plaintiff in the total amountn [sic] of US$7,499, 945.00 to partially defray the cost of transferring APC shares to APIC even as of the year 2000, as follows:

"Q Ms. Ting, can you please tell the Court if you know who owns shares of Air Philippines Corporation at this time?

A Air Philippines Corporation right now is own [sic] by Wellex Group and certain individual.

Q How much shares of Air Philippines Corporation is owned by Wellex Group?

A Around twenty...at this moment around twenty five percent (25%).

Q Can you tell us if you know who are the other owners of the shares of Air Philippines?

A There are several individual owners, I cannot recall the names.

Q Could [sic] you know if Air Philippines Int'l. Corporation is one of the owners?

A As of this moment, no sir."

(lbid, p. 16)

That defendant represented to plaintiff that it needed the remittances of plaintiff, even if no SPA was executed yet between the parties, to effect the transfer of APC shares to APIC is admitted by its same witness also in this wise:

"Q You said that remittances were made to the Wellex Group, Incorporated by plaintiff for the period from June 1998 to September 1998[,] is that correct?

A Yes, Sir.

Q During all these times, that remittances were made in the total amount of more than seven million dollars, did you ever know if plaintiff asked for evidence from your company that AIR PHILIPPINES INTERNATIONAL CORPORATION has already acquired shares of AIR PHILIPPINES CORPORATION?

A There were queries on the matter.

Q And what was your answer to those queries, Madam Witness?

A We informed them that the decision was still in the process.

Q Even up to the time that plaintiff U-Land stopped the remittances sometime in September 1998 you have not effected the transfer of shares of AIR PHILIPPINES CORPORATION to AIR PHILIPPINES INTERNATIONCAL [sic] CORPORATION[,] am I correct?

A APC to APIC, well at that time it's still in the process.

Q In fact, Madam Witness, is it not correct for me to say that one of the reasons why U-Land Incorporated was convinced to remit the amounts of money totalling seven million dollars plus, was that your company said that it needed funds to effect these transfers, is that correct?

A Yes, sir."

(Ibid, pp. 25-29)

As the evidence adduced by the parties stand, plaintiff has established the fact that it had made remittances in the total amount of US$7,499,945.00 to defendant in order that defendant will make good its representation that APC is a subsidiary of APIC. The said remittances are admitted by defendant.

Notwithstanding the said remittances, APIC does not own a single share of APC. On the other hand, defendant could not even satisfactorily substantiate its claim that at least it had the intention to cause the transfer of APC shares to APIC. [D]efendant obviously did not enter into the stipulated SPA because it did not have the shares of APC transferred to APIC despite its representations. Under the circumstances, it is clear that defendant fraudulently violated the provisions of the MOA.[120] (Emphasis supplied)

On appeal, the Court of Appeals affirmed the ruling of the Regional Trial Court.[121] In its July 30, 2004 Decision, the Court of Appeals held that the Regional Trial Court did not err in granting the rescission:

Records show that in the answer filed by defendant-appellant, the latter itself asked for the rescission of the MOA. Thus, in effect, it prays for the return of what has been given or paid under the MOA, as the law creates said obligation to return the things which were the object of the contract, and the same could be carried out only when he who demands

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120 Id. at 98–100.
121 Id. at 54.

rescission can return whatever he may be obliged to restore. The law says:

> "Rescission creates the obligation to return the things which were the object of the contract, together with their fruits, and the price with its interest; consequently, it can be carried out only when he who demands rescission can return whatever he may be obliged to restore."

Appellant, therefore, cannot ask for rescission of the MOA and yet refuse to return what has been paid to it. Further, appellant's claim that the lower court erred in ruling for the rescission of the MOA is absurd and ridiculous because rescission thereof is prayed for by the former. . . .

This Court agrees with the lower court that appellee is the injured party in this case, and therefore is entitled to rescission, because the rescission referred to here is predicated on the breach of faith by the appellant which breach is violative of the reciprocity between the parties. It is noted that appellee has partly complied with its own obligation, while the appellant has not. It is, therefore, the right of the injured party to ask for rescission because the guilty party cannot ask for rescission.

The lower court . . . correctly ruled that:

> ". . . This Court agrees with plaintiff that defendant's misrepresentations regarding APIC's not owning shares in APC vitiates its consent to the MOA. Defendant's continued misrepresentation that it will cause the transfer of APC shares in APIC inducing plaintiff to remit money despite the lapse of the stipulated forty day period, further establishes plaintiff's right to have the MOA rescinded.
>
> Section 9 of the MOA itself provides that in the event of the non-execution of an SPA within the 40 day period, or within the extensions thereof, the payments made by plaintiff shall be returned to it, to wit:
>
> "9 Validity.- In the event that the parties are unable to agree on the terms of the SHPA and/or JDA within forty (40) days from the date hereof (or such period as the parties shall mutually agree), this Memorandum of Agreement shall cease to be effective and the parties released from their respective undertakings herein, except that WELLEX shall refund the US$3.0 million under Section 4 within three (3) days therefrom, otherwise U-LAND shall have the right to recover the 57,000,000 PEC shares delivered to U-LAND under Section 4."

Clearly, the parties were not able to agree on the terms of the SPA within and even after the lapse of the stipulated 40 day period. There being no SPA entered into by and between the plaintiff and defendant, defendant's return of the remittances [of] plaintiff in the total amount of US$7,499,945 is only proper, in the same vein, plaintiff should return to

> defendant the titles and certificates of stock given to it by defendant.[122] (Citations omitted)

Hence, this Petition was filed.

Petitioner's Arguments

Petitioner Wellex argues that contrary to the finding of the Court of Appeals, respondent U-Land was not entitled to rescission because the latter itself violated the First Memorandum of Agreement. Petitioner Wellex states that respondent U-Land was actually bound to pay US$17.5 million for all of APIC shares and PEC shares under the First Memorandum of Agreement and the US$3 million to pursue the development projects under the joint development agreement. In sum, respondent U-Land was liable to petitioner Wellex for the total amount of US$20.5 million. Neither the Court of Appeals nor the Regional Trial Court made any mention of the legal effect of respondent U-Land's failure to pay the full purchase price.[123]

On the share purchase agreement, petitioner Wellex asserts that its obligation to deliver the totality of the shares of stock would become demandable only upon remittance of the full purchase price of US$17.5 million.[124] The full remittance of the purchase price of the shares of stock was a suspensive condition for the execution of the share purchase agreement and delivery of the shares of stock. Petitioner Wellex argues that the use of the term "upon" in Section 2 of the First Memorandum of Agreement clearly provides that the full payment of the purchase price must be given "simultaneously" or "concurrent" with the execution of the share purchase agreement.[125]

Petitioner Wellex raises that the Court of Appeals erred in saying that the rescission of the First Memorandum of Agreement was proper because petitioner Wellex itself asked for this in its Answer before the trial court.[126] It asserts that "there can be no rescission of a non-existent obligation, such as [one] whose suspensive condition has not yet happened[,]"[127] as held in *Padilla v. Spouses Paredes*.[128] Citing *Villaflor v. Court of Appeals*[129] and *Spouses Agustin v. Court of Appeals*,[130] it argues that "the vendor. . . has no obligation to deliver the thing sold. . . if the buyer. . . fails to fully pay the

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122 Id. at 52–54.
123 Id. at 399–400.
124 Id. at 400. According to petitioner, the amount of US$ 17.5 million was based on this: 1,050,000,000 APIC shares were to be purchased at the price of □0.30/share and 490,000,000 PEC shares were to be purchased at the price of □0.65 per share, at the exchange rate of □36.00 to US$1.00.
125 Id. at 401–402.
126 Id. at 403.
127 Id. at 402.
128 385 Phil. 128, 140 (2000) [Per J. Quisimbing, Second Division].
129 345 Phil. 524 (1997) [Per J. Panganiban, Third Division].
130 264 Phil. 744 (1990) [Per J. Regalado, Second Division].

price as required by the contract."[131] In this case, petitioner Wellex maintains that respondent U-Land's remittance of US$7,499,945.00 constituted mere *partial* performance of a reciprocal obligation.[132] Thus, respondent U-Land was not entitled to rescission. The nature of this reciprocal obligation requires both parties' simultaneous fulfillment of the totality of their reciprocal obligations and not only partial performance on the part of the allegedly injured party.

As to the finding of misrepresentations, petitioner Wellex raises that a seller may sell a thing not yet belonging to him at the time of the transaction, provided that he will become the owner at the time of delivery so that he can transfer ownership to the buyer. Contrary to the finding of the lower courts, petitioner Wellex was obliged to be the owner of the shares only when the time came to deliver these to respondent U-Land and not during the perfection of the contract itself.[133]

Finally, petitioner Wellex argues that respondent U-Land could have recovered through the securities given to the latter.[134] Petitioner Wellex invokes *Suria v. Intermediate Appellate Court*,[135] which held that an "action for rescission is not a principal action that is retaliatory in character [under Article 1191 of the Civil Code, but] a subsidiary one which. . . is available only in the absence of any other legal remedy [under Article 1384 of the Civil Code]."[136]

Respondent's Arguments

Respondent U-Land argues that it was the execution of the share purchase agreement that would result in its purchase of the APIC shares and PEC shares.[137] It was not the full remittance of the purchase price of the shares of stock as indicated in the First Memorandum of Agreement, as alleged by petitioner Wellex.[138] Respondent U-Land asserts that the First Memorandum of Agreement provides that the exact number of APIC shares and PEC shares to be purchased under the share purchase agreement and the final price of these shares were not yet determined by the parties.[139]

Respondent U-Land reiterates that it was petitioner Wellex that requested for the remittances amounting to US$7,499,945.00 to facilitate

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131 *Rollo*, p. 403.
132 Id.
133 Id. at 410–411.
134 Id. at 411.
135 235 Phil. 661, 667 (1987) [Per J. Gutierrez, Jr., Second Division].
136 *Rollo*, p. 411.
137 Id. at 332.
138 Id.
139 Id. at 333.

APIC's purchase of APC shares.[140] Thus, it was petitioner Wellex's refusal to enter into the share purchase agreement that led to respondent U-Land demanding rescission of the First Memorandum of Agreement and the return of the US$7,499,945.00.[141] Respondent U-Land further argues before this court that petitioner Wellex failed to present evidence as to how the money was spent, stating that Ms. Ting admitted that the Second Memorandum of Agreement "was not consummated at any time."[142]

Respondent U-Land raises that petitioner Wellex was guilty of fraud by making it appear that APC was a subsidiary of APIC.[143] It reiterates that, as an airline company, its primary reason for entering into the First Memorandum of Agreement was to acquire management of APC, another airline company.[144] Under Article 1191 of the Civil Code, respondent U-Land, as the injured party, was entitled to rescission due to the fatal misrepresentations committed by petitioner Wellex.[145]

Respondent U-Land further asserts that the "shareholdings in APIC and APC were never in question."[146] Rather, it was petitioner Wellex's misrepresentation that APIC was a majority shareholder of APC that compelled it to enter into the agreement.[147]

As for *Suria*, respondent U-land avers that this case was inapplicable because the pertinent provision in *Suria* was not Article 1191 but rescission under Article 1383 of the Civil Code.[148] The "rescission" referred to in Article 1191 referred to "resolution" of a contract due to a breach of a mutual obligation, while Article 1384 spoke of "rescission" because of lesion and damage.[149] Thus, the rescission that is relevant to the present case is that of Article 1191, which involves breach in a reciprocal obligation. It is, in fact, resolution, and not rescission as a result of fraud or lesion, as found in Articles 1381, 1383, and 1384 of the Civil Code.[150]

The Issue

The question presented in this case is whether the Court of Appeals erred in affirming the Decision of the Regional Trial Court that granted the rescission of the First Memorandum of Agreement prayed for by U-Land.

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140 Id. at 335.
141 Id.
142 Id. at 337.
143 Id. at 339.
144 Id. at 340.
145 Id. at 272–273.
146 Id. at 353.
147 Id. at 352–353.
148 Id. at 355.
149 Id. at 356.
150 Id.

The Petition must be denied.

I

The requirement of a share purchase agreement

The Civil Code provisions on the interpretation of contracts are controlling to this case, particularly Article 1370, which reads:

> ART. 1370. If the terms of a contract are clear and leave no doubt upon the intention of the contracting parties, the literal meaning of its stipulations shall control.
>
> If the words appear to be contrary to the evident intention of the parties, the latter shall prevail over the former.

In *Norton Resources and Development Corporation v. All Asia Bank Corporation*:[151]

> The cardinal rule in the interpretation of contracts is embodied in the first paragraph of Article 1370 of the Civil Code: "[i]f the terms of a contract are clear and leave no doubt upon the intention of the contracting parties, the literal meaning of its stipulations shall control." This provision is akin to the "plain meaning rule" applied by Pennsylvania courts, which assumes that *the intent of the parties to an instrument is "embodied in the writing itself, and when the words are clear and unambiguous the intent is to be discovered only from the express language of the agreement." It also resembles the "four corners" rule, a principle which allows courts in some cases to search beneath the semantic surface for clues to meaning. A court's purpose in examining a contract is to interpret the intent of the contracting parties, as objectively manifested by them. The process of interpreting a contract requires the court to make a preliminary inquiry as to whether the contract before it is ambiguous. A contract provision is ambiguous if it is susceptible of two reasonable alternative interpretations. Where the written terms of the contract are not ambiguous and can only be read one way, the court will interpret the contract as a matter of law.* If the contract is determined to be ambiguous, then the interpretation of the contract is left to the court, to resolve the ambiguity in the light of the intrinsic evidence.[152] (Emphasis supplied)

As held in *Norton*, this court must first determine whether a provision or stipulation contained in a contract is ambiguous. Absent any ambiguity, the provision on its face will be read as it is written and treated as the

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151 620 Phil. 381 (2009) [Per J. Nachura, Third Division].

152 Id. at 388, *citing Benguet Corporation, et al. v. Cabildo*, 585 Phil. 23, 34–35 (2008) [Per J. Nachura, Third Division].

binding law of the parties to the contract.

The parties have differing interpretations of the terms of the First Memorandum of Agreement. Petitioner Wellex even admits that "the facts of the case are fairly undisputed [and that] [i]t is only the parties' respective [understanding] of these facts that are not in harmony."[153]

The second preambular clause of the First Memorandum of Agreement reads:

> WHEREAS, WELLEX, on the other hand, has current airline operation in the Philippines through its majority-owned subsidiary Air Philippines International Corporation and the latter's subsidiary, *Air Philippines Corporation, and in like manner also desires to expand its operation in the Asian regional markets; a Memorandum of Agreement on _____, a certified copy of which is attached hereto as Annex "A" and is hereby made an integral part hereof, which sets forth, among others, the basis for WELLEX's present ownership of shares in Air Philippines International Corporation.*[154] (Emphasis supplied)

Section 1 of the First Memorandum of Agreement reads:

> I. Basic Agreement. - The parties agree to develop a long-term business relationship initially through the creation of joint interest in airline operations as well as in property development projects in the Philippines to be implemented as follows:
>
> (a) U-LAND shall acquire from WELLEX, shares of stock of AIR PHILIPPINES INTERNATIONAL CORPORATION ("APIC") equivalent to at least 35% of the outstanding capital stock of APIC, but in any case, not less than 1,050,000,000 shares (the "APIC Shares").
>
> (b) U-LAND shall acquire from WELLEX, shares of stock of PHILIPPINE ESTATES CORPORATION ("PEC") equivalent to at least 35% of the outstanding capital stock of PEC, but in any case, not less than 490,000,000 shares (the "PEC Shares").
>
> (c) U-LAND shall enter into a joint development agreement with PEC to jointly pursue property development projects in the Philippines.
>
> (d) U-LAND shall be given the option to acquire from WELLEX shares of stock of EXPRESS SAVINGS BANK ("ESB") up to 40% of the outstanding capital stock of ESB (the "ESB Shares") under terms to be mutually agreed.[155]

The First Memorandum of Agreement contained the following

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153 *Rollo*, p. 417.
154 Id. at 59.
155 Id. at 59–60.

stipulations regarding the share purchase agreement:

> 2. Acquisition of APIC and PEC Shares. - *Within forty (40) days from date hereof (unless extended by mutual agreement), U-LAND and WELLEX shall execute a Share Purchase Agreement ("SHPA") covering the acquisition by U-LAND of the APIC Shares and PEC Shares (collectively, the "Subject Shares"). Without prejudice to any subsequent agreement between the parties, the purchase price for the APIC Shares to be reflected in the SHPA shall be THIRTY CENTAVOS (P0.30) per share and that for the PEC Shares at SIXTY FIVE CENTAVOS (P0.65) per share.*
>
> *The purchase price for the Subject Shares as reflected in the SHPA shall be paid in full upon execution of the SHPA against delivery of the Subject Shares.* The parties may agree on such other terms and conditions governing the acquisition of the Subject Shares to be provided in a separate instrument.
>
> *The transfer of the Subject Shares shall be effected to U-LAND provided that: (i) the purchase price reflected in the SHPA has been fully paid; (ii) the Philippine Securities & Exchange Commission (SEC) shall have approved the issuance of the Subject Shares; and (iii) any required approval by the Taiwanese government of the acquisition by U-LAND of the Subject Shares shall likewise have been obtained.*[156] (Emphasis supplied)

As for the joint development agreement, the First Memorandum of Agreement contained the following stipulation:

> 4. Joint Development Agreement with PEC. – *Simultaneous with the execution of the SHPA, U-LAND and PEC shall execute a joint development agreement ("JDA") to pursue property development projects in the Philippines.* The JDA shall cover specific housing and other real estate development projects as the parties shall agree. All profits derived from the projects covered by the JDA shall be shared equally between U-LAND and PEC. *U-LAND shall, not later than May 22, 1998, remit the sum of US$3.0 million as initial funding for the aforesaid development projects against delivery by WELLEX of 57,000,000 shares of PEC as security for said amount in accordance with Section 9 below.*[157] (Emphasis provided)

Finally, the parties included the following stipulation in case of a failure to agree on the terms of the share purchase agreement or the joint development agreement:

> 9. Validity. - In the event the parties are unable to agree on the terms of the SHPA and/or the JDA within forty (40) days from date hereof (or such period as the parties shall mutually agree), this Memorandum of

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156 Id. at 60.
157 Id.

> Agreement shall cease to be effective and the parties released from their respective undertakings herein, except that WELLEX shall refund the US$3.0 million provided under Section 4 within three (3) days therefrom, otherwise U-LAND shall have the right to recover on the 57,000,000 PEC shares delivered to U-LAND under Section 4.[158]

Section 2 of the First Memorandum of Agreement clearly provides that the *execution* of a share purchase agreement containing mutually agreeable terms and conditions must first be accomplished by the parties *before* respondent U-Land purchases any of the shares owned by petitioner Wellex. A perusal of the stipulation on its face allows for no other interpretation.

The need for a share purchase agreement to be entered into before payment of the full purchase price can further be discerned from the other stipulations of the First Memorandum of Agreement.

In Section 1, the parties agreed to enter into a joint business venture, through entering into two (2) agreements: a share purchase agreement and a joint development agreement. However, Section 1 provides that in the share purchase agreement, "U-LAND shall acquire from WELLEX, shares of stock of AIR PHILIPPINES INTERNATIONAL CORPORATION ('APIC') equivalent to *at least 35% of the outstanding capital stock of APIC, but in any case, not less than 1,050,000,000 shares (the 'APIC Shares')*."[159]

As for the PEC shares, Section 1 provides that respondent U-Land shall purchase from petitioner Wellex "shares of stock of PHILIPPINE ESTATES CORPORATION ('PEC') equivalent to *at least 35% of the outstanding capital stock of PEC, but in any case, not less than 490,000,000 shares* (the 'PEC Shares')."[160]

The use of the terms "at least 35% of the outstanding capital stock of APIC, but in any case, not less than 1,050,000,000 shares" and "at least 35% of the outstanding capital stock of PEC, but in any case, not less than 490,000,000 shares" means that the parties *had yet to agree on the number of shares of stock to be purchased.*

The need to execute a share purchase agreement *before* payment of the purchase price of the shares is further shown by the clause, "[w]ithout prejudice to any subsequent agreement between the parties, the purchase price for the APIC Shares *to be reflected in the [share purchase agreement]* shall be... □0.30 per share and that for the PEC Shares at... □0.65 per

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158 Id. at 61.
159 Id. at 59–60.
160 Id. at 60.

share."[161] This phrase clearly shows that the final price of the shares of stock was to be reflected in the share purchase agreement. There being no share purchase agreement executed, respondent U-Land was under no obligation to begin payment or remittance of the purchase price of the shares of stock.

Petitioner Wellex argues that the use of "upon" in Section 2[162] of the First Memorandum of Agreement means that respondent U-Land must pay the purchase price of the shares of stock in its entirety when they are transferred. This argument has no merit.

Article 1373 of the Civil Code provides:

> ART. 1373. If some stipulation of any contract should admit of several meanings, it shall be understood as bearing that import which is most adequate to render it effectual.

It is necessary for the parties to first agree on the final purchase price and the number of shares of stock to be purchased *before respondent U-Land is obligated to pay or remit the entirety of the purchase price.* Thus, petitioner Wellex's argument cannot be sustained since the parties to the First Memorandum of Agreement were clearly unable to agree on all the terms concerning the share purchase agreement. It would be absurd for petitioner Wellex to expect payment when respondent U-Land did not yet agree to the final amount to be paid for the totality of an indeterminate number of shares of stock.

The third paragraph of Section 2[163] provides that the "transfer of the Subject Shares" shall take place upon the fulfillment of certain conditions, such as full payment of the purchase price "as reflected in the [share purchase agreement]." The *transfer* of the shares of stock is different from the *execution* of the share purchase agreement. The *transfer* of the shares of stock requires full payment of the final purchase price. However, that final purchase price must be *reflected in the share purchase agreement*. The execution of the share purchase agreement will require the existence of a *final* agreement.

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[161] Id.

[162] Sec. 2, par. 2 of the First Memorandum of Agreement reads:
The purchase price for the Subject Shares as reflected in the SHPA shall be paid in full *upon* execution of the SHPA against delivery of the Subject Shares. The parties may agree on such other terms and conditions governing the acquisition of the Subject Shares to be provided in a separate instrument. (Emphasis supplied)

[163] Sec. 2, par. 3 of the First Memorandum of Agreement reads:
The transfer of the Subject Shares shall be effected to U-LAND provided that: (i) the purchase price reflected in the SHPA has been fully paid; (ii) the Philippine Securities & Exchange Commission (SEC) shall have approved the issuance of the Subject Shares; and (iii) any required approval by the Taiwanese government of the acquisition by U-LAND of the Subject Shares shall likewise have been obtained. (Emphasis provided)

In its Answer with counterclaim before the trial court, petitioner Wellex argued that the payment of the shares of stock was to begin within the 40-day period. Petitioner Wellex's claim is not in any of the stipulations of the contract. Its subsequent claim that respondent U-Land was actually required to remit a total of US$20.5 million is likewise bereft of basis since *there was no final purchase price of the shares of stock that was agreed upon,* due to the failure of the parties to execute a share purchase agreement. In addition, the parties had yet to agree on the final number of APIC shares and PEC shares that respondent U-Land would acquire from petitioner Wellex.

Therefore, the understanding of the parties captured in the First Memorandum of Agreement was to continue their negotiation to determine the price and number of the shares to be purchased. Had it been otherwise, the specific number or percentage of shares and its price should already have been provided clearly and unambiguously. Thus, they agreed to a 40-day period of negotiation.

Section 9 of the First Memorandum of Agreement explicitly provides that:

> In the event the parties are unable to agree on the terms of the SHPA and/or the JDA within forty (40) days from date hereof (or such period as the parties shall mutually agree), this Memorandum of Agreement shall cease to be effective and the parties released from their respective undertakings herein . . .[164]

The First Memorandum of Agreement was, thus, an agreement to enter into a share purchase agreement. The share purchase agreement should have been executed by the parties within 40 days from May 16, 1998, the date of the signing of the First Memorandum of Agreement.

When the 40-day period provided for in Section 9 lapsed, the efficacy of the First Memorandum of Agreement ceased. The parties were "*released from their respective undertakings*." Thus, from June 25, 1998, the date when the 40-day period lapsed, the parties were no longer obliged to negotiate with each other in order to enter into a share purchase agreement.

However, Section 9 provides for another period within which the parties could still be required to negotiate. The clause "or such period as the parties shall mutually agree" means that the parties should agree on a period within which to continue negotiations for the execution of an

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[164] *Rollo*, p. 61.

agreement. This means that after the 40-day period, the parties were still allowed to negotiate, *provided that they could mutually agree on a new period of negotiation*.

Based on the records and the findings of the lower courts, the parties were never able to arrive at a specific period within which they would bind themselves to enter into an agreement. There being no other period specified, the parties were no longer under any obligation to negotiate and enter into a share purchase agreement. Section 9 clearly freed them from this undertaking.

II

There was no express or implied novation of the First Memorandum of Agreement

The subsequent acts of the parties after the 40-day period were, therefore, independent of the First Memorandum of Agreement.

In its Appellant's Brief before the Court of Appeals, petitioner Wellex mentioned that there was an "implied partial objective or real novation"[165] of the First Memorandum of Agreement. Petititoner did not raise this argument of novation before this court. In *Gayos v. Gayos*,[166] this court held that "it is a cherished rule of procedure that a court should always strive to settle the entire controversy in a single proceeding leaving no root or branch to bear the seeds of future litigation[.]"[167]

Articles 1291 and 1292 of the Civil Code provides how obligations may be modified:

> Article 1291. Obligations may be modified by:
>
> (1) Changing their object or principal conditions;
>
> (2) Substituting the person of the debtor;
>
> (3) Subrogating a third person in the rights of the creditor.
>
> Article 1292. In order that an obligation may be extinguished by another which substitute the same, it is imperative that it be so declared in unequivocal terms, or that the old and the new obligations be on every point incompatible with each other.

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165 Id. at 126.
166 160-A Phil. 285 (1975) [Per J. Aquino, Second Division].
167 Id. at 292–293, *citing Marquez v. Marquez*, 73 Phil. 74, 78 (1941) [Per J. Moran, En Banc].

In *Arco Pulp and Paper Co. v. Lim*,[168] this court discussed the concept of novation:

> Novation extinguishes an obligation between two parties when there is a substitution of objects or debtors or when there is subrogation of the creditor. It occurs only when the new contract declares so "in unequivocal terms" or that "the old and the new obligations be on every point incompatible with each other."
>
> . . . .
>
> For novation to take place, the following requisites must concur:
>
> 1) There must be a previous valid obligation.
> 2) The parties concerned must agree to a new contract.
> 3) The old contract must be extinguished.
> 4) There must be a valid new contract.
>
> Novation may also be express or implied. It is express when the new obligation declares in unequivocal terms that the old obligation is extinguished. It is implied when the new obligation is incompatible with the old one on every point. The test of incompatibility is whether the two obligations can stand together, each one with its own independent existence. (Emphasis from the original omitted)

Because novation requires that it be clear and unequivocal, it is never presumed, thus:

> In the civil law setting, *novatio* is literally construed as to make new. So it is deeply rooted in the Roman Law jurisprudence, the principle — *novatio non praesumitur* — that novation is never presumed. At bottom, for novation to be a jural reality, its *animus* must be ever present, *debitum pro debito* — basically extinguishing the old obligation for the new one.[169] (Emphasis from the original omitted, citations omitted)

Applying *Arco*, it is clear that there was no novation of the original obligation.

After the 40-day period, the parties did not enter into any subsequent written agreement that was couched in unequivocal terms. The transaction of the First Memorandum of Agreement involved large amounts of money

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[168] G.R. No. 206806, June 25, 2014 <http://sc.judiciary.gov.ph/pdf/web/viewer.html?file=/jurisprudence/2014/june2014/206806.pdf> [Per J. Leonen, Third Division].

[169] Id. at 7–8.

from both parties. The parties sought to participate in the air travel industry, which has always been highly regulated and subject to the strictest commercial scrutiny. Both parties admitted that their counsels participated in the crafting and execution of the First Memorandum of Agreement as well as in the efforts to enter into the share purchase agreement. Any subsequent agreement would be expected to be clearly agreed upon with their counsels' assistance and in writing, as well.

Given these circumstances, there was no express novation.

There was also no implied novation of the original obligation. In *Quinto v. People*:[170]

> [N]o specific form is required for an implied novation, and all that is prescribed by law would be an incompatibility between the two contracts. While there is really no hard and fast rule to determine what might constitute to be a sufficient change that can bring about novation, the touchstone for contrariety, however, would be an irreconcilable incompatibility between the old and the new obligations.
>
> . . . .
>
> . . . The test of incompatibility is whether or not the two obligations can stand together, each one having its independent existence. If they cannot, they are incompatible and the latter obligation novates the first. Corollarily, changes that breed incompatibility must be essential in nature and not merely accidental. The incompatibility must take place in any of the essential elements of the obligation, such as its object, cause or principal conditions thereof; otherwise, the change would be merely modificatory in nature and insufficient to extinguish the original obligation.[171] (Citations omitted)

There was no incompatibility between the original terms of the First Memorandum of Agreement and the remittances made by respondent U-Land for the shares of stock. These remittances were actually made with the view that both parties would subsequently enter into a share purchase agreement. It is clear that there was no subsequent agreement inconsistent with the provisions of the First Memorandum of Agreement.

Thus, no implied novation took place. In previous cases,[172] this court has consistently ruled that presumed novation or implied novation is not deemed favorable. In *United Pulp and Paper Co., Inc. v. Acropolis Central Guaranty Corporation*:[173]

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170 365 Phil. 259 (1999) [Per J. Vitug, Third Division].

171 Id. at 267–268.

172 *Magdalena Estates v. Rodriguez*, 125 Phil. 151, 157 (1966) [Per J. Regala, En Banc]; *Vda. de Mondragon v. Intermediate Appellate Court*, 263 Phil. 261, 268 (1990) [Per J. Griño-Aquino, First Division].

173 664 Phil. 65 (2012) [Per J. Mendoza, Third Division].

> Neither can novation be presumed in this case. As explained in *Duñgo v. Lopena*:
>
> > "*Novation by presumption has never been favored*. To be sustained, it need be established that the old and new contracts are incompatible in all points, or that the will to novate appears by express agreement of the parties or in acts of similar import."[174] (Emphasis supplied)

There being no novation of the First Memorandum of Agreement, respondent U-Land is entitled to the return of the amount it remitted to petitioner Wellex. Petitioner Wellex is likewise entitled to the return of the certificates of shares of stock and titles of land it delivered to respondent U-Land. This is simply an enforcement of Section 9 of the First Memorandum of Agreement. Pursuant to Section 9, only the execution of a final share purchase agreement within either of the periods contemplated by this stipulation will justify the parties' retention of what they received or would receive from each other.

III

Applying Article 1185 of the Civil Code, the parties are obligated to return to each other all they have received

Article 1185 of the Civil Code provides that:

> ART. 1185. The condition that some event will not happen at a determinate time shall render the obligation effective from the moment the time indicated has elapsed, or if it has become evident that the event cannot occur.
>
> If no time has been fixed, the condition shall be deemed fulfilled at such time as may have probably been contemplated, bearing in mind the nature of the obligation.

Article 1185 provides that if an obligation is conditioned on the non-occurrence of a particular event at a determinate time, that obligation arises (a) at the lapse of the indicated time, or (b) if it has become evident that the event cannot occur.

Petitioner Wellex and respondent U-Land bound themselves to negotiate with each other within a 40-day period to enter into a share

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[174] Id. at 77, *citing Duñgo v. Lopena*, 116 Phil. 1305, 1313–1314 (1962) [Per J. Regala, En Banc].

purchase agreement. If no share purchase agreement was entered into, both parties would be freed from their respective undertakings.

It is the non-occurrence or non-execution of the share purchase agreement that would give rise to the obligation to both parties to free each other from their respective undertakings. This includes returning to each other all that they received in pursuit of entering into the share purchase agreement.

At the lapse of the 40-day period, the parties failed to enter into a share purchase agreement. This lapse is the first circumstance provided for in Article 1185 that gives rise to the obligation. Applying Article 1185, the parties were then obligated to return to each other all that they had received in order to be freed from their respective undertakings.

However, the parties continued their negotiations after the lapse of the 40-day period. They made subsequent transactions with the intention to enter into the share purchase agreement. Despite that, they still failed to enter into a share purchase agreement. Communication between the parties ceased, and no further transactions took place.

It became evident that, once again, the parties would not enter into the share purchase agreement. This is the second circumstance provided for in Article 1185. Thus, the obligation to free each other from their respective undertakings remained.

As such, petitioner Wellex is obligated to return the remittances made by respondent U-Land, in the same way that respondent U-Land is obligated to return the certificates of shares of stock and the land titles to petitioner Wellex.

IV

Respondent U-Land is praying for rescission or resolution under Article 1191, and not rescission under Article 1381

The arguments of the parties generally rest on the propriety of the rescission of the First Memorandum of Agreement. This requires a clarification of rescission under Article 1191, and rescission under Article 1381 of the Civil Code.

Article 1191 of the Civil Code provides:

> ART. 1191. The power to rescind obligations is implied in reciprocal ones, in case one of the obligors should not comply with what is incumbent upon him.
>
> The injured party may choose between the fulfillment and the rescission of the obligation, with the payment of damages in either case. He may also seek rescission, even after he has chosen fulfillment, if the latter should become impossible.
>
> The court shall decree the rescission claimed, unless there be just cause authorizing the fixing of a period.
>
> This is understood to be without prejudice to the rights of third persons who have acquired the thing, in accordance with articles 1385 and 1388 and the Mortgage Law.

Articles 1380 and 1381, on the other hand, provide an enumeration of rescissible contracts:

> ART. 1380. Contracts validly agreed upon may be rescinded in the cases established by law.
>
> ART. 1381. The following contracts are rescissible:
>
> (1) Those which are entered into by guardians whenever the wards whom they represent suffer lesion by more than one-fourth of the value of the things which are the object thereof;
>
> (2) Those agreed upon in representation of absentees, if the latter suffer the lesion stated in the preceding number;
>
> (3) Those undertaken in fraud of creditors when the latter cannot in any other manner collect the claims due them;
>
> (4) Those which refer to things under litigation if they have been entered into by the defendant without the knowledge and approval of the litigants or of competent judicial authority;
>
> (5) All other contracts specially declared by law to be subject to rescission.

Article 1383 expressly provides for the subsidiary nature of rescission:

> ART. 1383. The action for rescission is subsidiary; it cannot be instituted except when the party suffering damage has no other legal means to obtain reparation for the same.

Rescission itself, however, is defined by Article 1385:

> ART. 1385. Rescission creates the obligation to return the things which were the object of the contract, together with their fruits, and the price with its interest; consequently, it can be carried out only when he who demands rescission can return whatever he may be obliged to restore.
>
> Neither shall rescission take place when the things which are the object of the contract are legally in the possession of third persons who did not act in bad faith.
>
> In this case, indemnity for damages may be demanded from the person causing the loss.

Gotesco Properties v. Fajardo[175] categorically stated that Article 1385 is applicable to Article 1191:

> At this juncture, it is noteworthy to point out that rescission does not merely terminate the contract and release the parties from further obligations to each other, but abrogates the contract from its inception and restores the parties to their original positions as if no contract has been made. Consequently, mutual restitution, which entails the return of the benefits that each party may have received as a result of the contract, is thus required. To be sure, it has been settled that the effects of rescission as provided for in Article 1385 of the Code are equally applicable to cases under Article 1191, to wit:
>
> x x x x
>
> **Mutual restitution is required in cases involving rescission under Article 1191.** This means bringing the parties back to their original status prior to the inception of the contract. Article 1385 of the Civil Code provides, thus:
>
> > ART. 1385. **Rescission creates the obligation to return the things which were the object of the contract, together with their fruits, and the price with its interest; consequently, it can be carried out only when he who demands rescission can return whatever he may be obligated to restore.**
> >
> > Neither shall rescission take place when the things which are the object of the contract are legally in the possession of third persons who did not act in bad faith.
> >
> > In this case, indemnity for damages may be demanded from the person causing the loss.
>
> **This Court has consistently ruled that this provision applies to rescission under Article 1191**:
>
> > [S]ince Article 1385 of the Civil Code expressly and clearly states

[175] G.R. No. 201167, February 27, 2013, 692 SCRA 319 [Per J. Perlas-Bernabe, Second Division].

> that "rescission creates the obligation to return the things which were the object of the contract, together with their fruits, and the price with its interest," the Court finds no justification to sustain petitioners' position that said Article 1385 does not apply to rescission under Article 1191. x x x[176] (Emphasis from the original, citations omitted)

Rescission, as defined by Article 1385, mandates that the parties must return to each other everything that they may have received as a result of the contract. This pertains to rescission or resolution under Article 1191, as well as the provisions governing all forms of rescissible contracts.

For Article 1191 to be applicable, however, there must be *reciprocal* prestations as distinguished from *mutual* obligations between or among the parties. A prestation is the object of an obligation, and it is the conduct required by the parties to do or not to do, or to give.[177] Parties may be mutually obligated to each other, but the prestations of these obligations are not necessarily reciprocal. The reciprocal prestations must necessarily emanate from the *same* cause that gave rise to the existence of the contract. This distinction is best illustrated by an established authority in civil law, the late Arturo Tolentino:

> This article applies only to reciprocal obligations. It has no application to every case where two persons are mutually debtor and creditor of each other. There must be reciprocity between them. Both relations must arise from the same cause, such that one obligation is correlative to the other. Thus, a person may be the debtor of another by reason of an agency, and his creditor by reason of a loan. They are mutually obligated, but the obligations are not reciprocal. Reciprocity arises from identity of cause, and necessarily the two obligations are created at the same time.[178] (Citation omitted)

Ang Yu Asuncion v. Court of Appeals[179] provides a clear necessity of the cause in perfecting the existence of an obligation:

> An obligation is a juridical necessity to give, to do or not to do (*Art. 1156, Civil Code*). The obligation is constituted upon the concurrence of the essential elements thereof, *viz*: (a) The *vinculum juris* or *juridical tie* which is the efficient cause established by the various sources of obligations (law, contracts, quasi-contracts, delicts and quasi-delicts); (b) the *object* which is the prestation or conduct, required to be observed (to give, to do or not to do); and (c) the *subject-persons* who, viewed from the demandability of the obligation, are the active (obligee)

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176 Id. at 329–330.

177 *Ang Yu Asuncion v. Court of Appeals,* G.R. No. 109125, December 2, 1994, 238 SCRA 602, 610. [Per J. Vitug, En Banc].

178 IV ARTURO M. TOLENTINO, COMMENTARIES AND JURISPRUDENCE ON THE CIVIL CODE OF THE PHILIPPINES 174–175 (1987).

179 G.R. No. 109125, December 2, 1994, 238 SCRA 602 [Per J. Vitug, En Banc].

and the passive (obligor) subjects.[180]

The cause is the *vinculum juris* or juridical tie that essentially binds the parties to the obligation. This linkage between the parties is a binding relation that is the result of their bilateral actions, which gave rise to the existence of the contract.

The failure of one of the parties to comply with its reciprocal prestation allows the wronged party to seek the remedy of Article 1191. The wronged party is entitled to rescission or resolution under Article 1191, and even the payment of damages. It is a principal action precisely because it is a violation of the original reciprocal prestation.

Article 1381 and Article 1383, on the other hand, pertain to rescission where creditors or even third persons not privy to the contract can file an action due to *lesion* or damage as a result of the contract. In *Ong v. Court of Appeals*,[181] this court defined rescission:

> Rescission, as contemplated in Articles 1380, *et seq.*, of the New Civil Code, is a remedy granted by law to the contracting parties and even to third persons, to secure the reparation of damages caused to them by a contract, even if this should be valid, by restoration of things to their condition at the moment prior to the celebration of the contract. It implies a contract, which even if initially valid, produces a lesion or a pecuniary damage to someone.[182] (Citations omitted)

Ong elaborated on the confusion between "rescission" or resolution under Article 1191 and rescission under Article 1381:

> On the other hand, Article 1191 of the New Civil Code refers to rescission applicable to reciprocal obligations. Reciprocal obligations are those which arise from the same cause, and in which each party is a debtor and a creditor of the other, such that the obligation of one is dependent upon the obligation of the other. They are to be performed simultaneously such that the performance of one is conditioned upon the simultaneous fulfillment of the other. Rescission of reciprocal obligations under Article 1191 of the New Civil Code should be distinguished from rescission of contracts under Article 1383. Although both presuppose contracts validly entered into and subsisting and both require mutual restitution when proper, they are not entirely identical.
>
> While Article 1191 uses the term "rescission," the original term which was used in the old Civil Code, from which the article was based, was "resolution." Resolution is a principal action which is based on breach of a party, while rescission under Article 1383 is a subsidiary

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[180] Id. at 610.
[181] 369 Phil. 243 (1999) [Per J. Ynares-Santiago, First Division].
[182] Id. at 251–252.

> action limited to cases of rescission for lesion under Article 1381 of the New Civil Code, which expressly enumerates the following rescissible contracts:
>
> 1. Those which are entered into by guardians whenever the wards whom they represent suffer lesion by more than one fourth of the value of the things which are the object thereof;
>
> 2. Those agreed upon in representation of absentees, if the latter suffer the lesion stated in the preceding number;
>
> 3. Those undertaken in fraud of creditors when the latter cannot in any manner collect the claims due them;
>
> 4. Those which refer to things under litigation if they have been entered into by the defendant without the knowledge and approval of the litigants or of competent judicial authority; [and]
>
> 5. All other contracts specially declared by law to be subject to rescission.[183] (Citations omitted)

When a party seeks the relief of rescission as provided in Article 1381, there is no need for reciprocal prestations to exist between or among the parties. All that is required is that the contract should be among those enumerated in Article 1381 for the contract to be considered rescissible. Unlike Article 1191, rescission under Article 1381 must be a subsidiary action because of Article 1383.

Contrary to petitioner Wellex's argument, this is not rescission under Article 1381 of the Civil Code. This case does not involve prejudicial transactions affecting guardians, absentees, or fraud of creditors. Article 1381(3) pertains in particular to a series of *fraudulent* actions on the part of the debtor who is in the process of transferring or alienating property that can be used to satisfy the obligation of the debtor to the creditor. There is no allegation of fraud for purposes of evading obligations to other creditors. The actions of the parties involving the terms of the First Memorandum of Agreement do not fall under any of the enumerated contracts that may be subject of rescission.

Further, respondent U-Land is pursuing rescission or resolution under Article 1191, which is a principal action. Justice J.B.L. Reyes' concurring opinion in the landmark case of *Universal Food Corporation v. Court of Appeals*[184] gave a definitive explanation on the principal character of

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[183] Id. at 252–253.
[184] 144 Phil. 1 (1970) [J. Castro, En Banc].

resolution under Article 1191 and the subsidiary nature of actions under Article 1381:

> The rescission on account of breach of stipulations is not predicated on injury to economic interests of the party plaintiff but on the breach of faith by the defendant, that violates the reciprocity between the parties. It is not a subsidiary action, and Article 1191 may be scanned without disclosing anywhere that the action for rescission thereunder is subordinated to anything other than the culpable breach of his obligations by the defendant. This rescission is a principal action retaliatory in character, it being unjust that a party be held bound to fulfill his promises when the other violates his. As expressed in the old Latin aphorism: *"Non servanti fidem, non est fides servanda."* Hence, the reparation of damages for the breach is purely secondary.
>
> On the contrary, in the rescission by reason of *lesion* or economic prejudice, the cause of action is subordinated to the existence of that prejudice, because it is the *raison detre* as well as the measure of the right to rescind. Hence, where the defendant makes good the damages caused, the action cannot be maintained or continued, as expressly provided in Articles 1383 and 1384. But the operation of these two articles is limited to the cases of rescission for *lesión* enumerated in Article 1381 of the Civil Code of the Philippines, and does not apply to cases under Article 1191.[185]

Rescission or resolution under Article 1191, therefore, is a principal action that is immediately available to the party at the time that the reciprocal prestation was breached. Article 1383 mandating that rescission be deemed a subsidiary action cannot be applicable to rescission or resolution under Article 1191.

Thus, respondent U-Land correctly sought the principal relief of rescission or resolution under Article 1191. The obligations of the parties gave rise to reciprocal prestations, which arose from the same cause: the desire of both parties to enter into a share purchase agreement that would allow both parties to expand their respective airline operations in the Philippines and other neighboring countries.

V

The jurisprudence relied upon by petitioner Wellex is not applicable

The cases that petitioner Wellex cited to advance its arguments against respondent U-Land's right to rescission are not in point.

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[185] J. J.B.L. Reyes, concurring opinion in *Universal Food Corporation v. Court of Appeals*, 144 Phil. 1, 21–22 (1970) [J. Castro, En Banc].

Suria v. Intermediate Appellate Court is not applicable. In that case, this court specifically stated that the parties entered into a contract of sale, and their reciprocal obligations had already been fulfilled:[186]

> There is no dispute that the parties entered into a contract of sale as distinguished from a contract to sell.
>
> By the contract of sale, the vendor obligates himself to transfer the ownership of and to deliver a determinate thing to the buyer, who in turn, is obligated to pay a price certain in money or its equivalent (Art. 1458, Civil Code). **From the respondents' own arguments, we note that they have fully complied with their part of the reciprocal obligation. As a matter of fact, they have already parted with the title as evidenced by the transfer certificate of title in the petitioners' name as of June 27, 1975.**
>
> The buyer, in turn, fulfilled his end of the bargain when he executed the deed of mortgage. The payments on an installment basis secured by the execution of a mortgage took the place of a cash payment. In other words, the relationship between the parties is no longer one of buyer and seller because the contract of sale has been perfected and consummated. It is already one of a mortgagor and a mortgagee. In consideration of the petitioners' promise to pay on installment basis the sum they owe the respondents, the latter have accepted the mortgage as security for the obligation.
>
> The situation in this case is, therefore, different from that envisioned in the cited opinion of Justice J.B.L. Reyes. The petitioners' breach of obligations is not with respect to the perfected contract of sale but in the obligations created by the mortgage contract. *The remedy of rescission is not a principal action retaliatory in character but becomes a subsidiary one which by law is available only in the absence of any other legal remedy. (Art. 1384, Civil Code).*
>
> Foreclosure here is not only a remedy accorded by law but, as earlier stated, is a specific provision found in the contract between the parties.[187] (Emphasis supplied)

In *Suria*, this court clearly applied rescission under Article 1384 and *not* rescission or resolution under Article 1191. In addition, the First Memorandum of Agreement is not a contract to sell shares of stock. It is an agreement to negotiate with the view of entering into a share purchase agreement.

Villaflor v. Court of Appeals is not applicable either. In *Villaflor*, this court held that non-payment of consideration of contracts only gave rise to the right to sue for collection, but this non-payment cannot serve as proof of

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186 *Suria v. Intermediate Appellate Court*, 235 Phil. 661, 668–669 (1987) [Per J. Gutierrez, Jr., Second Division].

187 Id.

a simulated contract.[188] The case did not rule that the vendor has no obligation to deliver the thing sold if the buyer fails to fully pay the price required by the contract. In *Villaflor*:

> Petitioner insists that nonpayment of the consideration in the contracts proves their simulation. We disagree. Nonpayment, at most, gives him only the right to sue for collection. Generally, in a contract of sale, payment of the price is a resolutory condition and the remedy of the seller is to exact fulfillment or, in case of a substantial breach, to rescind the contract under Article 1191 of the Civil Code. However, failure to pay is not even a breach, but merely an event which prevents the vendor's obligation to convey title from acquiring binding force.[189] (Citations omitted)

This court's statement in *Villaflor* regarding rescission under Article 1191 was a mere *obiter dictum*. In *Land Bank of the Philippines v. Suntay*,[190] this court discussed the nature of an *obiter dictum:*

> An *obiter dictum* has been defined as an opinion expressed by a court upon some question of law that is not necessary in the determination of the case before the court. It is a remark made, or opinion expressed, by a judge, in his decision upon a cause by the way, that is, incidentally or collaterally, and not directly upon the question before him, or upon a point not necessarily involved in the determination of the cause, or introduced by way of illustration, or analogy or argument. It does not embody the resolution or determination of the court, and is made without argument, or full consideration of the point. It lacks the force of an adjudication, being a mere expression of an opinion with no binding force for purposes of *res judicata*.[191] (Citations omitted)

Petitioner Wellex's reliance on *Padilla v. Spouses Paredes* and *Spouses Agustin v. Court of Appeals* is also misplaced. In these cases, this court held that there can be no rescission for an obligation that is non-existent, considering that the suspensive condition that will give rise to the obligation has not yet happened. This is based on an allegation that the contract involved is a contract to sell. In a contract to sell, the failure of the buyer to pay renders the contract without effect. A suspensive condition is one whose non-fulfillment prevents the existence of the obligation.[192] Payment of the purchase price, therefore, constitutes a suspensive condition in a contract to sell. Thus, this court held that non-remittance of the full price allowed the seller to withhold the transfer of the thing to be sold.

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188 345 Phil. 524, 570 (1997) [Per J. Panganiban, Third Division].
189 Id.
190 G.R. No. 188376, December 14, 2011, 662 SCRA 614 [Per J. Bersamin, First Division].
191 Id. at 647–648.
192 *Diego v. Diego*, G.R. No. 179965, February 20, 2013, 691 SCRA 361, 378 [Per J. Del Castillo, Second Division], citing *Luzon Development Bank v. Enriquez*, G.R. Nos. 168646 & 168666, January 12, 2011, 639 SCRA 332, 351. [Per J. Del Castillo, First Division].

In this case, the First Memorandum of Agreement is not a contract to sell. Entering into the share purchase agreement or the joint development agreement remained a stipulation that the parties themselves agreed to pursue in the First Memorandum of Agreement.

Based on the First Memorandum of Agreement, the execution of the share purchase agreement was necessary to put into effect respondent U-Land's purchase of the shares of stock. This is the stipulation indicated in this memorandum of agreement. There was no suspensive condition of full payment of the purchase price needed to execute either the share purchase agreement or the joint development agreement. Upon the execution of the share purchase, the obligation of petitioner Wellex to transfer the shares of stock and of respondent U-Land to pay the price of these shares would have arisen.

Enforcement of Section 9 of the First Memorandum of Agreement has the same effect as rescission or resolution under Article 1191 of the Civil Code. The parties are obligated to return to each other all that they may have received as a result of the breach by petitioner Wellex of the reciprocal obligation. Therefore, the Court of Appeals did not err in affirming the rescission granted by the trial court.

VI

Petitioner Wellex was not guilty of fraud but of violating Article 1159 of the Civil Code

In the issuance of the Writ of Preliminary Attachment, the lower court found that petitioner Wellex committed fraud by inducing respondent U-Land to purchase APIC shares and PEC shares and by leading the latter to believe that APC was a subsidiary of APIC.

Determining the existence of fraud is not necessary in an action for rescission or resolution under Article 1191. The existence of fraud must be established if the rescission prayed for is the rescission under Article 1381.

However, the existence of fraud is a question that the parties have raised before this court. To settle this question with finality, this court will examine the established facts and determine whether petitioner Wellex indeed defrauded respondent U-Land.

In *Tankeh v. Development Bank of the Philippines*,[193] this court enumerated the relevant provisions of the Civil Code on fraud:

> Fraud is defined in Article 1338 of the Civil Code as:
>
> > x x x fraud when, through insidious words or machinations of one of the contracting parties, the other is induced to enter into a contract which, without them, he would not have agreed to.
>
> This is followed by the articles which provide legal examples and illustrations of fraud.
>
> > . . . .
> >
> > Art. 1340. The usual exaggerations in trade, when the other party had an opportunity to know the facts, are not in themselves fraudulent. (n)
> >
> > Art. 1341. A mere expression of an opinion does not signify fraud, unless made by an expert and the other party has relied on the former's special knowledge. (n)
> >
> > Art. 1342. Misrepresentation by a third person does not vitiate consent, unless such misrepresentation has created substantial mistake and the same is mutual. (n)
> >
> > Art. 1343. Misrepresentation made in good faith is not fraudulent but may constitute error. (n)
>
> The distinction between fraud as a ground for rendering a contract voidable or as basis for an award of damages is provided in Article 1344:
>
> > In order that fraud may make a contract voidable, it should be serious and should not have been employed by both contracting parties.
> >
> > Incidental fraud only obliges the person employing it to pay damages. (1270)[194]

Tankeh further discussed the degree of evidence needed to prove the existence of fraud:

> [T]he standard of proof required is clear and convincing evidence. This standard of proof is derived from American common law. It is less than proof beyond reasonable doubt (for criminal cases) but greater than preponderance of evidence (for civil cases). The degree of believability

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193 G.R. No. 171428, November 11, 2013, 709 SCRA 19 [Per J. Leonen, Third Division].
194 Id. at 44–45.

> is higher than that of an ordinary civil case. Civil cases only require a preponderance of evidence to meet the required burden of proof. However, when fraud is alleged in an ordinary civil case involving contractual relations, an entirely different standard of proof needs to be satisfied. The imputation of fraud in a civil case requires the presentation of clear and convincing evidence. Mere allegations will not suffice to sustain the existence of fraud. The burden of evidence rests on the part of the plaintiff or the party alleging fraud. The quantum of evidence is such that fraud must be clearly and convincingly shown.[195]

To support its allegation of fraud, Mr. Tseng, respondent U-Land's witness before the trial court, testified that Mr. Gatchalian approached respondent U-Land on two (2) separate meetings to propose entering into an agreement for joint airline operations in the Philippines. Thus, the parties entered into the First Memorandum of Agreement. Respondent U-Land primarily anchors its allegation of fraud against petitioner Wellex on the existence of the second preambular clause of the First Memorandum of Agreement.

In its Appellant's Brief before the Court of Appeals, petitioner Wellex admitted that "[t]he amount of US$7,499,945.00 was remitted for the purchase of APIC and PEC shares."[196] In that brief, it argued that the parties were already in the process of partially executing the First Memorandum of Agreement.

As held in *Tankeh*, there must be clear and convincing evidence of fraud. Based on the established facts, respondent U-Land was unable to clearly convince this court of the existence of fraud.

Respondent U-Land had every reasonable opportunity to ascertain whether APC was indeed a subsidiary of APIC. This is a multimillion dollar transaction, and both parties admitted that the share purchase agreement underwent several draft creations. Both parties admitted the participation of their respective counsels in the drafting of the First Memorandum of Agreement. Respondent U-Land had every opportunity to ascertain the ownership of the shares of stock.

Respondent U-Land itself admitted that it was not contesting petitioner Wellex's ownership of the APIC shares or APC shares; hence, it was not contesting the existence of the Second Memorandum of Agreement. Upon becoming aware of petitioner Wellex's representations concerning APIC's ownership or control of APC as a subsidiary, respondent U-Land continued to make remittances totalling the amount sought to be rescinded. It had the option to opt out of negotiations after the lapse of the 40-day

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195 Id. at 52.
196 *Rollo*, p. 127.

period. However, it proceeded to make the remittances to petitioner Wellex and proceed with negotiations.

Respondent U-Land was not defrauded by petitioner Wellex to agree to the First Memorandum of Agreement. To constitute fraud under Article 1338, the words and machinations must have been so insidious or deceptive that the party induced to enter into the contract would not have agreed to be bound by its terms if that party had an opportunity to be aware of the truth.[197]

Respondent U-Land was already aware that APC was not a subsidiary of APIC after the 40-day period. Still, it agreed to be bound by the First Memorandum of Agreement by making the remittances from June 30 to September 25, 1998.[198] Thus, petitioner Wellex's failure to inform respondent U-Land that APC was not a subsidiary of APIC when the First Memorandum of Agreement was being executed did not constitute fraud.

However, the absence of fraud does not mean that petitioner Wellex is free of culpability. By failing to inform respondent U-Land that APC was not yet a subsidiary of APIC at the time of the execution of the First Memorandum of Agreement, petitioner Wellex violated Article 1159 of the Civil Code. Article 1159 reads:

> ART. 1159. Obligations arising from contracts have the force of law between the contracting parties and should be complied with in good faith.

In *Ochoa v. Apeta*,[199] this court defined good faith:

> Good faith is an intangible and abstract quality with no technical meaning or statutory definition, and it encompasses, among other things, an honest belief, the absence of malice and the absence of design to defraud or to seek an unconscionable advantage. It implies honesty of intention, and freedom from knowledge of circumstances which ought to put the holder upon inquiry. The essence of good faith lies in an honest belief in the validity of one's right, ignorance of a superior claim and absence of intention to overreach another.[200] (Citations omitted)

It was incumbent upon petitioner Wellex to negotiate the terms of the pending share purchase agreement in good faith. This duty included providing a full disclosure of the nature of the ownership of APIC in APC.

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197 *Tankeh v, Development Bank of the Philippines*, G.R. No. 171428, November 11, 2013, 709 SCRA 19, 50 [Per J. Leonen, Third Division], citing *Viloria v. Continental Airlines*, G.R. No. 188288, January 16, 2012, 663 SCRA 57, 81. [Per J. Reyes, Second Division].

198 *Rollo*. pp. 99–100 and 324.

199 559 Phil. 650 (2007) [Per. J. Sandoval-Gutierrez, First Division].

200 Id. at 655–656.

Unilaterally compelling respondent U-Land to remit money to finalize the transactions indicated in the Second Memorandum of Agreement cannot constitute good faith.

The absence of fraud in a transaction does not mean that rescission under Article 1191 is not proper. This case is not an action to declare the First Memorandum of Agreement null and void due to fraud at the inception of the contract or *dolo causante*. This case is not an action for fraud based on Article 1381 of the Civil Code. Rescission or resolution under Article 1191 is predicated on the failure of one of the parties in a reciprocal obligation to fulfill the prestation as required by that obligation. It is not based on vitiation of consent through fraudulent misrepresentations.

VII

Respondent U-Land was not bound to pay the US$3 million under the joint development agreement

The alleged failure of respondent U-Land to pay the amount of US$3 million to petitioner Wellex does not justify the actions of the latter in refusing to return the US$7,499,945.00.

Article 1374 of the Civil Code provides that:

> ART. 1374. The various stipulations of a contract shall be interpreted together, attributing to the doubtful ones that sense which may result from all of them taken jointly.

The execution of the joint development agreement was contingent on the execution of the share purchase agreement. This is provided for in Section 4 of the First Memorandum of Agreement, which stated that the execution of the two agreements is "[s]imultaneous."[201] Thus, the failure of the share purchase agreement's execution would necessarily mean the failure of the joint development agreement's execution.

Section 9 of the First Memorandum of Agreement provides that should the parties fail to execute the agreement, they would be released from their mutual obligations. Had respondent U-Land paid the US$3 million and petitioner Wellex delivered the 57,000,000 PEC shares for the purpose of the joint development agreement, they would have been obligated to return these to each other.

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[201] *Rollo*, p. 61.

Section 4 and Section 9 of the First Memorandum of Agreement must be interpreted together. Since the parties were unable to agree on a final share purchase agreement and there was no exchange of money or shares of stock due to the continuing negotiations, respondent U-Land was no longer obliged to provide the money for the real estate development projects. The payment of the US$3 million was for pursuing the real estate development projects under the joint development agreement. There being no joint development agreement, the obligation to deliver the US$3 million and the delivery of the PEC shares for that purpose were no longer incumbent upon the parties.

VIII

Respondent U-Land was not obligated to exhaust the "securities" given by petitioner Wellex

Contrary to petitioner Wellex's assertion, there is no obligation on the part of respondent U-Land to exhaust the "securities" given by petitioner Wellex. No such meeting of the minds to create a guarantee or surety or any other form of security exists. The principal obligation is not a loan or an obligation subject to the conditions of sureties or guarantors under the Civil Code. Thus, there is no need to exhaust the securities given to respondent U-Land, and there is no need for a legal condition where respondent U-Land should pursue other remedies.

Neither petitioner Wellex nor respondent U-Land stated that there was already a transfer of ownership of the shares of stock or the land titles. Respondent U-Land itself maintained that the delivery of the shares of stock and the land titles were not in the nature of a pledge or mortgage.[202] It received the certificates of shares of stock and the land titles with an understanding that the parties would subsequently enter a share purchase agreement. There being no share purchase agreement, respondent U-Land is obligated to return the certificates of shares of stock and the land titles to petitioner Wellex.

The parties are bound by the 40-day period provided for in the First Memorandum of Agreement. Adherence by the parties to Section 9 of the First Memorandum of Agreement has the same effect as the rescission or resolution prayed for and granted by the trial court.

Informal acts are prone to ambiguous legal interpretation. This will be based on the say-so of each party and is a fragile setting for good business

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[202] Id. at 325.

transactions. It will contribute to the unpredictability of the market as it would provide courts with extraordinary expectations to determine the business actor's intentions. The parties appear to be responsible businessmen who know that their expectations and obligations should be clearly articulated between them. They have the resources to engage legal representation. Indeed, they have reduced their agreement in writing.

Petitioner Wellex now wants this court to define obligations that do not appear in these instruments. We cannot do so. This court cannot interfere in the bargains, good or bad, entered into by the parties. Our duty is to affirm legal expectations, not to guarantee good business judgments.

WHEREFORE, the petition is **DENIED.** The Decision of the Regional Trial Court in Civil Case No. 99-1407 and the Decision of the Court of Appeals in CA-G.R. CV No. 74850 are **AFFIRMED.** Costs against petitioner The Wellex Group, Inc.

SO ORDERED.

MARVIC M.V.F. LEONEN
Associate Justice

WE CONCUR:

ANTONIO T. CARPIO
Associate Justice
Chairperson

PRESBITERO J. VELASCO, JR.
Associate Justice

MARIANO C. DEL CASTILLO
Associate Justice

JOSE CATRAL MENDOZA
Associate Justice

ATTESTATION

I attest that the conclusions in the above Decision had been reached in consultation before the case was assigned to the writer of the opinion of the Court's Division.

ANTONIO T. CARPIO
Associate Justice
Chairperson, Second Division

CERTIFICATION

Pursuant to Section 13, Article VIII of the Constitution and the Division Chairperson's Attestation, I certify that the conclusions in the above Decision had been reached in consultation before the case was assigned to the writer of the opinion of the Court's Division.

MARIA LOURDES P. A. SERENO
Chief Justice