Revisiting the Equality in Equity Doctrine in Light of the FRIA of 2010: Are Secured and Unsecured Creditors Still on Equal Footing During Rehabilitation Proceedings?

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I. INTRODUCTION

In the absence of a comprehensive legislation governing the effective rehabilitation of financially distressed corporations in the Philippines, the concept of Corporate Rehabilitation was not something clearly delineated in our jurisdiction. The Insolvency Law,[1] enacted in 1909 and patterned after

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1. An Act Providing for the Suspension of Payments, the Relief of Insolvent Debtors, the Protection of Creditors, and the Punishment of Fraudulent Debtors [The Insolvency Law], Act No. 1956 (1909).

the Insolvency Act of California of 1985,[2] merely provided for two remedies for distressed corporations, namely: (1) suspension of payments;[3] and (2) declaration of insolvency.[4] Under the first remedy, a debtor with sufficient property to cover all his debts, but who "foresees the impossibility of meeting them when they respectively fall due, may petition that he be declared in the state of suspension of payments" by the courts.[5] As can be gleaned from the wording of the applicable provision, this option is only available to solvent debtors.[6] The second remedy, on the other hand, can either be voluntary or involuntary. In the former, it is the insolvent debtor himself, by filing a petition in court, who applies to be adjudged insolvent and be discharged from its liabilities.[7] In the latter, the adjudication of insolvency is made based on a petition filed by three or more creditors on the ground of the debtor's "acts of insolvency," as enumerated by law.[8]

Sixty-seven years after the enactment of the Insolvency Act, Presidential Decree (P.D.) 902-A[9] was passed with the view of addressing the needs of modern commercial businesses and of attracting more domestic and foreign investments.[10] This law expanded the options available to financially distressed corporations and allowed debtors whose liabilities are more than their assets to undergo rehabilitation proceedings.[11] By virtue of P.D. 902-A, the Securities and Exchange Commission (SEC) was given the authority to create and appoint a management committee, board, or body and to approve Corporate Rehabilitation plans.[12] Rehabilitation has been defined as "the restoration of the debtor to a position of successful operation and solvency, if

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2. ASIAN DEVELOPMENT BANK, THE ASIA-PACIFIC RESTRUCTURING AND INSOLVENCY GUIDE 2006 134 (2006).
3. *See generally* The Insolvency Law, ch. II.
4. *See generally* The Insolvency Law, chs. III & IV.
5. *Id.* § 2.
6. *Id.*
7. *Id.* § 14.
8. *Id.* § 20.
9. Reorganization of the Securities and Exchange Commission with Additional Powers and Placing the Said Agency Under the Administrative Supervision of the Office of the President, Presidential Decree (P.D.) 902-A (1976).
10. ASIAN DEVELOPMENT BANK, *supra* note 2, at 1.
11. P.D. 902-A, § 5 (d).
12. *Id. See also* Amending Further Section 6 of Presidential Decree No. 902-A, Presidential Decree No. 1799, § 1 (d) (1981). Note, however, that jurisdiction over corporate rehabilitation proceedings has since been transferred from the SEC to the regional trial courts. *See* The Securities Regulation Code [THE SECURITIES REGULATION CODE], Republic Act No. 8799 (2000).

it is shown that its continuance of operation is economically feasible."[13] It is something which —

> contemplates a continuance of corporate life and activities in an effort to restore and reinstate the corporation to its former position of successful operation and solvency.[14] When a distressed company is placed under rehabilitation, the appointment of a management committee follows to avoid collusion between the previous management and creditors it might favor, to the prejudice of the other creditors.[15]

With the introduction of Corporate Rehabilitation in our jurisdiction came the issuance of procedural rules that govern the said proceedings, particularly the Rules of Procedure on Corporate Recovery issued in 1999,[16] the Securities Regulation Code in 2000,[17] the Interim Rules on Corporate Rehabilitation in 2000,[18] and the Rules of Procedure on Corporate Rehabilitation in 2009.[19] In 2010, the Financial Rehabilitation and Insolvency Act (FRIA),[20] a comprehensive law on Corporate Rehabilitation and insolvency, was passed in order to "encourage debtors ... to collectively and realistically resolve and adjust competing claims and property rights. ... [T]o ensure or maintain certainty and predictability in commercial affairs, ... [to] recognize creditor rights and respect priority of claims, and ensure equitable treatment of creditors who are similarly situated."[21]

The FRIA provides distressed corporations with three options, namely: (1) court-supervised rehabilitation; (2) pre-negotiated rehabilitation; and (3) out-of-court rehabilitation. The Court-supervised Rehabilitation may either

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13. RULES OF PROCEDURE ON CORPORATE REHABILITATION, A.M. No. 00-8-10-SC, Jan. 16, 2009, rule 2, § 1.
14. Ruby Industrial Corporation v. Court of Appeals, 284 SCRA 445, 460 (1998) (citing New York Title and Mortgage Co., v. Friedman, 276 N.Y.S. 72, 153, Misc. 697 (U.S.)).
15. *Id.* (citing Araneta v. Court of Appeals, 211 SCRA 390 (1992) and Rizal Commercial Banking Corporation v. Intermediate Appellate Court, 213 SCRA 830 (1992)).
16. Securities and Exchange Commission, Rules of Procedure on Corporate Recovery (Jan. 15, 2000).
17. THE SECURITIES REGULATION CODE.
18. INTERIM RULES OF PROCEDURE ON CORPORATE REHABILITATION, A.M. No. 00-8-10-SC, Nov. 21, 2000.
19. RULES OF PROCEDURE ON CORPORATE REHABILITATION.
20. An Act Providing for the Rehabilitation or Liquidation of Financially Distressed Enterprises and Individuals [Financial Rehabilitation and Insolvency Act (FRIA) of 2010], Republic Act No. 10142 (2010).
21. *Id.* § 2.

be a voluntary proceeding[22] initiated by the debtor or an involuntary proceeding commenced by the creditors.[23] On the other hand, a Pre-negotiated Rehabilitation is when the insolvent debtor files a petition for the approval of a Rehabilitation Plan which, in turn, has been approved by creditors "holding at least two-thirds of the total liabilities of the debtor, including secured creditors holding more than fifty per cent (50%) of the total secured claims of the debtor and unsecured creditors holding more than fifty per cent (50%) of the total unsecured claims of the debtor."[24] Finally, an Out-of-court Rehabilitation must meet the following requisites: (a) the debtor must agree to the Plan; (b) it must be approved by creditors representing at least sixty-seven per cent (67%) of the secured obligations of the debtor; (c) it must be approved by creditors representing at least seventy-five per cent (75%) of the unsecured obligations of the debtor; and (d) it must be approved by creditors holding at least eighty-five per cent (85%) of the total liabilities of the debtor.[25]

Corporate Rehabilitation, being anchored on the continuance of corporate life, seeks to ensure that the assets of a corporation under rehabilitation proceedings are preserved for the benefit of all creditors, in line with the goal of putting the said corporation back on its feet. This Essay will revisit the principle of Equality in Equity, where secured and unsecured creditors are placed on equal footing during rehabilitation proceedings, in light of the passage of the FRIA in 2010. The first part of the discussion will analyze the principle itself and will look into the intent behind the need to place the secured and unsecured creditors on equal footing pending the said proceedings. This will be followed by a discussion which traces the evolution of the doctrine's application in our jurisdiction, as can be gleaned from the jurisprudential decisions of the Supreme Court. Finally, the continued applicability of the principle of Equality in Equity will be assessed, in light of the provisions of the FRIA.

II. EQUALITY IN EQUITY DOCTRINE

A. Equality in Equity Doctrine and Its Rationale

Before discussing the principle of Equality in Equity, it is first imperative to understand why the concept of preference of credits is important. Preference of credits is grounded on the principle that when the debtor's liabilities exceed his assets, the debtor will inevitably be prevented from satisfying all of

22. *Id.* § 12.

23. *Id.* § 13.

24. *Id.* § 76.

25. *Id.* § 78.

his obligations.[26] This, in turn, gives rise to the necessity of classifying the creditors and making distinctions in order to determine which among the pending claims will first be satisfied.[27] This set-up is neither unjust nor unreasonable since the order of the preference of credits is provided for by law,[28] and hence, one who enters into a contract with another should be aware of his position in relation to other creditors.[29] In other words, it is a creditor's duty to ensure that he is in a more favorable position *vis-à-vis* the other creditors of the same debtor, and if he neglects to do something that will create a preference in his favor (e.g. fails to ask for any security), then he has no one to blame but himself.[30] In *Development Bank of the Philippines v. Secretary of Labor*,[31] the Supreme Court explained the concept of preference of credits, thus —

> A preference of credit bestows upon the preferred creditor an advantage of having his credit satisfied first ahead of other claims which may be established against the debtor. Logically, it becomes material only when the properties and assets of the debtors are insufficient to pay his debts in full; for if the debtor is amply able to pay his various creditors in full, how can the necessity exist to determine which of his creditors shall be paid first or whether they shall be paid out of the proceeds of the sale the debtor's specific property? Indubitably, the preferential right of credit attains significance only after the properties of the debtor have been inventoried and liquidated, and the claims held by his various creditors have been established.[32]

On the other hand, when a corporation is placed under rehabilitation proceedings with the view of preserving and maximizing the assets of the debtor and with the hopes of reviving and strengthening the latter's corporate life, the principle of Equality in Equity, where secured and unsecured creditors are placed on equal footing during rehabilitation proceedings, usually comes into play. This Principle is also in reference to

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26. *See* HECTOR S. DE LEON & HECTOR M. DE LEON, JR., COMMENTS AND CASES ON CREDIT TRANSACTIONS 512-13 (11th ed. 2010).

27. Jose U. Cochingyan III, *Concurrence and Preference of Credits and the Insolvent's Creditors*, 62 PHIL. L.J. 41, 49 (citing V.J. FRANCISCO, 2 CREDIT TRANSACTIONS 1087-88 (1953)).

28. An Act to Ordain and Institute the Civil Code of the Philippines [CIVIL CODE], Republic Act No. 386 (1950).

29. Cochingyan III, *supra* note 27.

30. *Id.*

31. Development Bank of the Philippines v. Secretary of Labor, 179 SCRA 631 (1989).

32. *Id.* at 634-35 (citing Kuenzle & Streiff (Ltd.) v. Villanueva, 41 Phil. 611 (1916); Barretto v. Villanueva, 6 SCRA 928 (1962); and Philippine Savings Bank v. Lantin, 124 SCRA 476 (1983)).

the *pari passu* principle which is considered as "a bastion of equal treatment."[33] In 1887, in the *Matter of Cavin v. Gleason*,[34] Equality in Equity has been explained by the district court of New York, thus —

> It is clear, we think, that upon an accounting in bankruptcy or insolvency, a trust creditor is not entitled to a preference over general creditors of the insolvent, merely on the ground of the nature of his claim, that is, that he is a trust creditor as distinguished from a general creditor. We know of no authority for such a contention. The equitable doctrine that as between creditors[,] equality i[n] equity, admits, so far as we know, of no exception founded on the greater supposed sacredness of one debt, or that it arose out of a violation of duty, or that its loss involves greater apparent hardship in one case than another, unless it appears in addition that there is some specific recognized equity founded on some agreement, or the relation of the debt to the assigned property, which entitles the claimant, according to equitable principles, to preferential payment. [35]

Equality in Equity is grounded on the very purpose for which a rehabilitation proceeding is undertaken. Preferences tend to create controversy among creditors and would urge those who consider themselves "preferred" to rush to the courts upon learning of the debtor's insolvency. Instead of focusing on rehabilitating the corporation, efforts will then be placed in defending against the said claims.[36] As a result, it would frustrate the goal of the proceedings, which is to put the corporate back into shape.[37] It must be noted, however, that this Doctrine operates only for so long as the corporation is under rehabilitation proceedings. If the said corporation has prospered back to its solvent state, or if the attempt to rehabilitate it fails, the secured creditors will again be able to enforce their preferential right over their claim.[38] In other words, Equality in Equity only operates upon the appointment of the management committee or rehabilitation receiver and remains operative only during the pendency of the said proceedings.[39]

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33. Kevin Kilgour, *Equality Redefined: Reassessing the Rationale of Voidable Preference Law*, 11 UCL JURIS. REV. 252, 253 (2004) (citing Adrian J. Walters, *Preferences*, *in* VULNERABLE TRANSACTIONS IN CORPORATE INSOLVENCY (J. Armour & H. Bennett eds., 2003).
34. Matter of Cavin v. Gleason, 60 Sickels 256, 11 N.E. 504 (1887) (U.S).
35. *Id.* at 262.
36. *See generally* BF Homes, Inc. v. Court of Appeals, 190 SCRA 262 (1990).
37. *See generally* Roberts v. Edie, 85 Md 181, 36 Atl. 820 (1897) (U.S.) & Ramisch v. Fulton, 41 Ohio App. 443, 180 N.E. 735 (1932) (U.S.).
38. Arturo M. De Castro, *Equality in Equity: Equal Footing of Secured and Unsecured Creditors in Suspension of Payments and Rehabilitation Proceedings*, 49 ATENEO L.J. 32, 41 (2004).
39. Castillo v. Uniwide Warehouse Club Inc., 619 SCRA 641, 647 (2010).

B. Equality in Equity in the Philippines

The application of Equality in Equity in our jurisdiction has evolved through our jurisprudence, largely because of the absence of a comprehensive law which clearly settles the matter. Thus, the Supreme Court initially rendered flip-flopping decisions regarding its application, until a settled doctrine has been reached and has been consistently applied since. In this Part of this Essay, a specific jurisprudence representative of a certain time frame, with the corresponding applicable doctrine during that time, will be discussed to enable us to trace the evolution and development of the application of the said Principle in our jurisdiction.

a. Tracing the Jurisprudential Development of Equality in Equity

Central Bank of the Philippines v. Morfe,[40] promulgated in 1975, involves the question of whether a final judgment for the payment of a time deposit in a savings bank which was obtained after the bank had already been declared insolvent, may be enforced against the bank as a preferred credit. In the said judgment, Fidelity Savings Bank was ordered to pay the Elizes spouses the sum of ₱50,584.00 plus accumulated interest. Because of this, other creditors followed suit and filed their respective claims.[41] The lower court further issued an order to Central Bank, the liquidator, to pay the time deposits "as *preferred judgments, evidenced by final judgments*."[42] In ruling against the said creditors, the Supreme Court recognized the application of Equality in Equity, thus —

> We are of the opinion that such judgments cannot be considered preferred and that article 2244 (14) (b) [of the Civil Code] does not apply to judgments for the payment of the deposits in an insolvent savings bank which were obtained after the declaration of insolvency. ... To recognize such judgments as entitled to priority would mean that depositors in insolvent banks, after learning that the bank is insolvent as shown by the fact that it can no longer pay withdrawals or that it has closed its doors or has been enjoined by the Monetary Board from doing business, would rush to the courts to secure judgments for the payment of their deposits.
>
> In such an eventuality, the courts would be swamped with suits of that character. Some of the judgments would be default judgments. Depositors armed with such judgments would pester the liquidation court with claims for preference on the basis of article 2244 (14) (b). Less alert depositors would be prejudiced. That inequitable situation could not have been contemplated by the framers of section 29.[43]

40. Central Bank of the Philippines v. Morfe, 63 SCRA 114 (1975).

41. *Id.* at 115.

42. *Id.* at 116.

43. *Id.* at 119-20.

In 1989, however, with the promulgation of *Philippine Commercial International Bank v. Court of Appeals*,[44] the Supreme Court has abandoned Equality in Equity, and instead, recognized the preference of credits. The Supreme Court, citing the 1921 case of *Chartered Bank v. Imperial and National Bank*,[45] ruled that the suspension of payments may only be applied to unsecured creditors and cannot cover creditors holding a mortgage, pledge, or lien, whose rights shall be respected at all times.[46] The Court even went as far as saying that "to hold otherwise would render the said rights inutile and illusory."[47]

In 1990, only a year after disregarding the principle of Equality in Equity in *Philippine Commercial International Bank*, the Supreme Court again recognized its application in *Alemar's Sibal and Sons v. Elbinias*.[48] In this case, the petitioner, Alemar's Bookstore, was placed under rehabilitation proceedings and yet, the lower court still issued an order commanding the said Bookstore to pay G.A. Yupangco, one of their creditors.[49] In compliance with the writ of execution, the Bank of the Philippine Islands allowed a certain check to be encashed as a payment to the said creditor. The petitioner opposed this on the ground that making the payment will, in effect, defeat the purpose for which it was placed under receivership.[50] The lower court ruled against the petitioner and decreed that "to discharge the writ will leave plaintiff with no recourse to enforce the judgment in its favor."[51] However, the Supreme Court overturned this and took note of the fact that the SEC explicitly ordered, without distinctions, that "all actions for claims against the corporation pending before any court ... are suspended accordingly."[52] Thus, it was held that —

> During rehabilitation receivership, the assets are held in trust for the equal benefit of all creditors to preclude one from obtaining an advantage or preference over another by the expediency of an attachment, execution, or otherwise. For what would prevent an alert creditor, upon learning of the receivership, from rushing posthaste to the courts to secure judgments for the satisfaction of its claims to the prejudice of the less alert creditors.

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44. Philippine Commercial International Bank v. Court of Appeals, 172 SCRA 436 (1989).
45. Chartered Bank v. Imperial and National Bank, 48 Phil. 931 (1921).
46. *Philippine Commercial International Bank*, 172 SCRA at 440.
47. *Id.* at 441.
48. Alemar's Sibal and Sons, Inc. v. Elbinias, 186 SCRA 94 (1990).
49. *Id.* at 95-96.
50. *Id.* at 97.
51. *Id.* at 98.
52. *Id.*

> *As between creditors, the key phrase is 'equality is equity.'* When a corporation threatened by bankruptcy is taken over by a receiver, all the creditors should stand on an equal footing. Not anyone of them should be given any preference by paying one or some of them ahead of the others. This is precisely the reason for the suspension of all pending claims against the corporation under receivership. *Instead of creditors vexing the courts with suits against the distressed firm, they are directed to file their claims with the receiver who is a duly appointed officer of the SEC.*[53]

Thus, when a ruling was made in favor of G.A. Yupangco in the collection case, the said ruling was only meant to determine the indebtedness of Alemar's Bookstore. However, such was not an authority to give G.A. Yupangco the right to enforce its claim at once, as such will frustrate the very purpose for which the petitioner was placed under receivership.[54]

In 1994, the Supreme Court, in *Bank of Philippine Islands v. Court of Appeals*,[55] expressly stated that the ruling in *Philippine Commercial International Bank* has since been abrogated[56] by the rulings of the Court after 1989, expressly recognizing the application of Equality in Equity in our jurisdiction. This Doctrine has been consistently applied since then.[57] In 1999, the Supreme Court, in *Rizal Commercial Banking Corporation v. Intermediate Appellate Court*,[58] laid down "rules of thumb" regarding the matter, to wit: (1) All pending claims against debtor-corporations, partnerships, or associations, whether secured or unsecured, shall be suspended upon the appointment of a management committee or a rehabilitation receiver; and (2) Even though secured creditors retain their preference over unsecured creditors, the enforcement of such preferred claim is suspended upon the appointment of a management committee or rehabilitation receiver.[59]

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53. *Id.* at 99-100 (citing *Central Bank of the Philippines*, 63 SCRA 114) (emphasis supplied).
54. *Alemar's Sibal and Sons, Inc.*, 186 SCRA at 100.
55. Bank of Philippine Islands v. Court of Appeals, 229 SCRA 223 (1994).
56. *Id.* at 227.
57. *See generally Ruby Industrial Corporation*, 284 SCRA 445; Rizal Commercial Banking Corporation v. Intermediate Appellate Court, 320 SCRA 279 (1999); Philippine Airlines, Inc. v. National Labor Relations Commission, 634 SCRA 19 (2010); Sobrejuanite v. ASB Development Corporation, 471 SCRA 763 (2005); and New Frontier Sugar Corporation v. Regional Trial Court, 513 SCRA 601 (2007).
58. *Rizal Commercial Banking Corporation*, 320 SCRA at 279.
59. *Id.* at 293.

In April of 2010, the Court, in *Castillo v. Uniwide Warehouse Club Inc.*,[60] had the occasion to discuss in detail the standing of creditors when a distressed corporation is placed under rehabilitation proceedings. In this case, the SEC approved the petition of Uniwide Group of Companies for suspension of payments and its proposed rehabilitation plan. The issue here is whether the proceedings for illegal dismissal of employees against the company, where backwages and damages were also claimed, should likewise be suspended.[61] In ruling that the said proceedings must likewise be suspended, the Court cited the rulings in *Finasia Investments and Finance Corporation v. Court of Appeals*,[62] where the term "claim" was used to refer to debts or demands of a pecuniary nature; *Arranza v. B.F. Homes, Inc.*,[63] where it was construed to refer to actions involving monetary considerations;[64] *Philippine Airlines v. Kurangking*,[65] where the term was defined as the right to payment of whatever nature — liquidated or unliquidated, fixed or contingent, matured or unmatured, disputed or undisputed, legal or equitable, and *secured or unsecured*.[66] Thus, the Court ruled that rehabilitation proceedings will have the effect of suspending all actions involving all kinds of claims against the distressed corporation — whether for damages arising from a breach of contract, labor case, collection suit or any other claims of a pecuniary nature.[67] It further noted that the rules on Corporate Rehabilitation promulgated in 2009, as well as the interim rules, provide an all-embracing definition of a "claim," which includes "*all* claims of whatever nature or character against a debtor or its property, whether for money or otherwise."[68] In further emphasizing the suspension of all types of claims, without any distinction whatsoever, whenever a corporation is under rehabilitation proceedings, the Supreme Court has this to say —

> Jurisprudence is settled that the suspension of proceedings referred to in the law uniformly applies to 'all actions for claims.' ... In the oft-cited case of *Rubberworld (Phils.) Inc. v. NLRC*, the Court noted that aside from the given exception, the law is clear and makes no distinction as to the claims that are suspended once a management committee is created or a

60. *Castillo*, 619 SCRA 641.

61. *Id.*

62. Finasia Investments and Finance Corporation v. Court of Appeals, 237 SCRA 446 (1994).

63. Arranza v. B.F. Homes, Inc., 333 SCRA 799 (2000).

64. *Id.* at 816.

65. Philippine Airlines v. Kurangking, 389 SCRA 588 (2002).

66. *Id.* at 593 (emphasis supplied).

67. *Id.* at 648 (citing Philippine Airlines, Inc. v. Zamora, 514 SCRA 548, 605 (2007)).

68. *Id.* at 648 (citing RULES OF PROCEDURE ON CORPORATE REHABILITATION, rule 2, § 1) (emphasis supplied).

> rehabilitation receiver is appointed. Since the law makes no distinction or exemptions, neither should this Court. *Ubi lex non distinguit nec nos distinguere debemos.* ... [F]or indeed[,] the indiscriminate suspension of actions for claims intends to expedite the rehabilitation of the distressed corporation by enabling the management committee or the rehabilitation receiver to effectively exercise its/his powers free from any judicial or extrajudicial interference that might unduly hinder or prevent the rescue of the debtor company. To allow such other actions to continue would only add to the burden of the management committee or rehabilitation receiver, whose time, effort and resources would be wasted in defending claims against the corporation, instead of being directed toward its restructuring and rehabilitation.[69]

III. EQUALITY IN EQUITY DOCTRINE REVISITED IN LIGHT OF THE FRIA

The FRIA was passed merely four months after the Court's decision in *Castillo*, where it held that the suspension of the claims of creditors applies to *all* kinds of pecuniary claims, whether secured or unsecured.[70] Thus, a question now lingers — considering the provisions of the newly-enacted FRIA, does the doctrine of Equality in Equity still hold?

At one glance, it could be said that the FRIA seems to have dispensed with the application of Equality in Equity, taking into consideration Sections 62 and 133 of the said law. Section 62 provides that "the Rehabilitation Plan shall, as a minimum: ... (i) ensure that the payments made under the plan follow the priority established under the provisions of the Civil Code on concurrence and preference of credits and other applicable laws." [71] On the other hand, Section 133 provides that the "Liquidation Plan and its Implementation shall ensure that the concurrence and preference of credits as enumerated in the Civil Code of the Philippines and other relevant laws shall be observed, unless a preferred creditor voluntarily waives his preferred right."[72] These provisions seem to imply that the concurrence and preference of credits provided for under the pertinent laws shall govern and in fact, shall be reflected in the proposed rehabilitation plan of the distressed corporation. However, on a closer look and on a more critical reading of provisions of the FRIA, Equality in Equity was not actually by-passed by the said provisions. Although the said law, as of the writing of this Essay, still has no implementing rules that clearly govern the matter, nor is there any jurisprudential ruling that will shed light on the issue, the continued applicability of Equality in Equity can be argued on two grounds: (1) the

69. *Id.* at 649 (citing Rubberworld (Phils.) Inc. v. NLRC, 305 SCRA 721, 729 (1999)).

70. *Castillo*, 619 SCRA at 648 (citing *Kurangking*, 389 SCRA 588 (2002)).

71. Financial Rehabilitation and Insolvency Act (FRIA) of 2010, § 62.

72. *Id.* § 133.

rationale of rehabilitation proceedings has remained the same even with the passage of the FRIA; and (2) the FRIA has more substantial provisions that override Sections 62 and 133.

A. The Rationale Behind Corporate Rehabilitation

The FRIA is meant to be a comprehensive law that will govern the rehabilitation or liquidation of debtors.[73] Even with its passage, the goal of a rehabilitation proceedings — the restoration of a distressed debtor to a more favorable position — remains the same. Likewise, the intent behind the application of Equality in Equity — to enable the management committee to focus on the rehabilitation of the corporation instead of defending against the claims of creditors pending the proceedings — still holds true. Thus, there is no reason why the said Principle should be held inapplicable now. This will also not prejudice the secured creditors since in case the attempts to restore the distressed corporation to its former glory either succeed or fail and the said proceedings are terminated, the secured creditors can again enforce their preferred credits. In other words, there has been no change in the rationale behind Corporate Rehabilitation that will merit the non-application of the Equality in Equity. For so long as the corporation is still under a management committee or rehabilitation receiver, all claims, except those incurred in the ordinary course of business, must give way to the more crucial objective of resuscitating the corporation.[74]

B. More Substantial Provisions of the FRIA

Another reason why Equality in Equity is argued to be still applicable despite Sections 62 and 133 of the FRIA is the existence of other more substantial provisions in the same law which overrides the notion that preference of credits shall be effective even during the pendency of rehabilitation proceedings. First, Section 16 (q) (1) provides —

> Section 16. Commencement of Proceedings and Issuance of a Commencement Order. — The rehabilitation proceedings shall commence upon the issuance of the Commencement Order, which shall:
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> ...
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> (q) include a Stay or Suspension Order which shall:
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> (1) suspend *all actions or proceedings,* in court or otherwise, for the enforcement of claims against the debtor;
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> (2) suspend all actions to enforce *any* judgment, attachment or other provisional remedies against the debtor;

73. *See* Financial Rehabilitation and Insolvency Act (FRIA) of 2010, § 2.

74. *Castillo*, 619 SCRA at 648-50.

> (3) prohibit the debtor from selling, encumbering, transferring or disposing in any manner any of its properties except in the ordinary course of business; and
>
> (4) prohibit the debtor from making *any payment* of its liabilities outstanding as of the commencement date except as may be provided herein.[75]

As can be gleaned from the said provision, the law does not distinguish between a secured and an unsecured creditor. Instead, it provides for the issuance of a Stay Order that suspends "*all* actions or proceedings for the enforcement of claims"[76] and prohibits the debtor "from making *any payment*"[77] of its outstanding liabilities. Again, where the law does *not* distinguish, we ought *not* to distinguish as well.[78] Hence, the issuance of a Stay Order shall cover the claims of both secured and unsecured creditors. Second, Section 60 of the FRIA, which governs the treatment of secured creditors, explicitly provides that —

> Section 60. No Diminution of Secured Creditor Rights. — The issuance of the Commencement Order and the Suspension or Stay Order, and any other provision of this Act, shall not be deemed in any way to diminish or impair the security or lien of a secured creditor, or the value of his lien or security, *except that his right to enforce said security or lien may be suspended during the term of the Stay Order.*
>
> The court, upon motion or recommendation of the rehabilitation receiver, *may allow* a secured creditor to enforce his security or lien, or foreclose upon property of the debtor securing his/its claim, *if the said property is not necessary for the rehabilitation of the debtor.* The secured creditor and/or the other lien holders shall be admitted to the rehabilitation proceedings only for the balance of his claim, if any.[79]

The provision above is clear in that although a preferred creditor retains such preference upon the termination of the rehabilitation proceedings, such preference is suspended during the effectivity of the Stay Order. This claim is further bolstered by the fact that the same Section of the FRIA expressly gives the rehabilitation receiver the discretion to allow or not to allow a secured creditor from enforcing his claim, depending on the circumstances. This means that enforcing a secured creditor's claim *during* the pendency of

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75. Financial Rehabilitation and Insolvency Act (FRIA) of 2010, § 16 (q) (1) (emphasis supplied).

76. *Id.* (emphasis supplied).

77. *Id.* (emphasis supplied).

78. *See Castillo*, 619 SCRA at 649 (citing *Rubberworld (Phils.) Inc.*, 305 SCRA at 729 (2002)).

79. Financial Rehabilitation and Insolvency Act (FRIA) of 2010, § 60 (emphasis supplied).

the rehabilitation proceedings is merely discretionary on the part of the receiver. It cannot be made as a matter of right.

These provisions are more substantive because the issuance of a Stay Order goes into the very purpose for which a Corporate Rehabilitation is being undertaken — the Stay Order, generally, suspends claims in order to allow the rehabilitation receiver or management committee to make the company viable once more.[80]

IV. CONCLUSION

The application of the principle of Equality in Equity in our jurisdiction has evolved through the years, beginning from when the Court rendered flip-flopping decisions on its applicability, up to the time the Court has established settled rules on the matter, taking into consideration the intent of the legislators in expanding the options of distressed corporations, associations, and partnerships, to include Corporate Rehabilitation. In line with the goal of continuing the life of a corporation as a going concern, with the view of restoring it to its former position of "successful operation,"[81] placing the secured and unsecured creditors on equal footing during the pendency of rehabilitation proceedings was deemed wise in order to focus the attention of the receiver to the restoration of the distressed corporations and the preservation of its remaining assets. After the said proceedings, the preference in favor of a secured creditor may again be enforced. Even with the passage of the FRIA in 2010 and despite Sections 62 and 133 of the said law which, at one glance, seem to insinuate the abandonment of the application of Equality in Equity, such Principle still applies. On a more critical reading of the provisions of the FRIA, other more substantial provisions of the said law, such as the issuance and the coverage of a Stay Order, will reveal that Equality in Equity still applies. Thus, the so-called "rules of thumb" enunciated by the Supreme Court in *Rizal Commercial Banking Corporation* still hold true up to this day.

80. Quarterly Newsletter of Fortun Narvasa & Salazar, *The Financial Rehabilitation and Insolvency Act of 2010: Prospects and Retrospect*, LEGAL FINESSE, July-Sep. 2010, *available at* http://www.fnslaw.com.ph/PDF%20Files/3Q2010-final.pdf (last accessed Feb. 25, 2012).

81. *See* RULES OF PROCEDURE ON CORPORATE REHABILITATION, rule 2, § 1.