

Title: Pioneer Insurance & Surety Corp. v. The Hon. Court of Appeals, et al.; Jacob S. Lim v. Court of Appeals, et al.

Facts:

In 1965, Jacob S. Lim, owner-operator of Southern Air Lines (SAL), entered into a contract with Japan Domestic Airlines (JDA) for the purchase of two DC-3A type aircraft and spare parts for \$109,000 to be paid in installments. Pioneer Insurance & Surety Corp. (Pioneer) issued a surety bond in JDA's favor covering the balance of the aircraft purchase price.

Border Machinery & Heavy Equipment Co., Inc. (Bormaheco), Francisco and Modesto Cervantes (the Cervanteses), and Constancio Maglana (collectively referred to as "respondents") contributed funds to the purchase, believing these were investments in a new corporation Lim proposed. Two indemnity agreements were executed: one by Maglana and another by Lim for SAL, Bormaheco, and the Cervanteses, indemnifying Pioneer against potential losses from issuing the bond.

Lim provided a chattel mortgage over the aircraft as security for the bond, which was registered with the relevant authorities. Lim eventually defaulted on the payments, causing Pioneer to pay JDA a total of P298,626.12.

Pioneer sought extrajudicial foreclosure on the chattel mortgage, but respondents filed third-party claims asserting co-ownership of the aircrafts. Subsequently, on July 19, 1966, Pioneer sought judicial foreclosure and a writ of preliminary attachment against Lim and respondents. During the proceedings, respondents cross-claimed against Lim for damages and recovery of funds they had advanced for the aircraft purchase.

The trial court dismissed Pioneer's complaint against all defendants except Lim, whom it held liable. The appellate court modified the decision, dismissing the complaint against all defendants and affirming the rest of the trial court's judgment.

Issues:

1. Whether Pioneer Insurance & Surety Corp. had the right to recover the paid amount considering it had already collected reinsurance for its liability.
2. Whether the indemnity agreements continued to be effective after the execution of the chattel mortgage.
3. The nature of the legal relationship among co-investors in a business venture that failed to incorporate and their respective liabilities and obligations.

**Court's Decision:**

The Supreme Court affirmed the appellate court's findings, noting that Pioneer, having been indemnified by the reinsurer, was not the real party in interest and therefore, could not pursue the claim against the respondents. Moreover, the indemnity agreement was deemed invalid after the execution of the chattel mortgage, which became the sole security for the claim. As such, Pioneer's election of foreclosure precluded any further action to recover an unpaid balance. The indemnity agreements were extinguished upon the foreclosure of the chattel mortgage.

As for the co-investors, no de facto partnership was created between the parties that would necessitate sharing in the losses of the proposed corporation. Evidence showed that Lim acted on his own and was not representing the other investors when dealing with the sale of airplanes and spare parts.

**Doctrine:**

When an insurance company indemnifies an insured party and the insured subsequently seeks to recover for the underlying loss, subrogation provides the insurer the right to pursue any claim that the insured may have against a third party. However, the insured cannot recover from the third party to the extent they have been compensated by the insurer (Article 2207 of the New Civil Code).

**Class Notes:**

- In suretyship, if the surety pays the debt, they become subrogated to the rights of the creditor against the debtor.
- An indemnity agreement can be invalidated by subsequent agreements or actions, like the execution of a chattel mortgage which serves as the new sole security for the claim.
- A failed corporation attempt among investors can lead to a de facto partnership, but only when there is an agreement among the participants suggesting such a relationship, and it is necessary to do justice among parties.
- Subrogation means stepping into the shoes of another person, in terms of their legal right to claim a remedy against a third party.

**Historical Background:**

During the time of the case, the Philippines was experiencing growth in its airline industry, which likely prompted the initial business venture proposed by Lim. The outcome of this case reaffirms principles of insurance law, subrogation, and the regularity of commercial transactions involving the use of corporate vehicles for business endeavors. It also

demonstrates the legal implications when individuals fail to properly incorporate their business and the risks associated with informal business agreements.