

JOE'S RADIO & ELECTRICAL SUPPLY, PLAINTIFF AND APPELLEE VS. ALTO ELECTRONICS CORPORATION AND ALTO SURETY & INSURANCE CO., INC., DEFENDANTS AND APPELLANTS.

G. R. No. L-12376. August 22, 1958

Ponente: REYES, J.B.L., J.

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REYES, J.B.L., J.:

Appeal from a judgment of the Court of First Instance of Manila, in its Civil Case No. 21805, ordering the defendants to pay jointly and severally to the plaintiff, the sum of P49,378.77, plus 6 per cent interest per annum from July 2, 1954, plus the further sum of P39,780 as liquidated damages, with legal interest from the filing of the complaint, provided, however, that the liability of the defendant surety company shall not exceed P66,150, in accordance with the surety bond.

The facts of this case are practically undisputed, and may be substantially stated as follows:

On May 23, 1953, the plaintiff and appellee and the Bolinao Electronics Corporation entered into a "dealership agreement", (Exhibit "A"), whereby the latter bound itself to sell and deliver to the former 500 television sets (RCA TV Model 21T—303, 21" KERBY) at the price of P1,134.00 each, in two shipments of 250 sets, the first shipment to be made within 90 days from May 23, 1953, and the next shipment within 60 days after the completion of the first shipment. On its part, the appellee, Joe's Radio & Electrical Supply, agreed to deposit 1/3 of the total price of the first shipment, minus a discount of 30 per cent, upon signing the contract; 1/3 of the total price of the second shipment, minus a discount of 30 per cent, immediately after its receipt of the first shipment; and the balance of the total price of each shipment (minus the discounts) immediately after making the performance test of each set in each shipment. To secure the true and faithful compliance of the agreement by the Bolinao Electronics Corporation, it agreed to put up a surety bond, in an amount sufficient to cover the advance payment to be made by appellee, and also that, should the Bolinao Electronics Corporation fail to comply with the terms of the agreement within the period specified, it would return to appellee upon demand whatever amount or amounts had been deposited by the latter, with interest at the rate of 6% per annum, plus damages equivalent to 20 per cent of the total cost of 250 television sets.

The defendant and appellant Alto Electronics Corporation was subrogated to the rights and obligations of the Bolinao Electronics Corporation in the "dealership agreement" on August 31, 1953; and on the same date, the other defendant-appellant Alto Surety & Insurance Co., Inc., issued in favor of appellee a surety bond in the amount of P66,150 to guarantee the full and faithful performance by the appellant Alto Electronics Corporation under the agreement.

The first shipment of 250 television sets was totally delivered, and totally paid for. Thereafter, appellee deposited with appellant Alto Electronics Corporation the sum of P66,150, the sum required under the "dealership agreement" as advance partial payment for the 250 sets of the second delivery. No delivery having been made on

this second batch, suit was commenced against the defendants and appellants on January 30, 1954.

During the pendency of the case, but before trial was held, the appellee and the Alto Electronics Corporation entered into another agreement, dated July 2, 1954, wherein the latter admitted having received from the former the sum of P66,150, as advance partial payment, as aforementioned, for the remaining 250 television sets slated for delivery by the Alto Electronics Corporation to the appellee under the dealership agreement; and that, as of the date of the additional agreement, said sum, together with interest thereon, amounted to P70,008.75. Under the terms of the second instrument, the said appellant agreed to liquidate thfe indebtedness by delivering to appellee 66 television sets of various models, delivery to commence within five days after the signing of the agreement and to be completed within 90 days thereafter. With this agreement, the Alto Surety & Insurance Co., inc. signed in conformity.

However, of the 66 television sets required to be delivered under the agreement, appellant Alto Electronics Corporation was only able to deliver 13 sets, with a total value of P20,629.98, leaving an unpaid balance of P49,378.77. Besides these 13 television sets, said appellant also delivered to appellee two other sets with a total value of P2,928.24, which were accepted by the latter as "deposit pending receipt of letter of approval from the appellant surety company" presumably (fearing a release of the surety bond should said delivery be accepted without the surety company's consent), because delivery was made after the lapse of the period provided in the second agreement.

In view of such failure of the appellant Alto Electronics Corporation to comply fully with the said additional agreement, appellee reactivated the present suit and on April 2, 1955, filed an amended and supplemental complaint alleging the above facts.

As already indicated, the trial court rendered judgment in favor of the plaintiff and appellee. Against this decision, the defendants-appellants, Alto Electronics Corporation and Alto Surety & Insurance Co., Inc., appealed to the Court of Appeals, which certified the case to this Court, in view of section 17, paragraph 2, of the Judiciary

Act of 1948, since the amount involved is far in excess of P50,000. Appellants, Alto Electronics Corporation and Alto Surety & Insurance Co., Inc., now urge that:—

- The lower court erred in not crediting the appellants with the sum of P2,928.24, representing the cost (current price less 40 per cent and 2 per cent discount) of three (3) TV sets delivered to and accepted by the appellee.
- The lower court erred in holding that the subsequent agreement Exhibit "G" is a supplement to the original dealership agreement and not a novation thereof.
- The lower court erred in holding that the stipulation for liquidated damages and interest contained in the original dealership agreement was tacitly carried over to the subsequent agreement, Exhibit "G."
- The lower court erred in holding that the appellants are jointly and severally liable for the principal sum of P49,378.77, with interest at 6% per annum from July 2, 1954, plus 20 per cent of the total cost of undelivered sets or the sum of P39,780 as liquidated damages, with interest at 6 per cent per annum from the filing of the complaint on January 30, 1954."

On the first assignment of error, it is urged by appellants that the value of two television sets which were accepted by appellee as "deposit pending receipt of letter of approval from the Alto Surety & Insurance Co., Inc.," should be credited to the principal amount owned by appellant Alto Electronics Corporation. They cite in this regard a statement from the Corpus Juris (Vol. 12, p. 320) to the effect that:

"Where a tender is made on condition that it shall be received in settlement of a disputed claim, it is the duty of

the party to whom it is made either to refuse it or accept it on the terms as made. He has no right to accept the tender and prescribe the terms of the acceptance. Where a tender thus made is accepted, it is binding, although the acceptance is under protest or with the 'express declaration that it is received in part satisfaction only.'

Aside from the fact that this rule would seem to have application only in cases where the thing offered is tendered by the debtor with the condition that it shall be in full satisfaction or settlement of a claim (which does not appear to be the case here), it is qualified thus:

"The rule that the retention of payment made on condition that they shall be in full satisfaction of the claim does not apply where the amount accepted does not purport to cover the amount in controversy (Bryant Lumber Co, vs. Coppock-Warner Lumber Co., 79 S.E. 282), when there is nothing to show that the payment was accepted as definite and final settlement (94 A.L.R.), (or), when the amount is transmitted under circumstances showing that it was tendered as a payment of indebtedness which was thereafter to be adjusted by the parties. * * *." (15 C.J.S., section 7, pp. 720-721)

Certainly, the delivery of the two television sets in question could not have been intended by either of the parties to be the full and final settlement of appellee's claim.

Upon the other hand, it would seem that the general principles on payment under the Civil Code^[1] sanctions such kind of acceptance, as where the performance of the obligation is incomplete or irregular. Observe that the delivery of the two television sets was made after the prescribed period fixed in the agreement of the parties. Lest the appellee be misunderstood as having granted an extension of the obligation that might release the surety company from its undertaking under the surety bond^[2], it was not improper nor unreasonable for it to subject its acceptance to the said delivery upon the surety company's consent. It should be noted further that when appellee imposed such condition, no objection was interposed by the appellant Alto Electronics Corporation, thereby at least implying its concurrence to it.

Pending the receipt of a letter of approval from the surety company, appellee could not have disposed of the two television sets in the ordinary course of business, its possession of the objects being merely in the nature of a deposit. Appellant Alto Electronics Corporation could have, at any time, if it wanted to, retake them prior to the said approval. Until such delivery was confirmed by the surety, no unqualified acceptance had been made, and ownership remained with the Alto Electronics Corporation, as the depositor.

As regards the appellant Alto Electronics Corporation, there is another reason why the first assigned error could not be given merit, and that is, its admission under paragraph 5 of its amended answer (Rec. App., p. 36) of paragraph 11 of the amended and supplemental complaint which in effect admitted the allegations contained in the said paragraph of the complaint, viz., "That under the aforesaid agreement, defendant delivered to plaintiff only 13 television sets with a total value of P20,629.98 leaving an unpaid balance of P49,378.77". It is a familiar doctrine that an admission made in the pleadings cannot be controverted by the party making such admission and are conclusive as to him, and that all proofs submitted by him contrary thereto or inconsistent therewith, should be ignored, whether objection is interposed by the party or not (Cunanan vs. Amparo, 80 Phil., 227; Ramirez vs. Orientalist Co., 38 Phil., 634; McDaniel vs. Apacible, 44 Phil., 248; see also section 7, Rule 123, Rules of Court; Francisco, Rules of Court ann., Vol. VI, p. 195; Comments on the Rules of Court, Morari, Vol. 3, '57 Ed., p. 66-67).

With respect to the second assignment of error, it is appellants' theory that the subsequent agreement, Exhibit "G", entered into during the pendency of this action, novated the original dealership agreement of May 23, 1953. They base this proposition on Article 1291 of the Civil Code which provides that obligations may be modified by changing the object or principal conditions.

In order to produce that effect, however, Article 1292 of the same Code prescribes:

"ART. 1292. In order that an obligation may be extinguished by another which substitutes the same, it is imperative that it be so declared in unequivocal terms, or that the old and new obligation be in every point incompatible with each other." (Italics supplied)

This rule definitely precludes the possibility of a novation taking place without the intention of the parties to do so (*animus novendi*), expressed in the manner provided in the aforequoted provision of the law. Hence, in the case of *La Tondena, Inc. vs. Alto Surety & Insurance Co., Inc. et al.*, 101 Phil., 879; 53 Off. Gaz. (18) 6101 this court ruled that in order to extinguish or discharge an obligation by novation, the intent of the parties to do so (*animus novendi*) must either be expressed, or else clearly apparent from the incompatibility in all points of the old and new obligations. Aside, therefore, from the changes or differences that might be brought about in the terms of the old agreement by the new one, "absolute incompatibility" in order to presume intention to novate should be evident in the absence of an express declaration to that effect by the parties. This Court has been uniform in its decisions in this respect. (*Lorenzo Lerma vs. V. Reyes and Adela Enriquez*, 103 Phil., 1027; *Maria Pascual vs. Jose Lacsamana*, 100 Phil., 381; *Reynold Santos vs. Emiliano Acuña, et al.*, 100 Phil., 230; 53 Off. Gaz. 358; *Mendoza vs. De Guia*, 84 Phil., 873; *Inchausti vs. Yulo*, 34 Phil., 624; *Zapanta vs. De Rotaeché*, 21 Phil., 154).

In the present case, the subsequent agreement, Exhibit "G", contains no express declaration extinguishing the previous one (the dealership agreement). Upon the other hand, it is clear that the parties still recognized the existence of the first agreement, as the arrangement was that upon the completion of the 66 television sets within the period agreed upon under the new covenant, the appellee would move for the dismissal of the pending case against the appellants, "otherwise, whatever deliveries might have been made would be applied on account of the claims, subject matter of the complaint." (Rec. App., p. 32). Evidently, in referring to the "claims subject matter of the complaint", the parties had in mind then the already existing liability of the appellants that arose from the breach of the original contract. The parties could not have intended as the "claims subject matter of the complaint" those to be derived from the second agreement, for there could not have been any violation thereof at the time it was entered into.

It thus appears that Exhibit "G" simply gave appellants more time and an added opportunity to liquidate their obligations and thus escape the sanctions provided in the first (dealership) agreement; it was not contemplated that the latter would be completely superseded unless and until there was a full performance of the terms in the new agreement. The appellee had experienced the breach of the first agreement by the appellant, and having no assurance that the second would not be likewise breached, it had no reason to forego the clause providing for liquidated damages, since that was established for its own protection. The terms of the second agreement clearly indicate, on the contrary, that the liquidated damages clause of the original contract was intended to subsist.

Did the new arrangement amount to an independent contract? It did not, for as we have already explained, it included specifically the stipulation that should there be partial performance of the new agreement, the same should be applied on account of the claims subject matter of the complaint, which "claims" embraced the recovery of the liquidated damages provided in the dealership agreement.

Having arrived at the above conclusion, the appellants' third and fourth assignments of error necessarily fail, for both are based on the proposition that the second agreement, Exhibit "G" extinguished by novation the previous dealership agreement, Exhibit "A". However, the amounts recoverable by the appellee must be reduced as follows:

(1) The first recoverable item stated by the trial court to be in the amount of P49,378.77[3] should bear interest at 6%, not from July 2, 1954 when the second agreement was entered into, but only from April 2, 1955, the date

when the amended and supplemental complaint was filed. As a debtor incurs in default only from the time the obligee judicially or extra judicially demands the fulfillment of the obligation (Article 1169, new Civil Code), and as no extra-judicial demand was made, legal interest thereon starts to run only from the date of judicial demand (Mariano Veloso, et al. vs. Aniceta Fontanosa, et al., 13 Phil. 79, citing the decision of the Supreme Court of Spain, dated December 3, 1902). The amount involved in this item, it is to be observed, has particular reference to a violation of the second agreement.

(2) The other item in the amount of P39,780 was ordered by the court below to be paid to appellee by way of liquidated damages, computed at 20 per cent of the total cost of 250 television sets (at the price of P1,134 per set less 30 per cent discount), as provided in the original dealership agreement, plus legal interest from the date of filing of the original complaint on January 30, 1954. Appellants contend that in view of the partial performance on their part of the agreement, they are entitled to an equitable reduction of damages irrespective of whether the stipulation for damages was intended as a penalty or as indemnity. Appellee, on the other hand, argues that while partial or irregular performance may justify a reduction of a penalty under Article 1229 of the new Civil Code, it may not do so in the case of liquidated damages, which according to it could only be reduced if found to be iniquitous or unconscionable as provided in Article 2227 of the same Code.

"Art 1229. The judge shall equitably reduce the penalty when the principal obligation has been partly or irregularly complied with by the debtor. Even if there has been no performance, the penalty may also be reduced by the courts if it is iniquitous or unconscionable."

"Art. 2227. Liquidated damages, whether intended as an indemnity or a penalty shall be equitably reduced if they are iniquitous or unconscionable."

We believe that the distinction that appellee stresses in this appeal, has no justification, While under the new Civil Code, penalties and liquidated damages are dealt with separately, nevertheless, the fundamental rules governing, them still remain basically the same, making them subject to reduction where equity so requires.

"In American law, it is only when the clause is a penalty that the courts will reduce the stipulated damages which are excessive. But article 2247 (now 2227) of the proposed Code states:

"ART. 2247. Liquidated damages, whether intended as an indemnity or a penalty shall be equitably reduced if they are iniquitous or unconscionable."

The reason is that in both cases, the stipulation is contra bonos mores under article 1326. It is a mere technicality to refuse to lessen the damages to their just amount simply because the stipulation is not meant to be a penalty. 'An immoral stipulation is none the less immoral because it is called an indemnity.' (Report of the Code Commission, p. 75)

What could be regarded as an equivalent provision of Article 1229 on penalties is Article 2228 with respect to liquidated damages:

"Art. 2228. When the breach of the contract committed by the defendant is not the one contemplated by the parties in agreeing upon the liquidated damages, the law shall determine the measure of damages, and not the stipulation." [4]

Where there is partial or irregular performance in a contract providing for liquidated damages, it can be said, in view of the foregoing cited provision of the Code, that the court may mitigate the sum stipulated therein since it is to be presumed that the parties only contemplated a total breach of the contract. And this is usually so because of the difficulty or sometimes inability of the parties to ascertain or gauge beforehand, the amount of indemnity in case of a partial breach, just as it is equally perplexing to foresee the extent of a partial or irregular performance.

And so it has been held in one case that a stipulation for liquidated damages in case of a total breach of the contract cannot be enforced if the party has accepted a partial performance thereof (*Tanenbaum Son & Co. vs. Drumbor Bingell Co.*, CCA. Pa. 47 F [2d] 1009, certiorari denied, 52 S. Ct. 7; 284 U.S. 619, 76 L. Ed. 588, cited 25 C.J.S. 695).

In this connection, we believe that the 20 per cent liquidated damages clause in the dealership agreement must have had reference to a failure to comply with the terms of the entire agreement, that is to say, the delivery of 500 television sets (in two shipments of 250 sets each) within the time provided therein. To permit appellee to collect the same amount of liquidated damages after more than half of the sets were delivered and received, would amount to doubling the stipulated damages in case none of the sets had been delivered, and nothing in the contract warrants such a possibility.

The correct principle has been declared in the case of *Sledge et ux., vs. Arcadia Orchards Co.* (77 Wash. 477, 317 Pac. 1051, citing *Shute vs. Taylor*, 5 Mete. [Mass.] 61, 67):

"* * * The question what is liquidated damages, and what is a penalty, is often a difficult one. It is not always the calling of a sum, to be paid for breach of contract, liquidated damages which makes it so. In general, it is the tendency and preference of the law to regard a sum, stated to be payable if a contract is not fulfilled, as a penalty, and not as liquidated damages, because then it may be apportioned to the loss actually sustained. But, without going at large into the subject, one consideration, we think, is decisive against recovering the sum in question as liquidated damages, namely: That here there has been a part performance, and an acceptance of stick part performance. If the parties intended the sum named to be liquidated damages for the breach of the contract therein expressed, it was for an entire breach. Whether divisible in its nature or not, it was in fact divided by an offer and acceptance of part performance. It is like the case of an obligation to perform two or more independent acts, with a provision for single liquidated damages for non-performance; if one is performed, and not the other, it is not a case for the recovery of the liquidated damages." (Italics supplied)

Consequently, it is immaterial whether the questioned clause in the dealership agreement is a provision for liquidated damages, or deemed a penalty clause under the above circumstances; it has to be mitigated in either case, in the former case, because of its being unconscionable if enforced in toto; and in the latter, because of the acceptance of a partial performance.

Accordingly, taking the stipulated sum as the basis for the measure of damages, and deducting therefrom the benefits received in view of the partial compliance, appellants should be made to pay as damages only the amount of P15,719.00, computed as follows:

P198,450

.—basic cost of 250 TV sets, minus a discount of 30% from the the stipulated price of P1,134 each.

P99,225

.—one-half (1/2) of the P198,450, as there has been 50 per cent partial compliance under the dealership agreement.

P20,629.98

.—extent of partial performance under the second agreement (13 additional TV sets).

P78,595.02

per cent.—agreed percentage for liquidated damages.

x 20

P15,719. —recoverable sum.

plus legal interest from the filing of the supplemental complaint on April 2, 1955.

Wherefore, the decision appealed is affirmed, with the modification that the 6% interest on the first item of P49,378.77 (representing balance of appellee's advances) be made to start only from April 2, 1955, the date of the filing of the amended and supplemental complaint; and with respect to the P39,780 liquidated damages awarded by the trial court, the same shall be reduced to only P15,719, plus legal interest thereon from the same date, April 2, 1955. Without costs in this instance. So ordered.

Paras, C. J., Bengzon, Padilla, Montemayor, Reyes, A., Bautista Angelo, Concepcion, Endencia, and Felix, JJ., concur.

[1]Art. 1235. When the obligee accepts the performance, knowing its incompleteness or irregularity, and without expressing any protest or objection, the obligation is deemed fully complied with. (new Civil Code)

[2]Art. 2079. An extension granted to the debtor by the creditor without the consent of the guarantor extinguishes the guaranty. The mere failure on the part of the creditor to demand payment after the debt has become due does not of itself constitute any extension of time referred to herein, (new Civil Code)

[3]Arrived at by deducting the total value of the 13 television sets delivered to appellee (P20,629.98) from the P70,008.75, the partial payment advanced to appellant Alto Electronics Corporation.

[4]Note also, that Article 2215 of the new Civil Code authorizes the courts to equitably mitigate the damages, where the plaintiff has derived some benefits as a result of the contract.

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