

SOUTH CITY HOMES, INC., FORTUNE MOTORS (PHILS.), PALAWAN LUMBER MANUFACTURING CORPORATION, PETITIONERS, VS. BA FINANCE CORPORATION, RESPONDENT.

G.R. No. 135462. December 07, 2001

Ponente: PARDO, J.

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PARDO, J.:

The Case

The case is a petition to set aside the decision[1] of the Court of Appeals, the dispositive portion of which reads:

"WHEREFORE, premises considered, the appealed Decision (as amended by that Order of July 22, 1992) of the lower court in Civil Case No. 21944 is hereby AFFIRMED with the MODIFICATION that defendant-appellee South City Homes, Inc. is hereby ordered to pay, jointly and severally, with Fortune Motors Corporation, Palawan Lumber Manufacturing Corporation and Joseph L. G. Chua, the outstanding amounts due under the six (6) drafts and trust receipts, with interest thereon at the legal rate from the date of filing of this case until said amounts shall have been fully paid, as follows:

Date of Draft

Amount

Balance Due

July 26, 1983

P 244,269.00

P 198,659.52

July 27, 1983

967,765.50

324,767.41

July 28, 1983

1,138,941.00

1,138,941.00

August 2, 1983

244,269.00

244,269.00

August 5, 1983

275,079.00

275,079.60

August 8, 1983

475,046.10

475,046.10

and the attorney's fees and costs of suit.

"SO ORDERED." [2]

The Facts

The facts, as found by the Court of Appeals, are as follows:

"The present controversy relates to the rights of an assignee (financing company) of drafts and trust receipts backed up by sureties, in the event of default by the debtor (car dealer) to whom the assignor creditor (car manufacturer) sold and delivered motor vehicles for resale. A consistent ruling on these cases is hereby reiterated: that a surety may secure obligations incurred subsequent to the execution of the surety contract.

"Prior to the transactions covered by the subject drafts and trust receipts, defendant-appellant Fortune Motors Corporation (Phils.) has been availing of the credit facilities of plaintiff-appellant BA Finance Corporation. On January 17, 1983, Joseph L. G. Chua, President of Fortune Motors Corporation, executed in favor of plaintiff-appellant a Continuing Suretyship Agreement, in which he "jointly and severally unconditionally" guaranteed the "full, faithful and prompt payment and discharge of any and all indebtedness" of Fortune Motors Corporation to BA Finance Corporation (Folder of Exhibits, pp. 21-22).

"On February 3, 1983, Palawan Lumber Manufacturing Corporation represented by Joseph L.G. Chua, George D. Tan, Edgar C. Rodriguez and Joselito C. Baltazar, executed in favor of plaintiff-appellant a Continuing Suretyship Agreement in which, said corporation "jointly and severally unconditionally" guaranteed the "full, faithful and prompt payment and discharge of any and all indebtedness of Fortune Motors Corporation to BA Finance Corporation (Folder of Exhibits, pp. 19-20). On the same date, South City Homes, Inc. represented by Edgar C. Rodriguez and Aurelio F. Tablante, likewise executed a Continuing Suretyship Agreement in which said corporation "jointly and severally unconditionally" guaranteed the "full, faithful and prompt payment and discharge of any and all indebtedness" of Fortune Motors Corporation to BA Finance Corporation (Folder of Exhibits, pp. 17-18).

"Subsequently, Canlubang Automotive Resources Corporation (CARCO) drew six (6) Drafts in its own favor, payable thirty (30) days after sight, charged to the account of Fortune Motors Corporation, as follows:

Date of Draft

Amount

July 26, 1983

P 244,269.00

July 27, 1983

967,765.50

July 28, 1983

1,138,941.00

August 2, 1983

244,269.00

August 5, 1983

275,079.00

August 8, 1983

475,046.10

"(Folder of Exhibits, pp. 1, 4, 7, 8, 11 and 14).

"Fortune Motors Corporation thereafter executed trust receipts covering the motor vehicles delivered to it by

CARCO under which it agreed to remit to the Entruster (CARCO) the proceeds of any sale and immediately surrender the remaining unsold vehicles (Folder of Exhibits, pp. 2, 5, 7-A, 9, 12 and 15). The drafts and trust receipts were assigned to plaintiff-appellant, under Deeds of Assignment executed by CARCO (Folder of Exhibits, pp. 3, 6, 7-B, 10, 13 and 16).

"Upon failure of the defendant-appellant Fortune Motors Corporation to pay the amounts due under the drafts and to remit the proceeds of motor vehicles sold or to return those remaining unsold in accordance with the terms of the trust receipt agreements, BA Finance Corporation sent demand letter to Edgar C. Rodriguez, South City Homes, Inc., Aurelio Tablante, Palawan Lumber Manufacturing Corporation, Joseph L. G. Chua, George D. Tan and Joselito C. Baltazar (Folder of Exhibits, pp. 29-37). Since the defendants-appellants failed to settle their outstanding account with plaintiff-appellant, the latter filed on December 22, 1983 a complaint for a sum of money with prayer for preliminary attachment, with the Regional Trial Court of Manila, Branch 1, which was docketed as Civil Case No. 83-21944 (Record, pp. 1-12). Plaintiff-appellant filed a surety bond in the amount of P3,391,546.56 and accordingly, Judge Rosalio C. Segundo ordered the issuance of a writ of preliminary attachment on January 3, 1984 (Record, pp. 37-47). Defendants Fortune Motors Corporation, South City Homes, Inc., Edgar C. Rodriguez, Aurelio F. Tablante, Palawan Lumber Manufacturing Corporation, Joseph L. G. Chua, George D. Tan and Joselito C. Baltazar filed a Motion to Discharge Attachment, which was opposed by plaintiff-appellant (Record, pp. 49-56). In an Order dated January 11, 1984, Judge Segundo dissolved the writ of attachment except as against defendant Fortune Motors Corporation and set the said incident for hearing (Record, p. 57). On January 19, 1984, the defendants filed a Motion to Dismiss. Therein, they alleged that conventional subrogation effected a novation without the consent of the debtor (Fortune Motors Corporation) and thereby extinguished the latter's liability; that pursuant to the trust receipt transaction, it was premature under P. D. No. 115 to immediately file a complaint for a sum of money as the remedy of the entruster is an action for specific performance; that the suretyship agreements are null and void for having been entered into without an existing principal obligation; and that being such sureties does not make them solidary debtors (Record, pp. 58-64).

"After due hearing, the court denied the motion to discharge attachment with respect to defendant Fortune Motors Corporation as well as the motion to dismiss by the defendants (Record, pp. 68 and 87). In their Answer, defendants stressed that their obligations to the creditor (CARCO) was extinguished by the assignment of the drafts and trust receipts to plaintiff-appellant without their knowledge and consent, and pursuant to legal provision on conventional subrogation a novation was effected, thereby extinguishing the liability of the sureties; that plaintiff-appellant failed to immediately demand the return of the goods under the trust receipt agreements or exercise the courses of action by the entruster as provided for under P. D. No. 115; and that at the time the suretyship agreements were entered into, there were no principal obligations, thus rendering them null and void. A counterclaim for the award of actual, moral and exemplary damages was prayed for by defendants (Record, pp. 91-110).

"During the pre-trial, efforts to reach a compromise was not successful, and in view of the retirement of Judge Rosalio C. Segundo of RTC Manila, Branch 1, the case was-re-raffled off to Branch XXXIII, presided over by Judge Felix V. Barbers (Record, pp. 155-160).

"Fortune Motors Corporation filed a motion to lift the writ of attachment covering three (3) vehicles described in the Third-Party Claim filed with the Office of Deputy Sheriff Jorge C. Victorino (RTC, Branch 1) by Fortune Equipment, Inc. which was opposed by plaintiff-appellant (Record, pp. 173-181). On June 15, 1984, Deputy Sheriff Jorge C. Victorino issued a "Notice of Levy Upon Personal Properties Pursuant to Order of Attachment" which was duly served on defendant Fortune Motors Corporation (Record, pp. 191-199). In an Order dated April 28, 1986, the court a quo denied the motion to lift the writ of attachment on three (3) vehicles described in the

Third-Party Claim filed by Fortune Equipment Inc. (Record, p. 207). On motion of their respective counsel, the trial court granted the parties time to sit down and appraise the machineries and spare parts owned by defendant Fortune Motors Corporation which are now in the possession of plaintiff corporation by virtue of the attachment. A series of conferences was allowed by the court, as means toward possible compromise agreement. In an Order dated June 2, 1987, the case was returned to Branch I, now presided over by Judge Rebecca G. Salvador (Record, p. 237). The pre-trial period was terminated and the case was set for trial on the merits (Record, p. 259).

"Acting on the motion to sell levied properties filed by defendant George D. Tan, the trial court ordered the public sale of the attached properties (Record, p. 406). The court likewise allowed the complaint-in-intervention filed by Fortune Equipment Inc. and South Fortune Motors Corporation who claimed ownership of four (4) vehicles earlier seized and attached (Record, p. 471-475). Plaintiff corporation admitted the allegations contained in the complaint-in-intervention only with respect to one truck so attached but denied the rest of intervenors' allegations (Record, pp. 479-482). Thereafter, the parties submitted their respective pre-trial briefs on the complaint-in-intervention, and after the submission of evidence thereon, the case was submitted for decision (Record, pp. 573-577).

"On November 25, 1991, the lower court rendered its judgment, the dispositive portion of which reads as follows:

"WHEREFORE, judgment is hereby rendered:

"1. Ordering defendants Fortune Motors, Palawan Lumber Manufacturing Corporation and Joseph Chua, jointly and severally to pay the plaintiff on the July 27, 1983 Draft, the sum of P324,767.41 with the interest thereon at the legal rate from the date of filing of this case, December 21, 1983 until the amount shall have been fully paid;

"2. Ordering defendants Fortune Motors, Palawan Manufacturing Corporation and Joseph Chua jointly and severally to pay to the plaintiff on the July 26, 1983 Draft, the sum of P198,659.52 with interest thereon at the legal rate from the date of filing of this case, until the amount shall have been fully paid;

"3. Ordering defendant Fortune Motors, Palawan Manufacturing Corporation and Joseph Chua jointly and severally to pay to the plaintiff on the July 28, 1983 Draft the sum of P1,138,941.00 with interest thereon at the legal rate from the date of filing of this case, until the amount shall have been fully paid;

"4. Ordering defendants Fortune Motors, Palawan Lumber Manufacturing Corporation and Joseph Chua jointly and severally to pay to the plaintiff on the August 2, 1983 Draft, the sum of P244,269.00 with interest thereon at the legal rate from the date of filing of this case, until the amount shall have been fully paid;

"5. Ordering defendants Fortune Motors, Palawan Lumber Manufacturing Corporation and Joseph Chua jointly and severally to pay to the plaintiff on the August 5, 1983 Draft the sum of P275,079.60 with interest thereon at the legal rate from the date of the filing of this case, until the amount shall have been fully paid;

"6. Ordering defendants Fortune Motors, Palawan Lumber Manufacturing Corporation and Joseph Chua jointly and severally to pay to the plaintiff on the August 8, 1983 Draft the sum of P475,046.10 with interest thereon at legal rate from the date of the filing of this case, until the amount shall been fully paid;

"7. Ordering defendant Fortune Motors, Palawan Lumber Manufacturing Corporation and Joseph Chua jointly and severally to pay the sum of P300,000.00 as attorney's fees and the costs of this suit;

"8. Dismissing plaintiff's complaint against South City Homes, Aurelio Tablante, Joselito Baltazar, George Tan and Edgar Rodriguez and the latter's counterclaim for lack of basis;

"9. Ordering Deputy Sheriff Jorge Victorino to return to Intervenor Fortune Equipment the Mitsubishi Truck Canter with Motor No. 310913 and Chassis No. 513234;

"10. Dismissing the complaint-in-intervention in so far as the three other vehicles mentioned in the complaint-in-intervention are concerned for lack of cause of action;

"11. Dismissing the complaint-in-intervention against Fortune Motor for lack of basis; and

"12. Ordering the parties-in-intervention to bear their respective damages, attorneys fees and the costs of the suit.

"Upon execution, the sheriff may cause the judgment to be satisfied out of the properties attached with the exception of one (1) unit Mitsubishi Truck Canter with Motor No. 310913 and Chassis No. 513234, if they be sufficient for that purpose. The officer shall make a return in writing to the court of his proceedings. Whenever the judgment shall have been paid, the officer, upon reasonable demand must return to the judgment debtor the attached properties remaining in his hand, and any of the proceeds of the properties not applied to the judgment.

"SO ORDERED.

"On two (2) separate motions for reconsideration, one filed by plaintiffs-intervenors dated December 18, 1991 and the other by plaintiff dated December 26, 1991, the trial court issued an Order dated July 22, 1992 amending its Decision dated November 25, 1991. Specifically, said Order amended paragraphs 9 and 10 thereof and deleted the last paragraph of the said Decision.

"Paragraphs 9 and 10 now read:

"9. Ordering Deputy Sheriff Jorge C. Victorino to return to Intervenor Fortune Equipment, Inc. the Mitsubishi Truck Canter with Motor No. 310913 and Chassis No. 513234; Mitsubishi Truck Canter with Motor No. 4D30-313012 and Chassis No. 513696, and Fuso Truck with Motor No. 006769 and Chassis No. 20756, and to Intervenor South Fortune Motors Corporation the Cimaron Jeepney with Plate No. NET-849;

"10. Ordering the plaintiff, in the event the motor vehicles could no longer be returned to pay the estimated value thereof, i.e., P750,000.00 for the three trucks, and P5,000.00 for the Cimaron Jeepney, to the plaintiffs-intervenors.

"x x x" (Records, pp. 664-665)

"Plaintiffs BA Finance Corporation, defendants Fortune Motors Corp. (Phils.) and Palawan Lumber Manufacturing Corporation, and intervenors Fortune Equipment and South Fortune Motors, interposed the present appeal and filed their respective Briefs."[3]

On September 8, 1998, the Court of Appeals promulgated a decision, the dispositive portion of which is quoted in the opening paragraph of this decision.

Hence, this appeal.[4]

The Issues

The issues presented are: (1) whether the suretyship agreement is valid; (2) whether there was a novation of the obligation so as to extinguish the liability of the sureties; and (3) whether respondent BAFC has a valid cause of action for a sum of money following the drafts and trust receipts transactions.[5]

The Court's Ruling

On the first issue, petitioners assert that the suretyship agreement they signed is void because there was no principal obligation at the time of signing as the principal obligation was signed six (6) months later. The Civil Code, however, allows a suretyship agreement to secure future loans even if the amount is not yet known.

Article 2053 of the Civil Code provides that:

"Art. 2053 - A guaranty may also be given as security for future debts, the amount of which is not yet known. x x x"

In *Fortune Motors (Phils.) Corporation v. Court of Appeals*,^[6] we held:

"To fund their acquisition of new vehicles (which are later retailed or resold to the general public), car dealers normally enter into wholesale automotive financing schemes whereby vehicles are delivered by the manufacturer or assembler on the strength of trust receipts or drafts executed by the car dealers, which are backed up by sureties. These trust receipts or drafts are then assigned and/or discounted by the manufacturer to/with financing companies, which assume payment of the vehicles but with the corresponding right to collect such payment from the car dealers and/or the sureties. In this manner, car dealers are able to secure delivery of their stock-in-trade without having to pay cash therefor; manufacturers get paid without any receivables/collection problems; and financing companies earn their margins with the assurance of payment not only from the dealers but also from the sureties. When the vehicles are eventually resold, the car dealers are supposed to pay the financing companies -- and the business goes merrily on. However, in the event the car dealer defaults in paying the financing company, may the surety escape liability on the legal ground that the obligations were incurred subsequent to the execution of the surety contract?

"x x x Of course, a surety is not bound under any particular principal obligation until that principal obligation is born. But there is no theoretical or doctrinal difficulty inherent in saying that the suretyship agreement itself is valid and binding even before the principal obligation intended to be secured thereby is born, any more than there would be in saying that obligations which are subject to a condition precedent are valid and binding before the occurrence of the condition precedent.

"Comprehensive or continuing surety agreements are in fact quite commonplace in present day financial and commercial practice. A bank or financing company which anticipates entering into a series of credit transactions with a particular company, commonly requires the projected principal debtor to execute a continuing surety agreement along with its sureties. By executing such an agreement, the principal places itself in a position to enter into the projected series of transactions with its creditor; with such suretyship agreement, there would be no need to execute a separate surety contract or bond for each financing or credit accommodation extended to the principal debtor."

Petitioners next posit (second issue) that a novation, as a result of the assignment of the drafts and trust receipts by the creditor (CARCO) in favor of respondent BAFC without the consent of the principal debtor (Fortune Motors), extinguished their liabilities.

An assignment of credit is an agreement by virtue of which the owner of a credit, known as the assignor, by a legal cause, such as sale, dacion en pago, exchange or donation, and without the consent of the debtor, transfers his credit and accessory rights to another, known as the assignee, who acquires the power to enforce it to the same extent as the assignor could enforce it against the debtor.^[7] As a consequence, the third party steps into the shoes of the original creditor as subrogee of the latter. Petitioners' obligations were not extinguished. Thus:

"x x x Moreover, in assignment, the debtor's consent is not essential for the validity of the assignment (Art. 1624 in relation to Art. 1475, Civil Code), his knowledge thereof affecting only the validity of the payment he might make (Article 1626, Civil Code).

"Article 1626 also shows that payment of an obligation which is already existing does not depend on the consent of the debtor. It, in effect, mandates that such payment of the existing obligation shall already be made to the new creditor from the time the debtor acquires knowledge of the assignment of the obligation.

"The law is clear that the debtor had the obligation to pay and should have paid from the date of notice whether

or not he consented.

"We have ruled in *Sison & Sison vs. Yap Tico and Avanceña*, 37 Phil. 587 [1918] that definitely, consent is not necessary in order that assignment may fully produce legal effects. Hence, the duty to pay does not depend on the consent of the debtor. Otherwise, all creditors would be prevented from assigning their credits because of the possibility of the debtor's refusal to give consent.

"What the law requires in an assignment of credit is not the consent of the debtor but merely notice to him. A creditor may, therefore, validly assign his credit and its accessories without the debtor's consent (*National Investment and Development Co. v. De Los Angeles*, 40 SCRA 489 [1971]). The purpose of the notice is only to inform that debtor from the date of the assignment, payment should be made to the assignee and not to the original creditor." [8]

Petitioners finally posit (third issue) that as an entruster, respondent BAFC must first demand the return of the unsold vehicles from Fortune Motors Corporation, pursuant to the terms of the trust receipts. Having failed to do so, petitioners had no cause of action whatsoever against Fortune Motors Corporation and the action for collection of sum of money was, therefore, premature. A trust receipt is a security transaction intended to aid in financing importers and retail dealers who do not have sufficient funds or resources to finance the importation or purchase of merchandise, and who may not be able to acquire credit except through utilization, as collateral, of the merchandise imported or purchased. [9] In the event of default by the trustee on his obligations under the trust receipt agreement, it is not absolutely necessary that the entruster cancel the trust and take possession of the goods to be able to enforce his rights thereunder. We ruled:

"x x x Significantly, the law uses the word "may" in granting to the entruster the right to cancel the trust and take possession of the goods. Consequently, petitioner has the discretion to avail of such right or seek any alternative action, such as a third party claim or a separate civil action which it deems best to protect its right, at any time upon default or failure of the trustee to comply with any of the terms and conditions of the trust agreement." [10]

The Judgment

WHEREFORE, the appealed decision is hereby **AFFIRMED**. However, the award of attorney's fees is deleted.

No costs.

SO ORDERED.

Davide, Jr., C.J., (Chairman), Puno, Kapunan, and Ynares-Santiago, JJ., concur.

[1] Petition, Annex "A", Rollo, pp. 19-36.

[2] *Ibid.*, at pp. 35-36.

[3] Docketed as CA-G. R. CV No. 39710, Rollo, pp. 19-36, at pp. 19-26.

[4] Petition, Rollo, pp. 8-17. On June 23, 1999, we gave due course to the petition (Rollo, pp. 106-107).

[5] Memorandum for the Petitioner, Rollo, pp. 111-127, at p. 118.

[6] 335 Phil. 315, 317-318, 326 [1997].

[7] Tolentino, *Civil Code of the Philippines*, Vol. V, p. 188.

[8] *Rodriguez vs. Court of Appeals*, 207 SCRA 553, 558-559 [1992].

[9] *Nacu v. Court of Appeals*, 231 SCRA 237, 247 [1994].

[10] *Prudential Bank v. NLRC*, 321 Phil. 798, 808 [1995].

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