

SPOUSES BENJAMIN AND AGRIFINA SIM, PETITIONERS, VS. M.B. FINANCE CORPORATION, RESPONDENT.

G.R. NO. 164300. November 29, 2006

Ponente: CARPIO MORALES, J.

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CARPIO MORALES, J.:

On August 1, 1997, spouses Benjamin and Agrifina Sim (petitioners) purchased on installment basis a motor vehicle from Angus Motors Corporation (Angus), more particularly described as follows:

Make : Nissan Terrano Gasoline
Motor No. : Z24-972004Y
Serial No. : WNLVD21-G01634
Year Model : 1997

Petitioners thus executed a promissory note[1] in favor of Angus in the amount of P1,105,344 to be paid in 36 consecutive monthly installments of P30,704, due and demandable on the first day of each month starting on September 1, 1997 until fully paid. The penalty for late payment was fixed at 5% a month based on installment in arrears.

To secure the payment of their obligation, petitioners executed a chattel mortgage[2] over the vehicle. And they insured the vehicle with the Commonwealth Insurance Company (CIC) which issued Commercial Vehicle Policy No. 35823 for P895,000.[3]

On August 14, 1997, Angus assigned its rights, title and interest over the promissory note and chattel mortgage to MB Finance Corporation (respondent).[4]

Starting January 1998, petitioners defaulted in paying the monthly installments. On March 23, 1998, the vehicle was carnapped and was not recovered,[5] prompting petitioners to file an insurance claim with the CIC which advised them, however, that it was respondent which was the beneficiary thereof.

Respondent opted to file a complaint against petitioners for sum of money with damages[6] before the Regional Trial Court (RTC) of Makati.

By Decision of September 6, 2000,[7] Branch 141 of the RTC Makati, discrediting petitioners' claim that payment of the proceeds of the insurance policy for the loss of the vehicle extinguished their obligation, held:

In the first place, there was no sufficient evidence to indicate that the car was insured. In the second place, there was no indication that the insurance had actually paid [respondent]. More importantly, the car which was mortgaged was a mere collateral or security to the loan and the loss of the collateral is not one of the modes of extinguishing the loan obligation.[8] (Underscoring supplied)

The trial court thus disposed:

WHEREFORE, judgment is hereby rendered ordering the [petitioners] jointly and severally to pay the

[respondent] the sum of P983,593.72 as of 15 July 1998 plus penalty charge of 5% per month until fully paid, attorney's fees equivalent to 25% of the principal amount due and to pay the costs of this suit.[9]

On petitioners' motion for reconsideration, the trial court, by Order of January 18, 2001,[10] reduced the penalty charge of 5% per month as being unconscionable, citing *Medel v. Court of Appeals*.[11]

The trial court thus pegged the penalty charge at 3% per month.

Petitioners appealed to the Court of Appeals, arguing that the insurance contract novated their obligation which should be computed on the basis of the principal amount of P716,000, and not P983,593.72 as held by the trial court, the latter sum having included interest and penalties whose rates are contrary to public policy; and that respondent is not entitled to attorney's fees, there being no existing obligation and, in any event, 25% of the amount due as such fees was exorbitant.

By Decision of February 5, 2004,[12] the appellate court held that there was no novation. It reduced the penalty charge, however, to 1% interest per month or 12% percent per annum, citing Article 1229[13] of the Civil Code. And it reduced too the award of attorney's fees to 10% of the principal amount due.

Thus, the appellate court disposed:

WHEREFORE, the Decision dated September 6, 2000 in Civil Case No. 98-2752 is AFFIRMED but modified in that the penalty interest per month on the unpaid installments is reduced to one percent (1%) per month or twelve percent (12%) per annum and the attorney's fees reduced to ten percent (10%) of the amount due. This ruling is without prejudice to pursuing whatever legal action Spouses Benjamin Sim and Agrifina Sim may have against Commonwealth Insurance Company pursuant to Commercial Vehicle Policy No. 35823, if so warranted.[14]

Petitioners' Motion for Reconsideration having been denied, the present Petition for Review[15] was filed, faulting the appellate court for

1. . . . fail[ure] to release petitioners from liability to the respondent.
2. . . . still holding petitioners liable for attorney's fees.[16]

The appeal fails.

Fabrigas v. San Francisco del Monte, Inc. explains the nature of novation, viz:

Novation, in its broad concept, may either be extinctive or modificatory. It is extinctive when an old obligation is terminated by the creation of a new obligation that takes the place of the former; it is merely modificatory when the old obligation subsists to the extent it remains compatible with the amendatory agreement. An extinctive novation results either by changing the object or principal conditions (objective or real), or by substituting the person of the debtor or subrogating a third person in the rights of the creditor (subjective or personal). Under this mode, novation would have dual functions – one to extinguish an existing obligation, the other to substitute a new one in its place – requiring a conflux of four essential requisites: (1) a previous valid obligation; (2) an agreement of all parties concerned to a new contract; (3) the extinguishment of the old obligation; and (4) the birth of a valid new obligation.

x x x x

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 the new obligations be on every point incompatible with each other. The test of incompatibility is whether or not the two obligations can stand together, each one having its independent existence. x x x [17]

Since novation is effected only when a new contract has extinguished an earlier contract between the same parties, it necessarily follows that there could be no novation if the parties in the new contract are not the same parties in the old contract as is the case here.[18]

As the appellate court observed:

In this case, there is no new or old contract to speak of since all agreements (consisting of the promissory note, chattel mortgage and insurance policy) were apparently executed simultaneously, or on or about the same time.

The records also reveal that the same parties did not enter into the promissory note and the insurance contract. Sps. Sim executed the promissory note in favor [of] ANGUS, which later assigned its rights, title and interest to [respondent]. There was no mention of CIC therein. On the other hand, the insurance agreement was between Benjamin L. Sim, [respondent] and CIC as the insured, beneficiary and the insurer, respectively. There was no reference to said promissory note. Clearly, the insurance policy was not intended to substitute the promissory note.

In the absence of an agreement, the mere fact that [respondent] is entitled to the proceeds of the insurance policy issued by CIC does not release spouses Sim from their responsibility. Such a situation does not constitute novation, and [respondent], as the creditor can still enforce the obligation of spouses Sim, as debtors.[19]

Under the circumstances attendant to the case, respondent had the option of filing a collection suit or foreclosing the chattel mortgage. In view, however, of the loss of the vehicle subject of the chattel mortgage, it had another option — that of going against the proceeds of the insurance policy.

Respondent opted to file a collection suit. The fear of petitioners that respondents would collect twice on the same obligation is unfounded. Respondent itself acknowledged that by filing a collection suit, it waived its right to go after the proceeds of the insurance policy[20] as in fact petitioner did not present proof that respondent did collect such proceeds.

On the questioned award of attorney's fees, a stipulation on attorney's fees was included in the Promissory Note executed by petitioners:

In case of breach by me/us of any of the terms and conditions of this Note and it is placed in the hands of an attorney for collection, I/We agree to pay an additional sum equivalent to ten (10%) percent of the amount due [a]s and for attorney's fees, in case no legal action is filed; otherwise the additional sum shall be equivalent to twenty five (25%) percent as and for attorney's fees, and the further sum of twenty (20%) percent as liquidated damages, in addition to costs and other expenses of litigation.[21]

Since obligations which arise from contracts have the force of law between the contracting parties,[22] the award of attorney's fees, which the appellate court reduced from 25% to 10% in light of Article 2208 of the Civil Code which mandates that "the attorney's fees and expenses of litigation must be reasonable," is in order.

WHEREFORE, the petition is DENIED.

Costs against petitioners.

SO ORDERED.

Quisumbing, (Chairperson), Carpio, Tinga, and Velasco, Jr., JJ., concur.

[1] Exhibit "A", records, p. 5.

[2] Exh. "B", id. at 6.

[3] Exh. "2", id. at 65.

[4] Exh. "C", id. at 7-8.

[5] Exh. "5", id. at 68.

[6] Records, p. 1-4.

[7] Id. at. 83-86.

[8] Id. at 85.

[9] Id. at 86.

[10] Id. at 105-106.

[11] 359 Phil. 820 (1998).

[12] Penned by Associate Justice Mariano C. del Castillo, with the concurrence of Justices Rodrigo V. Cosico and Rosalinda Asuncion-Vicente, CA rollo, pp. 43-51.

[13] 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.

[14] CA rollo, p. 50.

[15] Rollo, pp. 7-18.

[16] Id. at 11.

[17] G.R. No. 152346, November 25, 2005, 476 SCRA 247, 258-259.

[18] Velasquez v. Court of Appeals, 368 Phil. 863, 871-872 (1999).

[19] CA rollo, pp. 46-47.

[20] Comment, rollo, p. 105.

[21] Records, p. 5.

[22] CIVIL CODE, Art. 1159.

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