

MAKATI DEVELOPMENT CORPORATION, PLAINTIFF AND APPELLANT, VS. EMPIRE INSURANCE CO., DEFENDANT AND APPELLEE, RODOLFO P. ANDAL, THIRD PARTY DEFENDANT AND APPELLEE.

G.R. No. 21780. June 30, 1967

Ponente: CASTRO, J.

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CASTRO, J.:

On March 31, 1959, the Makati Development Corporation sold to Rodolfo P. Andal a lot, with an area of 1,589 square meters, in the Urdaneta Village, Makati, Rizal, for P55,615.

A so-called "special condition" contained in the deed of sale provides that "[T]he VENDEE/S shall commence the construction and complete at least 50% of his/her/their/ its residence on the property within two (2) years from March 31, 1959 to the satisfaction of the VENDOR and, in the event of his/her/their/its failure to do so, the bond which the VENDEE/S has delivered to the VENDOR in the sum of P11,123.00 and evidenced by a cash bond receipt dated April 10, 1959 will be forfeited in favor of the VENDOR by the mere fact of failure of the VENDEE/S to comply with this special condition." To insure faithful compliance with this "condition," Andal gave a surety bond on April 10, 1959 wherein he, as principal, and the Empire Insurance Company as surety, jointly and severally, undertook to pay the Makati Development Corporation the sum of P12,000 in case Andal failed to comply with his obligation under the deed of sale.

Andal did not build his house; instead he sold the lot to Juan Carlos on January 18, 1960. As neither Andal nor Juan Carlos built a house on the lot within the stipulated period, the Makati Development Corporation, on April 3, 1961, that is, three days after the lapse of the two-year period, sent a notice of claim to the Empire Insurance Co. advising it of Andal's failure to comply with his undertaking. Demand for the payment of P12,000 was refused, whereupon the Makati Development Corporation filed a complaint in the Court of First Instance of Rizal on May 22, 1961 against the Empire Insurance Co. to recover on the bond in the full amount, plus attorney's fees. In due time, the Empire Insurance Co. filed its answer with a third-party complaint against Andal. It asked that the complaint be dismissed or, in the event of a judgment in favor of the Makati Development Corporation, that judgment be rendered ordering Andal to pay the Empire Insurance Co. whatever amount it may be ordered to pay the Makati Development Corporation, plus interest at 12%, from the date of the filing of the complaint until said amount was fully reimbursed, and attorney's fees.

In his answer, Andal admitted the execution of the bond but alleged that the "special condition" in the deed of sale was contrary to law, morals and public policy. He averred that, at any rate, Juan Carlos had started construction of a house on the lot.

Hearing was held and, on March 28, 1963, the lower court rendered judgment, sentencing the Empire Insurance Co. to pay the Makati Development Corporation the amount of P1,500, with interest at the rate of 12% from the time of the filing of the complaint until the amount was fully paid, and to pay attorney's fees in the amount of

P500, and the proportionate part of the costs. The court directed that in case the amount of the judgment was paid by the Empire Insurance Co., Andal should in turn pay the former the sum of P1,500 with interest at 12% from the time of the filing of the complaint to the time of payment and to pay attorney's fees in the sum of P50 and proportionate part of the costs. The Makati Development Corporation appealed directly to this Court.

In reducing Andal's liability for breach of his unde taking from P12,000, as stipulated in the bond, to P1.500. the court noted that

"[W]hile no building has actually been constructed before the target date which is March 31, 1961, it is also a fact that even before that date the entire area was already fenced with a Stone wall and building materials were also stocked in the premises which are clear indicia of the owner's desire to construct his house with the least possible delay. As a matter of fact the incontrovertible testimony of Juan Carlos is to the effect that by the end of April 1961, he had finished very much more than the required 50% stipulated in the contract of sale. In short there was only really a little delay."

But the appellant argues that Andal became liable for the full amount of his bond upon his failure to build a house within the two-year period which expired on March 31, 1961 and that the trial court was without authority to reduce Andal's liability on the basis of Carlos' construction of a house a month after the stipulated period because there was no privity of contract between Carlos and the Makati Development Corporation.

To begin with, the so-called "special condition" in the deed of sale is in reality an obligation[1]—to build a house at least 50 per cent of which must be finished within two years. It was to secure the performance of this obligation that a penal clause was inserted.

While it is true that in obligations with a penal sanction the penalty takes the place of "damages and the payment of interest in case of non-compliance" [2] and that the obligee is entitled to recover upon the breach of the obligation without the need of proving damages,[3] it is nonetheless true that in certain instances a mitigation of the obligor's liability is allowed. Thus article 1229 of the Civil Code states:

"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 m also be reduced by the courts if it is iniquitous or unconscionable"

Here the trial court found that Juan Carlos had finished more than 50 per cent of his house by April 1961, or barely a month after the expiration on March 31, 1961 of the stipulated period. There was therefore a partial performance of the obligation within the meaning and intent of article 1229.[4] The case of *General Ins. & Surety Corp. vs. Republic*, G. R. L-13873, Jan. 31, 1963[5] cannot be invoked as authority for the forfeiture of the full amount of the bond because unlike this case there was in that case no performance at all of any part of the obligation to secure the payment of salaries to teachers. Indeed, it has been held that where there has been partial or irregular compliance with the provisions in a contract for special indemnification in the event of failure to comply with its terms, courts will rigidly apply the doctrine of strict construction against the enforcement in its entirety of the indemnification, where it is clear from the contract that the amount or character of the indemnity is fixed without regard to the probable damages which might be anticipated as a result of a breach of the terms of the contract, or, in other words, where the indemnity provided for is essentially a mere penalty having for its object the enforcement of compliance with the contract.[6] The penal clause in this case was inserted not to indemnify the Makati Development Corporation for any damage it might suffer as a result of a breach of the contract but rather to compel performance of the so-called "special condition" and thus encourage home building among lot owners in the Urdaneta Village.

Considering that a house had been built shortly after the period stipulated, the substantial, if tardy, performance of

the obligation, having in view the purpose of the penal clause, fully justified the trial court in reducing the penalty. Still it is insisted that Carlos' construction of a house on the lot sold cannot be considered a partial performance of Andal's obligation because Carlos bears no contractual relation to the Makati Development Corporation. This case is in many respects analogous to *Insular Gov't. vs. Amechazurra*, 10 Phil. 637 (1908) where a similar claim was made by a party and rejected by this Court. There the defendant gave a bond for \$800 to guarantee the return to the plaintiff of four firearms issued to him "on demand" of the Government. Three of the firearms were stolen from the defendant so that on demand of the Government he was able to produce only one. Subsequently the Constabulary recovered two of the missing guns and the question was whether defendant was entitled to a litigation of liability even if recovery of the firearms was made possible through the efforts of third parties (the Constabulary). This Court gave an affirmative answer.

Indeed the stipulation in this case to commence the construction and complete at least 50 per cent of the Sendee's house within two years cannot be construed as imposing a strictly personal obligation on Andal. To adopt such a construction would be to limit Andal's right to dispose of the lot. There is nothing in the deed of sale restricting Andal's right to sell the lot at least within the two-year period and we think it plain that a reading of such a limitation on one of the rights of ownership must rest on more explicit language in the contract, it cannot be left to mere inference.

Accordingly, the decision appealed from is affirmed, at appellant's cost.

Concepcion, C. J., Reyes, J. B. L., Dizon, Makalintal, Bengzon, J. P., Zaldivar and Sanchez, JJ., concur.

Judgment affirmed.

[1] For a discussion of the difference between a penalty and a condition, see 3 Padilla, Civil Law 208 (1956).

[2] Civ. Code art. 1226.

[3] E. g., *General Ins. & Surety Corp. vs. Republic*, G. R, No. L-13873, Jan. 31, 1963; *Lambert vs. Fox*, 26 Phil. 588 (1914); *Pa- vs. Municipality of Cavite*, 12 Phil. 140 (1908).

[4] See *Insular Gov't. vs. Punzalan*, 7 Phil. 547 (1907).

[5] The following is quoted from General Insurance.:

"There is nothing against public policy in forfeiting the bond for the full amount. The bond is penal in nature. Article 15 of the Code states that in an obligation with a penal clause the penalty shall substitute the indemnity for damages and the payment of interests in case of non-compliance, if there is stipulation to the contrary, and the party to whom payment to be made is entitled to recover the sum stipulated without need of proving damages because one of the primary purposes of the penalty clause is to avoid such necessity, (citations omitted) The mere non-performance of the principal obligation gives rise to the right to the penalty, (citation omitted)"

[6] *Laureano vs. Kilayco*, 32 Phil. 194, 200 (1915).

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