

**HEIRS OF MARY LANE R. KIM, REPRESENTED BY KIM SUNG II,
JANICE KIM AND BILLIELYN SHAFER, PETITIONERS, VS. JASPER
JASON M. QUICHO, JOINED BY HIS WIFE, RESPONDENTS.**

G.R. No. 249247. March 15, 2021

Ponente: LOPEZ, J., J.

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LOPEZ, J., J.:

Before this Court is a Petition for Review[1] challenging the Decision[2] dated December 27, 2018 and the Resolution[3] dated August 23, 2019 of the Court Appeals (CA) in CA-G.R. CV No. 108254. The assailed Decision affirmed with modification the Decision[4] dated July 11, 2016 and the Order[5] dated October 14, 2016 of the Regional Trial Court (RTC) of Olongapo City, Branch 75, in Civil Case No. 87-0-14. The challenged Resolution, on the other hand, denied petitioners' Motion for Partial Reconsideration.

Antecedents

During her lifetime, Mary Lane R. Kim (Kim) owned a 250-ton Portable Crusher and a five (5)-hectare parcel of land situated at Sitio Sapang Bayabas, Pabanlag, Floridablanca (subject lot), where the same portable crusher is installed.[6] Sometime in 2011, Jasper Jayson M. Quicho (Quicho) approached Kim and proposed to buy her portable crusher with all its accessories, which he will need to start a crushing plant business.[7] In line with this venture, Kim and Quicho executed a Deed of Conditional Sale dated August 4, 2011, where the former agreed to sell her portable crusher with all its accessories to the latter, for P18,000,000.00, payable in the following terms: P5,000,000.00 upon the execution of the contract, P5,000,000.00 within one (1) month from the signing of the contract, and the balance of P8,000,000.00 within a period of one (1) year from the commencement of his business operation.[8] The parties also stipulated in the Deed of Conditional Sale that the same shall be rescinded without need of a court action whereby the partial payments made shall be forfeited and considered as rentals in case of breach.[9] The pertinent portions of the Deed of Conditional Sale are quoted hereunder:

x x x that should the VENDEE fail to pay an[y] of the installments, when due, or otherwise fail to comply with any of the terms and conditions, herein stipulated, then this Deed of Conditional Sale shall automatically and without any further formality, become null and void, AND all sums so paid by the VENDEE by reason thereof, shall, except as herein provided, be considered as rentals and the VENDOR shall then and there be free to take possession thereof or sell the property to any other party.[10]

The parties, likewise, executed a Contract of Lease on August 15, 2011, for the use of the subject lot where the crusher would be operated.[11]

On the first week of October 2012, Kim successfully turned over the portable crusher and the subject lot to Quicho who accepted the same.[12] Quicho then paid a total of P9,000,000.00, but he, however failed to settle the succeeding installments despite several written demands, which prompted Kim to send a Notice of Rescission of Contracts dated October 31, 2013.[13] This notwithstanding, Quicho continuously refused to pay his outstanding balance which led Kim to file a complaint for the rescission of their contracts before the RTC.[14]

For failing to file his Answer, Quicho was initially declared in default, but the said order was eventually lifted by the RTC in its Order dated September 14, 2015.[15] In his Answer, Quicho claimed, among others, that the rescission of the contracts entitled him for the return of his P9,000,000.00 which he already paid to Kim, plus interest, since restitution is one of the effects thereof.[16]

Ruling of the RTC

After due proceedings, the RTC, in its Decision dated July 11, 2016, ruled in favor of petitioner Kim, convinced that she had already performed her obligations under the contracts when she delivered her crusher and subject lot to Quicho.[17] In return, full payment of the purchase price, among others, is expected from Quicho, but he failed to pay which entitled Kim to rescind their contracts.[18] Thus, the RTC in its assailed Decision, decreed:

WHEREFORE, judgment is rendered:

1. Declaring the Deed of Conditional Sale of [the] 250-ton Portable Crusher dated August 4, 2011 and the Contract of Lease dated August 15, 2011 rescinded and of no more legal effect;
2. Ordering the defendant, his successors or assigns[,] to surrender to the plaintiffs the peaceful possession of the 250-ton portable crusher and its accessories as well as the 5[-]hectare property subject of the Contract of Lease; and
3. Ordering the defendant to pay plaintiff (a) attorney's fees of Php50,000.00 inclusive of litigation expenses; (b) exemplary damages in the amount of Php50,000.00; and
4. Ordering the defendant to pay the cost of suit.

SO DECIDED.[19]

Dissatisfied, Quicho filed a Motion for New Trial (Motion) on the ground that he was denied due process as a consequence of the alleged negligence of his counsel.[20] In the interim, Kim passed away, thus she was substituted by her heirs, namely: Kim Sung II, Janice R. Kim and Billielyn R. Shafer (collectively referred to as herein petitioners), on September 13, 2016.[21] On October 14, 2016, the RTC found the Motion to be equally without merit and denied the same in an Order of even date.[22]

Unyielding, Quicho appealed before the CA.

Ruling of the CA

In its assailed Decision, the CA held that Kim had the right to rescind the contract under Article 1191 of the Civil Code because Quicho failed to comply with his obligation to pay the balance of the purchase price, the labor cost for setting up an operating crushing processing plant, and the monthly rental on the subject lot.[23] Nonetheless, the CA ordered petitioners, as heirs of the late Kim, to return the money paid by Quicho since rescission requires a mutual restitution of the benefits received.[24] Hence, the CA denied the appeal in its assailed Decision, the dispositive portion of which states:

FOR THESE REASONS, the instant appeal is hereby DISMISSED. The Decision dated 11 July 2016 and Order dated 14 October 2016 rendered by Branch 75 of the Third Judicial Region of the Regional Trial Court (RTC) of Olongapo City in Civil Case No. 87-0-14 are AFFIRMED with the MODIFICATION that appellees are ordered to return to appellants the amount of P9,000,000.00 which the latter paid as a consequence of the rescinded contract, with 6% legal interest thereon from 31 October 2013, the date of rescission.

SO ORDERED.[25]

Dissatisfied, petitioners moved for a partial reconsideration of the ruling aforesaid, insofar as it ordered them to return the partial payments of Quicho, contending that the said amounts should be forfeited, as expressly

stipulated in the contract.[26] However, the CA, in its assailed Resolution, denied their motion, guided by the rule that "rescission abrogates the contract from its inception and restores the parties to their original positions prior to the inception of the contract." [27]

Unperturbed, petitioners elevated the case before this Court and raised this lone assignment of error:

WHETHER [THE CA] COMMITTED AN ERROR IN DISREGARDING THE FORFEITURE CLAUSE IN THE CONTRACT AND IN REQUIRING THE PETITIONERS TO PAY THE RESPONDENTS WHO ARE GUILTY OF BREACH OF CONTRACT.[28]

In their petition, petitioners asserted in the main, that the partial payments from respondent Quicho should be forfeited in their favor, owing to the following reasons: first, there is an express stipulation to that effect in their contract;[29] and second, respondents will be unjustly enriched at their expense since the former derived income from the use of the subject properties for at least eight (8) years.[30]

On the contrary, respondents, in their Comment,[31] asserted that petitioners should return the amounts paid based on the following grounds: first, the legal consequence of rescission is mutual restitution which the CA had correctly ruled;[32] and second, [r]escission extinguishes the obligation with retroactive effect,[33] thus, the forfeiture of payment stipulated in the contract was deemed abrogated by operation of law.[34]

Our Ruling

The Court resolves to grant the petition.

At the outset, the Court underscores that respondents did not deny that they failed to pay the balance of the purchase price despite repeated demands, a finding which both the CA and the RTC uniformly held.[35] Likewise, both parties recognized Kim's right to rescind the contract under Article 1191 of the Civil Code.[36] Nonetheless, the parties differ with how the effect of rescission ought to be. Petitioners argued that the amounts paid should be considered as rentals for the use of the subject properties to avoid unjust enrichment on the part of respondents.[37] Quite the contrary, respondents maintained that the forfeiture of partial payments stipulated in the contract was deemed abrogated by operation of law.[38]

With this as premise, the Court shall now address the issue whether petitioners can retain the amounts paid by respondents despite the rescission of the contract.

The Court answers in the affirmative.

Rescission on account of breach of reciprocal obligations is provided under Article 1191 of the Civil Code,[39] which states:

ARTICLE 1191. The power to rescind obligations is implied in reciprocal ones, in case one of the obligors should not comply with what is incumbent upon him.

The injured party may choose between the fulfillment and the rescission of the obligation, with the payment of damages in either case. He may also seek rescission, even after he has chosen fulfillment, if the latter should become impossible.

The court shall decree the rescission claimed, unless there be just cause authorizing the fixing of a period.

This is understood to be without prejudice to the rights of third persons who have acquired the thing, in accordance with articles 1385 and 1388 and the Mortgage Law.

This provision refers to rescission applicable to reciprocal obligations. It is invoked when there is noncompliance by one (1) of the contracting parties in case of reciprocal obligations. "Reciprocal obligations are those which

arise from the same cause, and in which each party is a debtor and a creditor of the other, such that the obligation of one is dependent upon the obligation of the other. They are to be performed simultaneously such that the performance of one is conditioned upon the simultaneous fulfillment of the other." [40]

Rescission under Article 1191 will be ordered when a party to a contract fails to comply with his or her obligation. Rescission "is a principal action that is immediately available to the party at the time that the reciprocal [obligation] was breached." [41]

Here, both parties have reciprocal obligations. Kim bound herself to turn over the portable crusher and the subject land to Quicho, while the latter obligated himself to pay a total of P19,500,000.00, [42] which includes the price of the portable crusher (P18,000,000.00) and labor costs to set up an operating crushing processing plant (P1,500,000). [43] Regrettably, Quicho failed to comply with his undertaking, which prompted Kim to have their contract rescinded. [44]

Rescission of the obligation under Article 1191 is a declaration that a contract is void at its inception. Its effect is to restore the parties to their original position, insofar as practicable. [45] Mutual restitution is required in cases involving rescission under Article 1191. "Where a contract is rescinded, it is the duty of the court to require both parties to surrender that which they have respectively received and to place each other as far as practicable in his original situation[;] the rescission has the effect of abrogating the contract in all parts." [46]

Be that as it may, the Court, in *Camp John Jay Development Corporation v. Charter Chemical and Coating Corporation (Camp John Hay)*, [47] clarified that "[a]lthough rescission repeals the contract from its inception, it does not disregard all the consequences that the contract has created." [48]

One such consequence that remains is the validity of the forfeiture or penalty clause stipulated by the parties in a contract. [49] In this accord, the Court, in *Laperal and Filipinas Golf & Country Club Inc., v. Solid Homes, Inc., et al., (Laperal)* [50] recognized the validity of a forfeiture or penalty clause which the parties stipulated in a contract that was eventually rescinded.

It is well to note that rescission under Article 1191 of the Civil Code gives the injured party two (2) remedies: first, exact fulfillment; and second, rescind the contract, with payment of damages in either case. Along this line, the Court, in *Laperal*, applied the forfeiture or penalty clause notwithstanding the rescission of the contract where it was stipulated, reasoning in this wise:

If this Court recognized the right of the parties to stipulate on an extrajudicial rescission under Article 1191, there is no reason why this Court will not allow the parties to stipulate on the matter of damages in case of such rescission under Book IV, Title VIII, Chapter 3, Section 2 of the Civil Code governing liquidated damages. [51]

In the same vein, the Court, in *Philippine Economic Zone Authority (PEZA) v. Pilhino Sales Corporation*, [52] categorically held that "mutual restitution under Article 1191 is, however, no license for the negation of contractually stipulated liquidated damages." While the *Laperal* case involves extrajudicial rescission, and the *PEZA* case entails rescission through judicial action, "this distinction does not diminish the rights of a contracting party under Article 1191 of the Civil Code and is immaterial for purposes of the availability of liquidated damages." [53]

Prescinding therefrom, the rescission of the contract did not render the forfeiture or penalty clause inoperative, but rather brought to fore its application. Undoubtedly, the parties stipulated on the forfeiture or penalty clause precisely to facilitate the injured party's recompense in case of breach. In doing so, the parties already determined for themselves that forfeiture of the payments made shall be sufficient as a measure of indemnity to the injured party, which is actually in consonance with "the [s]tate's policy to promote party autonomy in the mode of

resolving disputes."[54]

When parties enter into contracts, they are free to stipulate on the terms and conditions of their agreement as they may deem convenient,[55] including a particular method of settling any conflict between them.[56] Contracts have the force of law between the contracting parties. Thus, whatever stipulations agreed upon [between the parties] must be complied with in good faith.[57]

Needless to say, "a contracting party's failure, without legal reason, to comply with contract stipulations breaches their contract and can be the basis for the award of damages to the other contracting party."[58] As a consequence of this rule, "it is not for this Court to release said party from its obligation."[59] In *Esguerra v. Court of Appeals*,[60] the Court emphasized that courts cannot relieve parties from the legal consequences of the obligations they voluntarily assumed, thus:

It is a long established doctrine that the law does not relieve a party from the effects of an unwise, foolish, or disastrous contract, entered into with all the required formalities and with full awareness of what he was doing. Courts have no power to relieve parties from obligations voluntarily assumed, simply because their contracts turned out to be disastrous deals or unwise investments.

The Court cannot take a contrary stand for to do so will violate not only the principle of autonomy of contracts, but also undermine the contract's obligatory force by the simple expedient of a party's deliberate non-compliance. As aptly put by the Court in *PEZA*:

To sustain respondent's claim would be to sustain an absurdity and an injustice. Respondent's position suggests that with rescission must necessarily come the obliteration of the punitive consequence which, to begin with, was the product of its own (along with the other contracting party's) volition. Its position turns delinquency into a profitable enterprise, enabling contractual breach to itself be the means for evading its own fallout. It is a position we cannot tolerate.[61]

Moreso, the payments made partake of the nature of an earnest money. Earnest money, under Article 1482 of the Civil Code, is ordinarily given in a perfected contract of sale. However, earnest money may also be given in a contract to sell.[62]

In a contract to sell, earnest money is generally intended to compensate the seller for the opportunity cost of not looking for any other buyers.[63] It is a show of commitment on the part of the party who intimates his or her willingness to go through with the sale after a specified period or upon compliance with the conditions stated in the contract to sell.[64]

Opportunity cost is defined as "the cost of the foregone alternative." [65] In a potential sale, the seller reserves the property for a potential buyer and foregoes the alternative of searching for other offers.[66] This Court, in *Philippine National Bank v. Court of Appeals*, [67] construed earnest money given in a contract to sell as "consideration for [seller's] promise to reserve the subject property for [the buyer]." The seller, "in excluding all other prospective buyers from bidding for the subject property ... [has given] up what may have been more lucrative offers or better deals." [68]

Earnest money, therefore, is paid for the seller's benefit. It is part of the purchase price while at the same time proof of commitment by the potential buyer.[69] Absent proof of a clear agreement to the contrary, it is intended to be forfeited if the sale does not happen without the seller's fault.[70] For this reason, the Court, in *Racelis v. Javier*, [71] ruled that "[t]here is no unjust enrichment on the part of the seller should the initial payment be deemed forfeited. After all, the owner could have found other offers or a better deal. The earnest money given by respondents is the cost of holding this search in abeyance."

Towards this end, the Supreme Court, in *Spouses Godinez v. Spouses Norman (Godinez)*,^[72] held that "partial payments may be retained and considered as rentals by the seller if the buyer was given possession or was able to use the property prior to transfer of title." In *Godinez*, the Court ruled that it is only proper that respondents reciprocate their use of the premises with the payment of rentals while full payment on their contract was still pending, to compensate petitioners' inability to enjoy or use their own property.^[73] Here, the records show that petitioners were unable to use the property during the duration of their contract with respondents, for at least eight (8) years.^[74] Thus, this Court finds that the partial payments made by respondents may be converted into rentals.^[75]

The conversion of partial payments into rentals is also consistent with Article 1378 of the Civil Code, which teaches that doubts in the interpretation of onerous contracts "should be settled in favor of the greatest reciprocity of interests."^[76] Construction of the terms of a contract, which would amount to impairment or loss of right, is not favored. Conservation and preservation, not waiver, abandonment or forfeiture of a right, is the rule.^[77]

In order to harmonize the pertinent jurisprudence on the matter, the Court so holds that as a general rule, the rescission of a contract under Article 1191 of the Civil Code will result in the mutual restitution of the benefits which the parties received, except in the following instances: 1) when there is an express stipulation to the contrary by way of a forfeiture or penalty clause in recognition of the parties' autonomy to contract; or 2) if the buyer was given possession or was able to use the property prior to transfer of title, where in such case, partial payments may be retained and considered as rentals by the seller to avoid unjust enrichment.

Over time, courts have recognized with almost pedantic adherence that what is inconvenient or contrary to reason is not allowed in law.^[78] Thus, the injured party should be afforded recompense in the exceptions enumerated in order to give life and meaning to the purpose of the law.

WHEREFORE, the Petition for Review on Certiorari is GRANTED. The Court of Appeals' Decision dated December 27, 2018 and its Resolution dated on August 23, 2019 in CA-G.R. CV No. 108254 are hereby AFFIRMED with MODIFICATION in that the ORDER for the heirs of Mary Lane R. Kim TO PAY Jasper Jason M. Quicho and his wife, P9,000,000.00, with six percent (6%) legal interest is hereby DELETED. The rest of the assailed CA Decision and Resolution stand.

Accordingly, Jasper Jason M. Quicho and his wife are likewise ordered to pay the heirs of Mary Lane R. Kim the following amounts: a) attorney's fees of Php50,000.00 inclusive of litigation expenses, and b) exemplary damages in the amount of Php50,000.00.

Ail damages awarded shall earn interest at the rate of six percent (6%) per annum from the date of the finality of this Decision until fully paid.

SO ORDERED.

Leonen, (Chairperson, Third Division), Hernando, Inting, and Delos Santos, JJ., concur.

[1] Rollo, pp. 9-33.

[2] Penned by Honorable Associate Justice Elihu A. Ybañez, with Associate Justices Ma. Luisa Quijano-Padilla and Perpetua T. Atal-Paño, concurring; *id.* at 35-50.

[3] *Id.* at 52-55.

[4] Penned by Judge Raymond C. Viray; rollo, pp. 75-81.

- [5] Rollo, pp. 82-84.
- [6] Id. at 36.
- [7] Id.
- [8] Id.
- [9] Id. at 13-14.
- [10] Id. (Emphasis supplied)
- [11] Id. at 36.
- [12] Id.
- [13] Id. at 36-37.
- [14] Id.
- [15] Id. at 37-38.
- [16] Id. at 38.
- [17] Id. at 39.
- [18] Id.
- [19] Id. at 39. (Emphasis in the original)
- [20] Id. at 40.
- [21] Id.
- [22] Id.
- [23] Rollo, p. 45.
- [24] Id. at 46-48.
- [25] Id. at 49. (Emphasis in the original)
- [26] Id. at 53-54.
- [27] Id. at 55.
- [28] Rollo, 9, 19.
- [29] Id.
- [30] Id. at 20-22.
- [31] Id. at 132-140.
- [32] Id. at 133.
- [33] Id. at 134.
- [34] Id. at 137-138.
- [35] Id. at 39 in relation to rollo, p. 43.

[36] *Id.* at 23 in relation to rollo, p. 133.

[37] *Id.*

[38] Rollo, pp. 137-138.

[39] *Camp John Jay Development Corporation v. Charter Chemical and Coating Corporation*, G.R. No. 198849, August 7, 2019.

[40] *Id.* citing *The Wellex Group. Inc. v. U-Land Airlines, Co., Ltd*, 750 Phil. 530, 585 (2015), citing *Ong v. Court of Appeals*, 369 Phil. 243-257 (1999).

[41] *Camp John Jay Development Corporation v. Charter Chemical and Coating Corporation*, *supra* note 36.

[42] Rollo, pp. 36-37.

[43] *Id.* at 37.

[44] *Id.*

[45] *Camp John Jay Development Corporation v. Charter Chemical and Coating Corporation*, *supra* note 36.

[46] *Id.*

[47] *Supra* note 36.

[48] *Id.*

[49] *Laperal v. Solid Homes, Inc., et al.*, 499 Phil. 367, 380 (2005).

[50] *Supra*.

[51] *Id.* (Emphasis supplied).

[52] 796 Phil. 79, 90 (2016).

[53] *Id.* at 92.

[54] *Steamship Mutual Underwriting Association (Bermuda) Limited v. Sulpicio Lines, Inc.*, G.R. Nos. 196072 & 208603, September 20, 2017, citing *Bases Conversion Development Authority v. DMCI Project Developers, Inc.*, G.R. No. 173137 & 173170, January 11, 2015.

[55] *CJH Development Corporation v. Aniceto*, G.R. Nos. 224006 & 224474, July 6, 2020, citing *Spouses Mallari v. Prudential Bank*, 110 Phil. 490 (2013).

[56] *Steamship Mutual Underwriting Association (Bermuda) Limited v. Sulpicio Lines, Inc.*, *supra* note 51, citing *Chung Fu Industries (Philippines), Inc. v. Court of Appeals*, 283 Phil. 474, 483 (1992).

[57] *CJH Development Corporation v. Aniceto*, G.R. Nos. 224006 & 224474, July 6, 2020, citing *Bustamante v. Spouses Rosel*, 311 Phil. 436 (1999).

[58] *Talampas Jr. v. Moldex Realty, Inc.*, 760 Phil. 632, 646 (2015), citing in *RCPI v. Verchez*, 516 Phil. 725, 735 (2006), citing *FGU Insurance Corporation v. G.P. Sarmiento Trucking Corporation*, 435 Phil. 333, 341-342 (2002).

[59] *Laperal v. Solid Homes, Inc., et al.*, *supra* note 46, at 383.

[60] 335 Phils. 58, 69 (1997).

[61] Philippine Ecorwmic Zone Authority v. Pilhino Sales Corporation, *supra* note 49, at 92. (Emphasis supplied)

[62] *Racelis v. Javier*, G.R. No. 189609, January 29, 2018, 853 SCRA 256, 273.

[63] *Id.* (Emphasis supplied)

[64] *Id.* at 273-274.

[65] *Id.* citing *Reyes v. Spouses Valentin*, 753 Phil. 551 (2015).

[66] *Id.* at 274.

[67] 330 Phil. 1048 (1996).

[68] *Racelis v. Spouses Javier*, 1073 *supra* note 59 at 274, citing *Philippine National Bank v. Court of Appeals*, *supra*.

[69] *Racelis v. Spouses Javier*, *supra* note 59 at 274. (Emphasis supplied)

[70] *Id.* (Emphasis supplied)

[71] *Supra* note 59, at 274.

[72] G.R. No. 225449, February 26, 2020. (Emphasis supplied)

[73] *Id.* (Emphasis supplied)

[74] *Rollo*, pp. 20-22.

[75] *Spouses Godinez v. Spouses Norman*, *supra* note 69.

[76] *Id.* (Emphasis supplied)

[77] *Agas v. Sabico*, 496 Phil. 729, 742 (2005).

[78] *Gotesco Properties Inc., et al. v. Spouses Fajardo*, 705 Phil. 294, 304 (2013), citing *Solid Homes v. Spouses Tan*, 503 Phil. 121, 133 (2005).

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