

SOCIAL SECURITY SYSTEM, PETITIONER, VS. MOONWALK DEVELOPMENT & #038; HOUSING CORPORATION, ROSITA U. ALBERTO, ROSITA U. ALBERTO, JMA HOUSE, INC., MILAGROS SANCHEZ SANTIAGO, IN HER CAPA...

G.R. No. 73345. April 07, 1993

Ponente: CAMPOS, JR., J.

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CAMPOS, JR., J.:

Before Us is a petition for review on certiorari of a decision[1] of the then Intermediate Appellate Court affirming in toto the decision of the former Court of First Instance of Rizal, Seventh Judicial District, Branch XXIX, Pasay City.

The facts as found by the Appellate Court are as follows:

"On February 20, 1980, the Social Security System, SSS for brevity, filed a complaint in the Court of First Instance of Rizal against Moonwalk Development & Housing Corporation, Moonwalk for short, alleging that the former had committed an error in failing to compute the 12% interest due on delayed payments on the loan of Moonwalk --- resulting in a chain of errors in the application of payments made by Moonwalk and, in an unpaid balance on the principal loan agreement in the amount of P7,053.77 and, also in not reflecting in its statement or account an unpaid balance on the said penalties for delayed payments in the amount of P7,517,178.21 as of October 10, 1979.

Moonwalk answered denying SSS' claims and asserting that SSS had the opportunity to ascertain the truth but failed to do so.

The trial court set the case for pre-trial at which pre-trial conference, the court issued an order giving both parties thirty (30) days within which to submit a stipulation of facts.

The Order of October 6, 1980 dismissing the complaint followed the submission by the parties on September 19, 1980 of the following stipulation of Facts:

"1. On October 6, 1971, plaintiff approved the application of defendant Moonwalk for an interim loan in the amount of THIRTY MILLION PESOS (P30,000,000.00) for the purpose of developing and constructing a housing project in the provinces of Rizal and Cavite;

"2. Out of the approved loan of THIRTY MILLION PESOS (P30,000,000.00), the sum of P9,595,000.00 was released to defendant Moonwalk as of November 28, 1973;

"3. A third Amended Deed of First Mortgage was executed on December 18, 1973. Annex 'D' providing for restructuring of the payment of the released amount of P9,595,000.00.

"4. Defendants Rosita U. Alberto and Rosita U. Alberto, mother and daughter respectively, under paragraph 5 of the aforesaid Third Amended Deed of First Mortgage substituted Associated Construction and Surveys

Corporation, Philippine Model Homes Development Corporation, Mariano Z. Velarde and Eusebio T. Ramos, as solidary obligors;

"5. On July 23, 1974, after considering additional releases in the amount of P2,659,700.00, made to defendant Moonwalk, defendant Moonwalk delivered to the plaintiff a promissory note for TWELVE MILLION TWO HUNDRED FIFTY FOUR THOUSAND SEVEN HUNDRED PESOS (P12,254,700.00) Annex 'E', signed by Eusebio T. Ramos, and the said Rosita U. Alberto and Rosita U. Alberto;

"6. Moonwalk made a total payment of P23,657,901.84 to SSS for the loan principal of P12,254,700.00 released to it. The last payment made by Moonwalk in the amount of P15,004,905.74 were based on the Statement of Account, Annex "F" prepared by plaintiff SSS for defendant;

"7. After settlement of the account stated in Annex 'F' plaintiff issued to defendant Moonwalk the Release of Mortgage for Moonwalk's mortgaged properties in Cavite and Rizal, Annexes 'G' and 'H' on October 9, 1979 and October 11, 1979 respectively.

"8. In letters to defendant Moonwalk, dated November 28, 1979 and followed up by another letter dated December 17, 1979, plaintiff alleged that it committed an honest mistake in releasing defendant.

"9. In a letter dated December 21, 1979, defendant's counsel told plaintiff that it had completely paid its obligations to SSS;

"10. The genuineness and due execution of the documents marked as Annex (sic) 'A' to 'O' inclusive, of the Complaint and the letter dated December 21, 1979 of the defendant's counsel to the plaintiff are admitted.

"Manila for Pasay City, September 2, 1980.""[2]

On October 6, 1990, the trial court issued an order dismissing the complaint on the ground that the obligation was already extinguished by the payment by Moonwalk of its indebtedness to SSS and by the latter's act of cancelling the real estate mortgages executed in its favor by defendant Moonwalk. The Motion for Reconsideration filed by SSS with the trial court was likewise dismissed by the latter.

These orders were appealed to the Intermediate Appellate Court. Respondent Court reduced the errors assigned by the SSS into this issue: "x x x are defendants'appellees, namely, Moonwalk Development and Housing Corporation, Rosita U. Alberto, Rosita U. Alberto, JMA House, Inc. still liable for the unpaid penalties as claimed by plaintiff-appellant or is their obligation extinguished?"[3] As We have stated earlier, the respondent Court held that Moonwalk's obligation was extinguished and affirmed the trial court.

Hence, this Petition wherein SSS raises the following grounds for review:

"First, in concluding that the penalties due from Moonwalk are "deemed waived and/or barred," the appellate court disregarded the basic tenet that waiver of a right must be express, made in a clear and unequivocal manner. There is no evidence in the case at bar to show that SSS made a clear, positive waiver of the penalties, made with full knowledge of the circumstances.

Second, it misconstrued the ruling that SSS funds are trust funds, and SSS, being a mere trustee, cannot perform acts affecting the same, including condonation of penalties, that would diminish property rights of the owners and beneficiaries thereof. (United Christian Missionary Society v. Social Security Commission, 30 SCRA 982, 988 [1969])

Third, it ignored the fact that penalty at the rate of 12% p.a. is not inequitable.

Fourth, it ignored the principle that equity will cancel a release on the ground of mistake of fact."[4]

The same problem which confronted the respondent court is presented before Us: Is the penalty demandable even after the extinguishment of the principal obligation?

The former Intermediate Appellate Court, through Justice Eduardo P. Caguioa, held in the negative. It reasoned, thus:

"2. As we have explained under No. 1, contrary to what the plaintiff-appellant states in its Brief, what is sought to be recovered in this case is not the 12% interest on the loan but the 12% penalty for failure to pay on time the amortization. What is sought to be enforced therefore is the penal clause of the contract entered into between the parties.

Now, what is a penal clause. A penal clause has been defined as

"an accessory obligation which the parties attach to a principal obligation for the purpose of insuring the performance thereof by imposing on the debtor a special prestation (generally consisting in the payment of a sum of money) in case the obligation is not fulfilled or is irregularly or inadequately fulfilled" (3 Castan 8th Ed. p. 118)

Now an accessory obligation has been defined as that attached to a principal obligation in order to complete the same or take its place in the case of breach (4 Puig Peña Part 1 p. 76). Note therefore that an accessory obligation is dependent for its existence on the existence of a principal obligation. A principal obligation may exist without an accessory obligation but an accessory obligation cannot exist without a principal obligation. For example, the contract of mortgage is an accessory obligation to enforce the performance of the main obligation of indebtedness. An indebtedness can exist without the mortgage but a mortgage cannot exist without the indebtedness, which is the principal obligation. In the present case, the principal obligation is the loan between the parties. The accessory obligation of a penal clause is to enforce the main obligation of payment of the loan. If therefore the principal obligation does not exist the penalty being accessory cannot exist.

Now then when is the penalty demandable? A penalty is demandable in case of non performance or late performance of the main obligation. In other words in order that the penalty may arise there must be a breach of the obligation either by total or partial non fulfillment or there is non fulfillment in point of time which is called mora or delay. The debtor therefore violates the obligation in point of time if there is mora or delay. Now, there is no mora or delay unless there is a demand. It is noteworthy that in the present case during all the period when the principal obligation was still subsisting, although there were late amortizations there was no demand made by the creditor, plaintiff-appellant for the payment of the penalty. Therefore up to the time of the letter of plaintiff-appellant there was no demand for the payment of the penalty, hence the debtor was not in mora in the payment of the penalty.

However, on October 1, 1979, plaintiff-appellant issued its statement of account (Exhibit F) showing the total obligation of Moonwalk as P15,004,905.74, and forthwith demanded payment from defendant-appellee. Because of the demand for payment, Moonwalk made several payments on September 29, October 9 and 19, 1979 respectively, all in all totalling P15,004,905.74 which was a complete payment of its obligation as stated in Exhibit F. Because of this payment the obligation of Moonwalk was considered extinguished, and pursuant to said extinguishment, the real estate mortgages given by Moonwalk were released on October 9, 1979 and October 10, 1979 (Exhibits G and H). For all purposes therefore the principal obligation of defendant-appellee was deemed extinguished as well as the accessory obligation of real estate mortgage; and that is the reason for the release of all the Real Estate Mortgages on October 9 and 10, 1979 respectively.

Now, besides the Real Estate Mortgages, the penal clause which is also an accessory obligation, must also be deemed extinguished considering that the principal obligation was considered extinguished, and the penal clause being an accessory obligation cannot exist without a principal obligation. That being the case, the

demand for payment of the penal clause made by plaintiff-appellant in its demand letter dated November 28, 1979 and its follow up letter dated December 17, 1979 (which parenthetically are the only demands for payment of the penalties) are therefore ineffective as there was nothing to demand. It would be otherwise, if the demand for the payment of the penalty was made prior to the extinguishment of the obligation because then the obligation of Moonwalk would consist of: 1) the principal obligation 2) the interest of 12% on the principal obligation and 3) the penalty of 12% for late payment for after demand, Moonwalk would be in mora and therefore liable for the penalty.

Let it be emphasized that at the time of the demand made in the letters of November 28, 1979 and December 17, 1979 as far as the penalty is concerned, the defendant-appellee was not in default since there was no mora prior to the demand. That being the case, therefore, the demand made after the extinguishment of the principal obligation which carried with it the extinguishment of the penal clause being merely an accessory obligation, was an exercise in futility.

3. At the time of the payment made of the full obligation on October 10, 1979 together with the 12% interest by defendant-appellee Moonwalk; its obligation was extinguished. It being extinguished, there was no more need for the penal clause. Now, it is to be noted that penalty at anytime can be modified by the Court. Even substantial performance under Art. 1234 authorizes the Court to consider it as complete performance minus damages. Now, Art. 1229 Civil Code of the Philippines provides:

"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."

If the penalty can be reduced after the principal obligation has been partly or irregularly complied with by the debtor, which is nonetheless a breach of the obligation, with more reason the penal clause is not demandable when full obligation has been complied with since in that case there is no breach of the obligation. In the present case, there has been as yet no demand for payment of the penalty at the time of the extinguishment of the obligation, hence there was likewise an extinguishment of the penalty.

Let Us emphasize that the obligation of defendant-appellee was fully complied with by the debtor, that is, the amount loaned together with the 12% interest has been fully paid by the appellee. That being so, there is no basis for demanding the penal clause since the obligation has been extinguished. Here there has been a waiver of the penal clause as it was not demanded before the full obligation was fully paid and extinguished. Again, emphasis must be made on the fact that plaintiff-appellant has not lost anything under the contract since it got back in full the amount loan (sic) as well as the interest thereof. The same thing would have happened if the obligation was paid on time, for then the penal clause, under the terms of the contract would not apply. Payment of the penalty does not mean gain or loss of plaintiff-appellant since it is merely for the purpose of enforcing the performance of the main obligation. Since the obligation has been fully complied with and extinguished, the penal clause has lost its *raison d'etre*." [5]

We find no reason to depart from the appellate court's decision. We, however, advance the following reasons for the denial of this petition.

Article 1226 of the Civil Code provides:

"Art. 1226. In obligations with a penal clause, the penalty shall substitute the indemnity for damages and the payment of interests in case of noncompliance, if there is no stipulation to the contrary. Nevertheless, damages shall be paid if the obligor refuses to pay the penalty or is guilty of fraud in the fulfillment of the obligation.

The penalty may be enforced only when it is demandable in accordance with the provisions of this Code."
(Underscoring Ours.)

A penal clause is an accessory undertaking to assume greater liability in case of breach.[6] It has a double function: (1) to provide for liquidated damages, and (2) to strengthen the coercive force of the obligation by the threat of greater responsibility in the event of breach.[7] From the foregoing, it is clear that a penal clause is intended to prevent the obligor from defaulting in the performance of his obligation. Thus, if there should be default, the penalty may be enforced. One commentator of the Civil Code wrote:

"Now when is the penalty deemed demandable in accordance with the provisions of the Civil Code? We must make a distinction between a positive and a negative obligation. With regard to obligations which are positive (to give and to do), the penalty is demandable when the debtor is in mora; hence, the necessity of demand by the debtor unless the same is excused. x x x"[8]

When does delay arise? Under the Civil Code, delay begins from the time the obligee judicially or extrajudicially demands from the obligor the performance of the obligation.

"Art. 1169. Those obliged to deliver or to do something incur in delay from the time the obligee judicially or extrajudicially demands from them the fulfillment of their obligation."

There are only three instances when demand is not necessary to render the obligor in default. These are the following:

"(1) When the obligation or the law expressly so declares;

(2) When from the nature and the circumstances of the obligation it appears that the designation of the time when the thing is to be delivered or the service is to be rendered was a controlling motive for the establishment of the contract; or

(3) When the demand would be useless, as when the obligor has rendered it beyond his power to perform."[9]

This case does not fall within any of the established exceptions. Hence, despite the provision in the promissory note that "(a) II amortization payments shall be made every first five (5) days of the calendar month until the principal and interest on the loan or any portion thereof actually released has been fully paid,"[10] petitioner is not excused from making a demand. It has been established that at the time of payment of the full obligation, private respondent Moonwalk has long been delinquent in meeting its monthly arrears and in paying the full amount of the loan itself as the obligation matured sometime in January, 1977. But mere delinquency in payment does not necessarily mean delay in the legal concept. To be in default "x x x is different from mere delay in the grammatical sense, because it involves the beginning of a special condition or status which has its own peculiar effects or results." [11] In order that the debtor may be in default it is necessary that the following requisites be present: (1) that the obligation be demandable and already liquidated; (2) that the debtor delays performance; and (3) that the creditor requires the performance judicially and extrajudicially.[12] Default generally begins from the moment the creditor demands the performance of the obligation.[13]

Nowhere in this case did it appear that SSS demanded from Moonwalk the payment of its monthly amortizations. Neither did it show that petitioner demanded the payment of the stipulated penalty upon the failure of Moonwalk to meet its monthly amortization. What the complaint itself showed was that SSS tried to enforce the obligation sometime in September, 1977 by foreclosing the real estate mortgages executed by Moonwalk in favor of SSS. But this foreclosure did not push through upon Moonwalk's requests and promises to pay in full. The next demand for payment happened on October 1, 1979 when SSS issued a Statement of Account to Moonwalk. And in accordance with said statement, Moonwalk paid its loan in full. What is clear, therefore, is that Moonwalk was never in default because SSS never compelled performance. Though it tried to foreclose the mortgages, SSS itself desisted from doing so upon the entreaties of Moonwalk. If the Statement of Account could properly be considered as demand for payment, the demand was complied with on time. Hence, no delay occurred and there

was, therefore, no occasion when the penalty became demandable and enforceable. Since there was no default in the performance of the main obligation -- payment of the loan -- SSS was never entitled to recover any penalty, not at the time it made the Statement of Account and certainly, not after the extinguishment of the principal obligation because then, all the more that SSS had no reason to ask for the penalties. Thus, there could never be any occasion for waiver or even mistake in the application for payment because there was nothing for SSS to waive as its right to enforce the penalty did not arise.

SSS, however, in buttressing its claim that it never waived the penalties, argued that the funds it held were trust funds and as trustee, the petitioner could not perform acts affecting the funds that would diminish property rights of the owners and beneficiaries thereof. To support its claim, SSS cited the case of *United Christian Missionary Society v. Social Security Commission*.^[14]

We looked into the case and found out that it is not applicable to the present case as it dealt not with the right of the SSS to collect penalties which were provided for in contracts which it entered into but with its right to collect premiums and its duty to collect the penalty for delayed payment or non-payment of premiums. The Supreme Court, in that case, stated:

"No discretion or alternative is granted respondent Commission in the enforcement of the law's mandate that the employer who fails to comply with his legal obligation to remit the premiums to the System within the prescribed period shall pay a penalty of three (3%) per month. The prescribed penalty is evidently of a punitive character, provided by the legislature to assure that employers do not take lightly the State's exercise of the police power in the implementation of the Republic's declared policy "to develop, establish gradually and perfect a social security system which shall be suitable to the needs of the people throughout the Philippines and (to) provide protection to employers against the hazards of disability, sickness, old age and death. x x x."

Thus, We agree with the decision of the respondent Court on the matter which We quote, to wit:

"Note that the above case refers to the condonation of the penalty for the non remittance of the premium which is provided for by Section 22(a) of the Social Security Act x x x. In other words, what was sought to be condoned was the penalty provided for by law for non remittance of premium for coverage under the Social Security Act.

The case at bar does not refer to any penalty provided for by law nor does it refer to the non remittance of premium. The case at bar refers to a contract of loan entered into between plaintiff and defendant Moonwalk Development and Housing Corporation. Note, therefore, that no provision of law is involved in this case, nor is there any penalty imposed by law nor a case about non-remittance of premium required by law. The present case refers to a contract of loan payable in installments not provided for by law but by agreement of the parties. Therefore, the ratio decidendi of the case of *United Christian Missionary Society vs. Social Security Commission* which plaintiff-appellant relies is not applicable in this case; clearly, the Social Security Commission, which is a creature of the Social Security Act cannot condone a mandatory provision of law providing for the payment of premiums and for penalties for non remittance. The life of the Social Security Act is in the premiums because these are the funds from which the Social Security Act gets the money for its purposes and the non-remittance of the premiums is penalized not by the Social Security Commission but by law.

x x x x x

It is admitted that when a government created corporation enters into a contract with private party concerning a loan, it descends to the level of a private person. Hence, the rules on contract applicable to private parties are applicable to it. The argument therefore that the Social Security Commission cannot waive or condone the penalties which was applied in the *United Christian Missionary Society* cannot apply this case. First, because what was not paid were installments on a loan but premiums required by law to be paid by the parties covered

by the Social Security Act. Secondly, what is sought to be condoned or waived are penalties not imposed by law for failure to remit premiums required by law, but a penalty for non payment provided for by the agreement of the parties in the contract between them. x x x"[15]

WHEREFORE, in view of the foregoing, the petition is DISMISSED and the decision of the respondent Court is AFFIRMED.

SO ORDERED.

Narvasa, C.J., (Chairman), Padilla, Regalado, and Nocon, JJ., concur.

[1] AC-G.R. CV No. 68692, "Social Security System vs. Moonwalk Development & Housing Corporation, et al.", penned by Associate Justice Eduardo P. Caguioa, Associate Justices Abdulwahid A. Bidin and Florelia C. Bartolome, concurring with dissenting opinion of Presiding Justice Ramon G. Gaviola, Jr. and Associate Justice Ma. Rosario Quetulio-Losa, concurring.

[2] Annex "A" of Petition, pp. 1-3; Rollo, pp. 44-46.

[3] Decision, p. 13; Rollo, p. 56.

[4] Petition, p. 12; Rollo, p. 27.

[5] Rollo, pp. 62-66.

[6] 4 TOLENTINO, CIVIL CODE OF THE PHILIPPINES 259 (1991 ed.).

[7] Ibid.

[8] 4 E.P. CAGUIOA, COMMENTS AND CASES ON CIVIL LAW 280 (1983 ed.).

[9] CIVIL CODE, Art. 1169.

[10] Annex "C" of the Petition, Record on Appeal, p. 10.

[11] Supra, note 6.

[12] Ibid.

[13] Ibid.

[14] 30 SCRA 982, 987 (1969).

[15] Supra, note 3, pp. 17-18.

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