

SECOND DIVISION

[G.R. No. 130886, January 29, 2004]

**COMMONWEALTH INSURANCE CORPORATION, PETITIONER, VS.
COURT OF APPEALS AND RIZAL COMMERCIAL BANKING
CORPORATION, RESPONDENTS.**

D E C I S I O N

AUSTRIA-MARTINEZ, J.:

Before us is a petition for review on certiorari assailing the Decision^[1] of the Court of Appeals (CA), promulgated on May 16, 1997 in CA-G.R. CV No. 44473^[2], which modified the decision dated March 5, 1993 of the Regional Trial Court of Makati (Branch 64); and the Resolution^[3] dated September 25, 1997, denying petitioner's motion for reconsideration.

The facts of the case as summarized by the Court of Appeals are as follows:

In 1984, plaintiff-appellant Rizal Commercial Banking Corporation (RCBC) granted two export loan lines, one, for P2,500,000.00 to Jigs Manufacturing Corporation (JIGS) and, the other, for P1,000,000.00 to Elba Industries, Inc. (ELBA). JIGS and ELBA which are sister corporations both drew from their respective credit lines, the former in the amount of P2,499,992.00 and the latter for P998,033.37 plus P478,985.05 from the case-to-case basis and trust receipts. These loans were evidenced by promissory notes (Exhibits 'A' to 'L', inclusive – JIGS; Exhibits 'V' to 'BB', inclusive – ELBA) and secured by surety bonds (Exhibits 'M' to 'Q' inclusive – JIGS; Exhibits 'CC' to 'FF', inclusive – ELBA) executed by defendant-appellee Commonwealth Insurance Company (CIC).

Specifically, the surety bonds issued by appellee CIC in favor of appellant RCBC to secure the obligations of JIGS totaled P2,894,128.00 while that securing ELBA's obligation was P1,570,000.00. Hence, the total face value of the surety bonds issued by appellee CIC was P4,464,128.00.

JIGS and ELBA defaulted in the payment of their respective loans. On October 30, 1984, appellant RCBC made a written demand (Exhibit 'N') on appellee CIC to pay JIG's account to the full extend (sic) of the suretyship. A similar demand (Exhibit 'O') was made on December 17, 1984 for appellee CIC to pay ELBA's account to the full extend (sic) of the suretyship. In response to those demands, appellee CIC made several payments from February 25, 1985 to February 10, 1988 in the total amount of P2,000,000.00. There having been a substantial balance unpaid, appellant RCBC made a final demand for payment (Exhibit 'P') on July 7, 1988 upon appellee CIC but the latter ignored it. Thus, appellant

RCBC filed the Complaint for a Sum of Money on September 19, 1988 against appellee CIC.^[4]

The trial court rendered a decision dated March 5, 1993, the dispositive portion of which reads as follows:

"WHEREFORE, premises considered, in the light of the above facts, arguments, discussion, and more important, the law and jurisprudence, the Court finds the defendants Commonwealth Insurance Co. and defaulted third party defendants Jigs Manufacturing Corporation, Elba Industries and Iluminada de Guzman solidarily liable to pay herein plaintiff Rizal Commercial Banking Corporation the sum of Two Million Four Hundred Sixty-Four Thousand One Hundred Twenty-Eight Pesos (P2,464,128.00), to pay the plaintiff attorney's fees of P10,000.00 and to pay the costs of suit.

"IT IS SO ORDERED."^[5]

Not satisfied with the trial court's decision, RCBC filed a motion for reconsideration praying that in addition to the principal sum of P2,464,128.00, defendant CIC be held liable to pay interests thereon from date of demand at the rate of 12% per annum until the same is fully paid. However, the trial court denied the motion.

RCBC then appealed to the Court of Appeals.

On May 16, 1997, the CA rendered the herein assailed decision, ruling thus:

. . .

Being solidarily bound, a surety's obligation is primary so that according to Art. 1216 of the Civil Code, he can be sued alone for the entire obligation. However, one very important characteristic of this contract is the fact that a surety's liability shall be limited to the amount of the bond (Sec. 176, Insurance Code). This does not mean however that even if he defaults in the performance of his obligation, the extend (sic) of his liability remains to be the amount of the bond. If he pays his obligation at maturity upon demand, then, he cannot be made to pay more than the amount of the bond. **But if he fails or refuses without justifiable cause to pay his obligation upon a valid demand so that he is in mora solvendi (Art. 1169, CC), then he must pay damages or interest in consequence thereof according to Art. 1170. Even if this interest is in excess of the amount of the bond, the defaulting surety is liable according to settled jurisprudence.**

. . .

Appellant RCBC contends that when appellee CIC failed to pay the obligation upon extrajudicial demand, it incurred in delay in consequence of which it became liable to pay legal interest. **The obligation to pay such interest does not arise from the contract of suretyship but from law as a result of delay or mora. Such an interest is not, therefore, covered by the limitation of appellee's liability expressed in the contract.** Appellee CIC refutes this argument stating

that since the surety bonds expressly state that its liability shall in no case exceed the amount stated therein, then that stipulation controls. Therefore, it cannot be made to assume an obligation more than what it secured to pay.

The contention of appellant RCBC is correct because it is supported by Arts. 1169 and 1170 of the Civil Code and the case of Asia Surety & Insurance Co., Inc. and Manila Surety & Fidelity Co. supra. On the other hand, the position of appellee CIC which upholds the appealed decision is untenable. The best way to show the untenability of this argument is to give this hypothetical case situation: Surety issued a bond for P1 million to secure a Debtor's obligation of P1 million to Creditor. Debtor defaults and Creditor demands payment from Surety. If the theory of appellee and the lower court is correct, then the Surety may just as well not pay and use the P1 million in the meantime. It can choose to pay only after several years – after all, his liability can never exceed P1 million. That would be absurd and the law could not have intended it.^[6] (Emphasis supplied)

and disposed of the case as follows:

WHEREFORE, the appealed Decision is MODIFIED in the manner following:

The appellee Commonwealth Insurance Company shall pay the appellant Rizal Commercial Banking Corporation:

1. On the account of JIGS, P2,894,128.00 ONLY with 12% legal interest per annum from October 30, 1984 minus payments made by the latter to the former after that date; and on the account of ELBA, P1,570,000.00 ONLY with 12% legal interest per annum from December 17, 1984 minus payments made by the latter to the former after that day; respecting in both accounts the applications of payment made by appellant RCBC on appellee CIC's payments;
2. Defendant-appellee Commonwealth Insurance Company shall pay plaintiff-appellant RIZAL COMMERCIAL BANKING CORP. and (sic) attorney's fee of P10,000.00 and cost of this suit;
3. The third-party defendants JIGS MANUFACTURING CORPORATION, ELBA INDUSTRIES and ILUMINADA N. DE GUZMAN shall respectively indemnify COMMONWEALTH INSURANCE CORPORATION for whatever it had paid and shall pay to RIZAL COMMERCIAL BANKING CORPORATION of their respective individual obligations pursuant to this decision.

SO ORDERED.^[7]

CIC filed a motion for reconsideration but the CA denied the same.

Hence, herein petition by CIC raising a single assignment of error, to wit:

Respondent Court of Appeals grievously erred in ordering petitioner to pay respondent RCBC the amount of the surety bonds plus legal interest of 12% per annum minus payments made by the petitioner.^[8]

The sole issue is whether or not petitioner should be held liable to pay legal interest over and above its principal obligation under the surety bonds issued by it.

Petitioner argues that it should not be made to pay interest because its issuance of the surety bonds was made on the condition that its liability shall in no case exceed the amount of the said bonds.

We are not persuaded. Petitioner's argument is misplaced.

Jurisprudence is clear on this matter. As early as *Tagawa vs. Aldanese and Union Gurantee Co.*^[9] and reiterated in *Plaridel Surety & Insurance Co., Inc. vs. P.L. Galang Machinery Co., Inc.*^[10], and more recently, in *Republic vs. Court of Appeals and R & B Surety and Insurance Company, Inc.*^[11], we have sustained the principle that if a surety upon demand fails to pay, he can be held liable for interest, even if in thus paying, its liability becomes more than the principal obligation. The increased liability is not because of the contract but because of the default and the necessity of judicial collection.^[12]

Petitioner's liability under the suretyship contract is different from its liability under the law. There is no question that as a surety, petitioner should not be made to pay more than its assumed obligation under the surety bonds.^[13] However, it is clear from the above-cited jurisprudence that petitioner's liability for the payment of interest is not by reason of the suretyship agreement itself but because of the delay in the payment of its obligation under the said agreement.

Petitioner admits having incurred in delay. Nonetheless, it insists that mere delay does not warrant the payment of interest. Citing Section 244 of the Insurance Code,^[14] petitioner submits that under the said provision of law, interest shall accrue only when the delay or refusal to pay is unreasonable; that the delay in the payment of its obligation is not unreasonable because such delay was brought about by negotiations being made with RCBC for the amicable settlement of the case.

We are not convinced.

It is not disputed that out of the principal sum of P4,464,128.00 petitioner was only able to pay P2,000,000.00. Letters demanding the payment of the respective obligations of JIGS and ELBA were initially sent by RCBC to petitioner on October 30, 1984^[15] and December 17, 1984.^[16] Petitioner made payments on an installment basis spanning a period of almost three years, i.e., from February 25, 1985 until February 10, 1988. On July 7, 1988, or after a period of almost five months from its last payment, RCBC, thru its legal counsel, sent a final letter of demand asking petitioner to pay the remaining balance of its obligation including interest.^[17] Petitioner failed to pay. As of the date of the filing of the complaint on September 19, 1988, petitioner was even unable to pay the remaining balance of P2,464,128.00 out of the principal amount it owes RCBC.