



Republic of the Philippines
Supreme Court
Manila

THIRD DIVISION

MONDRAGON
SALES, INC.,

PERSONAL

G.R. No. 174882

Petitioner,

Present:

- versus -

VELASCO, JR., *J.*, Chairperson,
PERALTA,
ABAD,
MENDOZA, and
LEONEN, *JJ.*

Promulgated:

VICTORIANO S. SOLA, JR.,
Respondent.

January 21, 2013

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DECISION

PERALTA, *J.*:

Before us is a petition for review on *certiorari* seeking to set aside the Decision¹ dated February 10, 2006 and the Resolution² dated September 6, 2006 issued by the Court of Appeals (CA) in CA-G.R. CV No. 71690.

Petitioner Mondragon Personal Sales Inc., a company engaged in the business of selling various consumer products through a network of sales representatives, entered into a Contract of Services³ with respondent Victoriano S. Sola, Jr. for a period of three years commencing on October 2, 1994 up to October 1, 1997. Under the said contract, respondent, as service contractor, would provide service facilities, *i.e.*, bodega cum office, to petitioner's products, sales force and customers in General Santos City and as such, he was entitled to a commission or service fee as follows:

¹ Penned by Associate Justice Myrna Dimaranan Vidal, with Associate Justices Romulo V. Borja and Ricardo R. Rosario concurring; *rollo*, pp. 23-35.

² Penned by Associate Justice Ricardo R. Rosario, with Associate Justices Romulo V. Borja and Sixto C. Marella, Jr. concurring; *rollo*, pp. 43-44.

³ *Id.* at 71-78.

MONTHLY SALES (net of vat)	SERVICE FEE
₱50,000.00 to 2,500,000.00	Five percent (5%)
₱2,500,001.00 to 3,000,000.00	₱125,000.00
₱3,000,001.00 to 3,500,000.00	150,000.00
₱3,500,001.00 – UP	200,000.00 ⁴

The agreement then came into effect when petitioner's goods were delivered to respondent's bodega and were sold by petitioner's employees. Prior to the execution of the contract, however, respondent's wife, Lina Sola, had an existing obligation with petitioner arising from her Franchise Distributorship Agreement with the latter. On January 26, 1995, respondent wrote a letter⁵ addressed to Renato G. de Leon, petitioner's Vice-President for Finance, wherein he acknowledged and confirmed his wife's indebtedness to petitioner in the amount of ₱1,973,154.73 (the other accountability in the sum of ₱1,490,091.15 was still subject to reconciliation) and, together with his wife, bound himself to pay on installment basis the said debt. Consequently, petitioner withheld the payment of respondent's service fees from February to April 1995 and applied the same as partial payments to the debt which he obligated to pay. On April 29, 1995, respondent closed and suspended operation of his office cum bodega where petitioner's products were stored and customers were being dealt with.

On May 24, 1995, respondent filed with the Regional Trial Court (RTC) of Davao, a Complaint⁶ for accounting and rescission against petitioner alleging that petitioner withheld portions of his service fees covering the months from October 1994 to January 1995 and his whole service fees for the succeeding months of February to April 1995, the total amount of which was ₱222,202.84; that petitioner's act grossly hampered, if not paralyzed, his business operation, thus left with no other recourse, he suspended operations to minimize losses. He prayed for the rescission of the contract of services and for petitioner to render an accounting of his service fees.

In its Answer with Counterclaim⁷ filed on June 14, 1995, petitioner contended that respondent's letter dated January 26, 1995 addressed to petitioner's Vice-President for Finance, confirmed and obligated himself to pay on installment basis the accountability of his wife with petitioner, thus respondent's service fees/commission earned for the period of February to April 1995 amounting to ₱125,040.01 was applied by way of compensation

⁴ *Id.* at 74.
⁵ *Id.* at 79.
⁶ *Id.* at 48-53; Docketed as Civil Case No. 23,625-95.
⁷ *Id.* at 54-65.

to the amounts owing to it; that all the service fees earned by respondent prior to February 1995 were fully paid to him. By way of counterclaim, petitioner asked for the payment of the amount of ₱1,547,892.55 which respondent obligated to pay plus interest; the delivery of petitioner's products padlocked in respondent's office cum bodega, the payment for the loss of income in the amount of ₱833,600.00 as well as the remaining balance of ₱45,728.30 from the ₱100,000.00 given by petitioner to respondent as advance money for the purchase of office equipment and the renovation of the bodega cum office.

In his Reply and Answer⁸ to petitioner's counterclaim, respondent averred that he was made to believe that the sales commission contained in petitioner's memorandum dated July 5, 1994 would be applicable to him; that it was improper for petitioner to confuse respondent's transaction with that of his wife as it was divergent in nature and terms.

Pending trial, petitioner moved for the issuance of a preliminary attachment and replevin which the RTC granted in its Order dated June 19, 1995 upon the filing of bonds.⁹ Respondent filed a Motion to Quash the Writ of Attachment, which the RTC denied in an Order dated July 24, 1995.¹⁰ As respondent's motion for reconsideration was also denied, he filed with us a petition for *certiorari*, docketed as G.R. No. 126427, assailing the RTC orders which we dismissed in a Resolution¹¹ dated November 11, 1996 on procedural matters.

Trial thereafter ensued.

On July 6, 2000, the RTC rendered its Decision,¹² the dispositive portion of which reads:

FOR THE FOREGOING, judgment is hereby rendered in favor of defendant and against plaintiff, ordering the latter to pay the former:

- 1) the sum of ₱1,543,643.96 representing the principal balance of plaintiff's account with defendant, plus legal interest from the time of filing of the complaint until fully paid, at the rate of 6% per annum;
- 2) attorney's fees in the amount of ₱25,000.00
- 3) costs of the suit.¹³

⁸ Records, pp. 34-35.

⁹ *Id.* at 42.

¹⁰ *Id.* at 85-88.

¹¹ *Id.* at 174-175.

¹² *Id.* at 262-274; Per Judge Salvador M. Ibarreta, Jr.

¹³ *Id.* at 273-274.

In so ruling, the RTC found that in computing the service fees/commissions due respondent, the rate as provided in the contract of service dated January 27, 1995 was controlling, since respondent was a party thereto duly affixing his signature therein; that petitioner's computation of respondent's service fees for the months of February to April 1995 in the total amount of ₱125,040.01 which was based on the said contract deserved credence. The RTC ruled that while Article 1381 of the Civil Code provides for the grounds for which a contract may be rescinded, none of these grounds existed in this case; that there was no showing of fraud which petitioner employed when it entered into the contract with respondent nor did respondent agree to such a contract without knowing its content, thus the contract was not rescissible.

As regards to petitioner's counterclaim that respondent confirmed and assumed the payment of his wife's account with petitioner, the RTC found that respondent obligated himself to pay his wife's account as evidenced by his letter dated January 26, 1995; that after deducting from the confirmed amount of ₱1,668,683.97 the respondent's service commission for the period from February 1995 to April 1995, which was in the total amount of ₱125,040.01, the amount owing to petitioner would still be ₱1,543,643.96. The RTC dismissed the other counterclaims, since they were not substantiated but found petitioner entitled to attorney's fees due to the amount of money involved and the time spent in pursuing the case.

Respondent filed his appeal to the CA to which petitioner filed its appellee's brief. On February 10, 2006, the CA rendered its assailed decision, the dispositive portion of which reads as follows:

WHEREFORE, in the light of the foregoing premises, herein appeal is **GRANTED**. Accordingly, the *Contract of Services* is hereby **RESCINDED**. Let the case be **REMANDED** to the court *a quo* for the proper determination of the amount of service fees unlawfully withheld from the appellant.

Furthermore, Appellee is hereby ordered to pay the Appellant attorney's fees in the amount of twenty-five thousand pesos (₱25,000.00).¹⁴

The CA found that under Article 1191 of the Civil Code, respondent was entitled to rescind the contract of services as it was petitioner who breached the same by withholding the service fees lawfully due to the former; that petitioner's act of unlawfully withholding the service fees due respondent constituted a willful and deliberate infringement on contractual obligations which would justify rescission under Article 1191. The CA declared that the contract of services entered into by the parties did not fall

¹⁴ *Rollo*, p. 34. (Emphasis in the original).

under any of the rescissible contracts enumerated under Article 1381 of the Civil Code but under Article 1191 which pertains to rescission of reciprocal obligations as in the instant case.

The CA ruled that respondent did not assume his wife's obligation as he did not substitute himself in the shoes of his wife regarding the payment of the latter's liability; that there can be no novation as novation was never presumed. Petitioner's act of withholding respondent's service fee and thereafter applying them to the obligation of his wife was unlawful, considering that respondent never assumed his wife's obligation with petitioner; that there could be no legal compensation, since it was respondent's wife who was principally indebted to petitioner owing from the franchise distributorship agreement she earlier entered into with petitioner; that granting the debt redounded to the benefit of the family and incurred with the consent of respondent, and the spouse, as joint administrators of the community property are solidarily liable with their separate properties for debts incurred, however, such liability is only subsidiary, when the community property is not sufficient to pay for all liabilities, however, in this case, there was no showing that the community property of the spouses was insufficient to pay the debt.

The CA ordered the deletion of attorney's fees as it was respondent who was entitled to such award, since he was compelled to litigate to protect his interest for the unjustified act of petitioner.

Petitioner's motion for reconsideration was denied in a Resolution dated September 6, 2006.

Hence, this petition where petitioner alleges that the CA erred:

1. In finding that petitioner breached its contract with respondent and that there is no compensation in accordance to Article 1279 of the Civil Code;
2. In finding that respondent did not assume the obligation of his wife;
3. In remanding the case to the court *a quo* for proper determination of service fee withheld when the same has been determined;
4. In obliterating the award of petitioner's counterclaim when respondent admitted his obligation to petitioner.¹⁵

The CA found that petitioner's act of withholding respondent's service fees and thereafter applying them as partial payment to the obligation of respondent's wife with petitioner was unlawful, considering that respondent never assumed his wife's obligation, thus, there can be no legal compensation under Article 1279 of the Civil Code.

¹⁵

Id. at 13.

We do not agree.

In his letter dated January 26, 1995 addressed to Mr. Renato G. De Leon, petitioner's Vice-President for Finance, respondent wrote, and which we quote in full:

Gentlemen:

This refers to the account of my wife, Lina (Beng) Sola, with Mondragon Personal Sales, Inc. in the amount of ₱3,463,173.88. Of this total amount, we are initially confirming the total amount of ₱1,973,154.73 as due from Lina (Beng) Sola, while the remaining balance of ₱1,490,091.15 will be subject to a reconciliation on or before February 5, 1995.

In recognition of Lina (Beng) Sola's account, we undertake to pay ₱100,000.00 on or before February 01, 1995 and the balance of ₱1,873,154.73 plus interest of 18% per annum and 2% administrative charge per month on the diminishing balance will be covered by postdated checks of not less than ₱100,000.00 per month starting February 28, 1995 and every end of the month thereafter but not to exceed eighteen (18) months or July 31, 1996.

With regards to the remaining balance of ₱1,490,019.15, we agree that upon final verification of these accounts, we will issue additional postdated checks subject to the same terms and conditions as stated above.

We further agree that all subsequent orders that will be released to us will be covered by postdated checks.

I fully understand and voluntarily agree to the above undertaking with full knowledge of the consequences which may arise therefrom.

Very truly yours,

(signed)
Victoriano S. Sola¹⁶

A reading of the letter shows that respondent becomes a co-debtor of his wife's accountabilities with petitioner. Notably, the last paragraph of his letter which states "I fully understand and voluntarily agree to the above undertaking with full knowledge of the consequences which may arise therefrom" and which was signed by respondent alone, shows that he solidarily bound himself to pay such debt. Based on the letter, respondent's wife had an account with petitioner in the amount of ₱3,463,173.88, out of which only the amount of ₱1,973,154.73 was confirmed while the remaining amount of ₱1,490,019.15 would still be subject to reconciliation. As respondent bound himself to pay the amount of ₱1,973,154.73, he becomes petitioner's principal debtor to such amount.

¹⁶

Id. at 79.

On the other hand, respondent, as petitioner's service contractor, was entitled to a payment of service fees as provided in their contract of services dated January 26, 1995. We note that respondent never refuted the amount of monthly sales recorded but only assailed in the RTC the rate of the service fees which he was entitled to. However, we find that there could be no other computation of the rate of the service fees other than what was provided in the contract of services dated January 26, 1995 signed by respondent and petitioner. Thus, we give credence to petitioner's computation of respondent's service fees for the months of February to April 1995 in the total amount of ₱125,040.01. Since respondent promised petitioner in his letter dated January 26, 1995, to monthly pay a certain amount to cover the indebtedness to petitioner which he failed to do, the latter withheld the payment of respondent's service fees and applied the same as partial payments of the debt by way of compensation.

We find that petitioner's act of withholding respondent's service fees/commissions and applying them to the latter's outstanding obligation with the former is merely an acknowledgment of the legal compensation that occurred by operation of law between the parties.¹⁷ Compensation is a mode of extinguishing to the concurrent amount the obligations of persons who in their own right and as principals are reciprocally debtors and creditors of each other. Legal compensation takes place by operation of law when all the requisites are present, as opposed to conventional compensation which takes place when the parties agree to compensate their mutual obligations even in the absence of some requisites.¹⁸ Legal compensation requires the concurrence of the following conditions:

- (1) That each one of the obligors be bound principally, and that he be at the same time a principal creditor of the other;
- (2) That both debts consist in a sum of money, or if the things due are consumable, they be of the same kind, and also of the same quality if the latter has been stated;
- (3) That the two debts be due;
- (4) That they be liquidated and demandable;
- (5) That over neither of them there be any retention or controversy, commenced by third persons and communicated in due time to the debtor.¹⁹

We find the presence of all the requisites for legal compensation. Petitioner and respondent are both principal obligors and creditors of each other. Their debts to each other consist in a sum of money. Respondent acknowledged and bound himself to pay petitioner the amount of ₱1,973,154.73 which was already due, while the service fees owing to

¹⁷ See *Bank of the Philippine Islands v. Court of Appeals*, G.R. No. 142731, June 8, 2006, 490 SCRA 168, 178; 523 Phil. 548, 560 (2006).

¹⁸ *Id.*

¹⁹ Civil Code, Art. 1279.

respondent by petitioner become due every month. Respondent's debt is liquidated and demandable, and petitioner's payments of service fees are liquidated and demandable every month as they fall due. Finally, there is no retention or controversy commenced by third persons over either of the debts. Thus, compensation is proper up to the concurrent amount where petitioner owes respondent ₱125,040.01 for service fees, while respondent owes petitioner ₱1,973,154.73.

As legal compensation took place in this case, there is no basis for respondent to ask for rescission since he was the first to breach their contract when, on April 29, 1995, he suddenly closed and padlocked his bodega cum office in General Santos City occupied by petitioner.

Petitioner claims that the CA erred in obliterating the RTC's award of its counterclaim which it had alleged and proved during trial and which respondent even admitted.

We agree.

In his letter dated January 6, 1995, respondent confirmed the amount of ₱1,973,154.73 owing to petitioner. On September 29, 1997, petitioner wrote another letter²⁰ to petitioner's Credit and Collection Manager, Rudy Machanco, wherein he again confirmed the indebtedness in the amount of ₱1,973,154.73. In the same letter, he showed the payments he had already made and after deducting the same from the confirmed indebtedness, the total balance remained to be at ₱1,668,683.97. As we have said earlier, respondent's service fees from February to April 1995 which was in the total amount of ₱125,040.01 was not assailed at all by respondent in his appeal with the CA, thus he is bound by such computation. Hence, the amount of ₱125,040.01 which petitioner owes respondent shall be offset against the ₱1,973,154.73 which respondent owes petitioner, and therefore leaving a balance of ₱1,543,643.96 which respondent must pay.

WHEREFORE, the petition for review is **GRANTED**. The Decision dated February 10, 2006 and the Resolution dated September 6, 2006 of the Court of Appeals are hereby **REVERSED** and **SET ASIDE**. Respondent is hereby ordered to pay petitioner the amount of ₱1,543,643.96 with 6% percent per annum from June 14, 1995 until finality of this Decision and 12% percent per annum thereafter until full payment.

²⁰


Rollo, p. 81.

SO ORDERED.




DIOSDADO M. PERALTA
Associate Justice


WE CONCUR:



PRESBITERO J. VELASCO, JR.
Associate Justice
Chairperson



ROBERTO A. ABAD
Associate Justice




JOSE CARRAL MENDOZA
Associate Justice



MARVIC MARIO VICTOR F. LEONEN
Associate Justice

ATTESTATION


I attest that the conclusions in the above Decision had been reached in consultation before the case was assigned to the writer of the opinion of the Court's Division.



PRESBITERO J. VELASCO, JR.
Associate Justice
Chairperson, Third Division

CERTIFICATION

Pursuant to Section 13, Article VIII of the Constitution and the Division Chairperson's Attestation, I certify that the conclusions in the above Decision had been reached in consultation before the case was assigned to the writer of the opinion of the Court's Division.



MARIA LOURDES P. A. SERENO
Chief Justice