



Republic of the Philippines  
**Supreme Court**  
 Manila

SECOND DIVISION

**HEIRS OF MANUEL UY EK  
 LIONG, represented by BELEN  
 LIM VDA. DE UY,**  
**Petitioners,**

**G.R. No. 176425**

Present:

BRION,\* J.,  
 Acting Chairperson,  
 DEL CASTILLO,  
 PEREZ,  
 PERLAS-BERNABE, and  
 LEONEN,\*\* JJ.

- versus -

**MAURICIA MEER CASTILLO,  
 HEIRS OF BUENAFLORE C.  
 UMALI, represented by NANCY  
 UMALI, VICTORIA H.  
 CASTILLO, BERTILLA C.  
 RADA, MARIETTA C.  
 CAVANEZ, LEOVINA C.  
 JALBUENA and PHILIP M.  
 CASTILLO,**

**Respondents.**

Promulgated:

JUN 05 2013

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DECISION

**PEREZ, J.:**

Assailed in this Petition for Review on *Certiorari* filed pursuant to Rule 45 of the *Rules of Court* is the Decision<sup>1</sup> dated 23 January 2007

\* As per Special Order No. 1460 dated 29 March 2013.

\*\* As per Special Order No. 1461 dated 29 March 2013.

<sup>1</sup> Penned by Court of Appeals Associate Justice Vicente Q. Roxas and concurred in by Associate Justices Josefina Guevara-Salonga and Ramon R. Garcia; CA rollo, pp. 153-169.

rendered by the Fifteenth Division of the Court of Appeals in CA-G.R. CV No. 84687,<sup>2</sup> the dispositive portion of which states:

WHEREFORE, premises considered, the assailed January 27, 2005 Decision of the Regional Trial Court of Lucena City, Branch 59, in Civil Case No. 93-176, is hereby REVERSED and SET ASIDE and a new one entered declaring the AGREEMENT and the KASUNDUAN *void ab initio* for being contrary to law and public policy, without prejudice to the attorney's filing a proper action for collection of reasonable attorney's fees based on *quantum meruit* and without prejudice also to administrative charges being filed against counsel for counsel's openly entering into such an illegal AGREEMENT in violation of the Canons of Professional Responsibility which action may be instituted with the Supreme Court which has exclusive jurisdiction to impose such penalties on members of the bar.

No pronouncement as to costs.

SO ORDERED.<sup>3</sup> (*Italics and Underscore Ours*)

### ***The Facts***

Alongside her husband, ***Felipe*** Castillo, ***respondent*** ***Mauricia*** Meer Castillo was the owner of four parcels of land with an aggregate area of 53,307 square meters, situated in Silangan Mayao, Lucena City and registered in their names under Transfer Certificate of Title (***TCT***) Nos. T-42104, T-32227, T-31752 and T-42103. With the death of Felipe, a deed of extrajudicial partition over his estate was executed by his heirs, namely, ***Mauricia***, ***Buenaflor*** Umali and ***respondents*** ***Victoria*** Castillo, ***Bertilla*** Rada, ***Marietta*** Cavanez, ***Leovina*** Jalbuena and ***Philip*** Castillo. Utilized as security for the payment of a tractor purchased by ***Mauricia***'s nephew, ***Santiago*** Rivera, from ***Bormaheco***, Inc., it appears, however, that the subject properties were subsequently sold at a public auction where Insurance Corporation of the Philippines (***ICP***) tendered the highest bid. Having consolidated its title, ICP likewise sold said parcels in favor of Philippine Machinery Parts Manufacturing Co., Inc. (***PMPMCI***) which, in turn, caused the same to be titled in its name.<sup>4</sup>

On 29 September 1976, respondents and Buenaflor instituted Civil Case No. 8085 before the then Court of First Instance (***CFI***) of Quezon, for the purpose of seeking the annulment of the transactions and/or proceedings

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<sup>2</sup> Id.

<sup>3</sup> Id. at 168.

<sup>4</sup> *Umali v. Court of Appeals*, G.R. No. 89561, 13 September 1990, 189 SCRA 529.

involving the subject parcels, as well as the TCTs procured by PMPMCI.<sup>5</sup> Encountering financial difficulties in the prosecution of Civil Case No. 8085, respondents and Buenaflor entered into an *Agreement* dated 20 September 1978 whereby they procured the legal services of *Atty.* Edmundo *Zepeda* and the assistance of *Manuel* Uy Ek Liong who, as financier, agreed to underwrite the litigation expenses entailed by the case. In exchange, it was stipulated in the notarized Agreement that, in the event of a favorable decision in Civil Case No. 8085, *Atty.* Zepeda and Manuel would be entitled to “a share of forty (40%) percent of all the realties and/or monetary benefits, gratuities or damages” which may be adjudicated in favor of respondents.<sup>6</sup>

On the same date, respondents and Buenaflor entered into another notarized agreement denominated as a *Kasunduan* whereby they agreed to sell their remaining sixty (60%) percent share in the subject parcels in favor of Manuel for the sum of ₱180,000.00. The parties stipulated that Manuel would pay a downpayment in the sum of ₱1,000.00 upon the execution of the *Kasunduan* and that respondents and Buenaflor would retain and remain the owners of a 1,750-square meter portion of said real properties. It was likewise agreed that any party violating the *Kasunduan* would pay the aggrieved party a penalty fixed in the sum of ₱50,000.00, together with the attorney’s fees and litigation expenses incurred should a case be subsequently filed in court. The parties likewise agreed to further enter into such other stipulations as would be necessary to ensure that the sale would push through and/or in the event of illegality or impossibility of any part of the *Kasunduan*.<sup>7</sup>

With his death on 19 August 1989,<sup>8</sup> Manuel was survived by *petitioners*, Heirs of Manuel Uy Ek Liong, who were later represented in the negotiations regarding the subject parcels and in this suit by *petitioner Belen* Lim Vda. de Uy. The record also shows that the proceedings in Civil Case No. 8085 culminated in this Court’s rendition of a 13 September 1990 Decision in G.R. No. 89561<sup>9</sup> in favor of respondents and Buenaflor.<sup>10</sup>

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<sup>5</sup> Id.

<sup>6</sup> Exhibit “A,” folder of Exhibits, records, pp. 306-308

<sup>7</sup> Exhibit “B,” id. at 310-312.

<sup>8</sup> Exhibit “K,” id. at 323.

<sup>9</sup> Exhibit “L” and submarkings, id. at 324-348.

<sup>10</sup> WHEREFORE, the decision of respondent Court of Appeals is hereby REVERSED and SET ASIDE, and judgment is hereby rendered declaring the following as null and void: (1) Certificate of Sale, dated September 28, 1973, executed by the Provincial Sheriff of Quezon in favor of the Insurance Corporation of the Philippines; (2) Transfer Certificates of Title Nos. T-23705, T-23706, T-23707 and T-23708 issued in the name of the Insurance Corporation of the Philippines; (3) the sale of Insurance Corporation of the Philippines in favor of Philippine Machinery Parts Manufacturing Co., Inc. of the four (4) parcels of land covered by the aforesaid certificates of title;

Subsequent to the finality of the Court's Decision,<sup>11</sup> it appears that the subject parcels were subdivided in accordance with the Agreement, with sixty (60%) percent thereof consisting of 31,983 square meters equally apportioned among and registered in the names of respondents and Buenaflor under TCT Nos. T-72027, T-72028, T-72029, T-72030, T-72031, T-72032 and T-72033.<sup>12</sup> Consisting of 21,324 square meters, the remaining forty (40%) percent was, in turn, registered in the names of petitioners and Atty. Zepeda under TCT No. T-72026.<sup>13</sup>

Supposedly acting on the advice of Atty. Zepeda, respondents wrote petitioners a letter dated 22 March 1993, essentially informing petitioners that respondents were willing to sell their sixty (60%) percent share in the subject parcels for the consideration of ₱500.00 per square meter.<sup>14</sup> Insisting on the price agreed upon in the *Kasunduan*, however, petitioners sent a letter dated 19 May 1993, requesting respondents to execute within 15 days from notice the necessary Deed of Absolute Sale over their 60% share as aforesaid, excluding the 1,750-square meter portion specified in their agreement with Manuel. Informed that petitioners were ready to pay the remaining ₱179,000.00 balance of the agreed price,<sup>15</sup> respondents wrote a 28 May 1993 reply, reminding the former of their purported refusal of earlier offers to sell the shares of Leovina and of Buenaflor who had, in the meantime, died.<sup>16</sup> In a letter dated 1 June 1993, respondents also called petitioners' attention to the fact, among others, that their right to ask for an additional consideration for the sale was recognized under the *Kasunduan*.<sup>17</sup>

On 6 October 1993, petitioners commenced the instant suit with the filing of their complaint for specific performance and damages against the respondents and *respondent* Heirs of Buenaflor, as then represented by **Menardo** Umali. Faulting respondents with unjustified refusal to comply with their obligation under the *Kasunduan*, petitioners prayed that the former be ordered to execute the necessary Deed of Absolute Sale over their shares

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and (4) Transfer Certificates of Title Nos. T-24846, T-24847, T-24848 and T-24849 subsequently issued by virtue of said sale in the name of the latter corporation.

The Register of Deeds of Lucena City is hereby directed to cancel Transfer Certificates of Title Nos. T-24846, T-24847, T-24848 and T-24849 in the name of Philippine Machinery Parts Manufacturing Co., Inc. and to issue in lieu thereof the corresponding transfer certificates of title in the name of herein petitioners, except Santiago Rivera.

The foregoing dispositions are without prejudice to such other proper legal remedies as may be available to respondent Bormaheco, Inc. against herein petitioners.

SO ORDERED. Id. at 346-347.

<sup>11</sup> Exhibit "L-25," records, pp. 349-350.

<sup>12</sup> Exhibits "C" to "I," id. at 313-320.

<sup>13</sup> Exhibit "J," id. at 321-322.

<sup>14</sup> Exhibit "S" and submarkings, id. at 465-466.

<sup>15</sup> Exhibit "M," id. at 354.

<sup>16</sup> Exhibit "T" and submarkings, id. at 468.

<sup>17</sup> Exhibit "N" and submarkings, id. at 355-356.

in the subject parcels, with indemnities for moral and exemplary damages, as well as attorney's fees, litigation expenses and the costs of the suit.<sup>18</sup> Served with summons, respondents filed their Answer with Counterclaim and Motion to File Third Party Complaint on 3 December 1993. Maintaining that the Agreement and the *Kasunduan* were illegal for being unconscionable and contrary to public policy, respondents averred that Atty. Zepeda was an indispensable party to the case. Together with the dismissal of the complaint and the annulment of said contracts and TCT No. T-72026, respondents sought the grant of their counterclaims for moral and exemplary damages, as well as attorney's fees and litigation expenses.<sup>19</sup>

The issues thereby joined, the Regional Trial Court (**RTC**), Branch 54, Lucena City, proceeded to conduct the mandatory preliminary conference in the case.<sup>20</sup> After initially granting respondents' motion to file a third party complaint against Atty. Zepeda,<sup>21</sup> the RTC, upon petitioners' motion for reconsideration,<sup>22</sup> went on to issue the 18 July 1997 Order disallowing the filing of said pleading on the ground that the validity of the Agreement and the cause of action against Atty. Zepeda, whose whereabouts were then unknown, would be better threshed out in a separate action.<sup>23</sup> The denial<sup>24</sup> of their motion for reconsideration of the foregoing order<sup>25</sup> prompted respondents to file a notice of appeal<sup>26</sup> which was, however, denied due course by the RTC on the ground that the orders sought to be appealed were non-appealable.<sup>27</sup> On 14 December 1997, Menardo died<sup>28</sup> and was substituted by his daughter Nancy as representative of respondent Heirs of Buenaflor.<sup>29</sup>

In the ensuing trial of the case on the merits, petitioners called to the witness stand Samuel Lim Uy Ek Liong<sup>30</sup> whose testimony was refuted by Philip<sup>31</sup> and Leovina<sup>32</sup> during the presentation of the defense evidence. On 27 January 2005, the RTC rendered a decision finding the *Kasunduan* valid and binding between respondents and petitioners who had the right to demand its fulfillment as Manuel's successors-in-interest. Brushing aside

<sup>18</sup> Petitioners' 5 October 1993 Complaint, id. at 1-5.

<sup>19</sup> Respondents' 29 November 1993 Answer, id. at 37-43.

<sup>20</sup> RTC's 10 January 1994 Order, id. at 74.

<sup>21</sup> RTC's 5 April 1994 Order, id. at 93.

<sup>22</sup> Petitioners' 18 April 1994 Motion for Reconsideration, id. at 100-101.

<sup>23</sup> RTC's 18 July 1997 Order, id. at 151-153.

<sup>24</sup> RTC's 20 August 1997 Order, id. at 157.

<sup>25</sup> RTC's 6 August 1997 Order, id. at 154-156.

<sup>26</sup> Respondents' 27 August 1997 Notice of Appeal, id. at 158-160.

<sup>27</sup> RTC's 1 October 1998 Order, id. at 197-198.

<sup>28</sup> Respondents' 19 December 1998 Notice of Death of a Party, id. at 209-210.

<sup>29</sup> RTC's 18 March 1999 Order, id. at 223.

<sup>30</sup> TSNs, 22 October 2001, 16 January 2002, 5 March 2002.

<sup>31</sup> TSNs, 19 November 2002, 19 February 2003, 21 July 2003, 18 August 2003, 20 October 2003.

<sup>32</sup> TSNs, 1 December 2003, 1 March 2004, 26 April 2004.

Philip's testimony that respondents were forced to sign the *Kasunduan*, the RTC ruled that said contract became effective upon the finality of this Court's 13 September 1990 Decision in G.R. No. 89561 which served as a suspensive condition therefor. Having benefited from the legal services rendered by Atty. Zepeda and the financial assistance extended by Manuel, respondents were also declared estopped from questioning the validity of the Agreement, *Kasunduan* and TCT No. T-72026. With the *Kasunduan* upheld as the law between the contracting parties and their privies,<sup>33</sup> the RTC disposed of the case in the following wise:

WHEREFORE, premises considered, the Court finds for the [petitioners] and hereby:

1. Orders the [respondents] to execute and deliver a Deed of Conveyance in favor of the [petitioners] covering the 60% of the properties formerly covered by Transfer Certificates of Title Nos. T-3175, 42104, T-42103, T-32227 and T-42104 which are now covered by Transfer Certificates of Title Nos. T-72027, T-72028, T-72029, T-72030, T-72031, T-72032, T-72033 and T-72026, all of the Registry of Deeds of Lucena City, for and in consideration of the amount of ₱180,000.00 in accordance with the provisions of the *KASUNDUAN*, and

2. Orders the [petitioners] to pay and deliver to the [respondents] upon the latter's execution of the Deed of Conveyance mentioned in the preceding paragraph, the amount of ₱179,000.00 representing the balance of the purchase price as provided in the *KASUNDUAN*, and

3. Orders the [respondents] to pay the [petitioners] the following amounts:

- a). ₱50,000.00 as and for moral damages;
- b). ₱50,000.00 as and for exemplary damages; and
- c). ₱50,000.00 as and for attorney's fees.

and to pay the costs.

SO ORDERED.<sup>34</sup>

Dissatisfied with the RTC's decision, both petitioners<sup>35</sup> and respondents perfected their appeals<sup>36</sup> which were docketed before the CA as CA-G.R. CV No. 84687. While petitioners prayed for the increase of the monetary awards adjudicated *a quo*, as well as the further grant of liquidated damages in their favor,<sup>37</sup> respondents sought the complete reversal of the

<sup>33</sup> Records, pp. 522-531.

<sup>34</sup> Id. at 530-531.

<sup>35</sup> Respondents' 10 February 2005 Notice of Appeal, id. at 532.

<sup>36</sup> Petitioners' 3 February 2005 Notice of Appeal, id. at 533.

<sup>37</sup> Petitioners' 5 July 2005 Apellants' Brief, CA *rollo*, pp. 56-80.

appealed decision on the ground that the Agreement and the *Kasunduan* were null and void.<sup>38</sup> On 23 January 2007, the CA rendered the herein assailed decision, setting aside the RTC's decision, upon the following findings and conclusions, to wit: (a) the Agreement and *Kasunduan* are byproducts of the partnership between Atty. Zepeda and Manuel who, as a non-lawyer, was not authorized to practice law; (b) the *Agreement* is void under Article 1491 (5) of the *Civil Code of the Philippines* which prohibits lawyers from acquiring properties which are the objects of the litigation in which they have taken part; (c) jointly designed to completely deprive respondents of the subject parcels, the Agreement and the *Kasunduan* are invalid and unconscionable; and (d) without prejudice to his liability for violation of the Canons of Professional Responsibility, Atty. Zepeda can file an action to collect attorney's fees based on *quantum meruit*.<sup>39</sup>

### *The Issue*

Petitioners seek the reversal of the CA's decision on the following issue:

**WHETHER [OR NOT] THE HONORABLE COURT OF APPEALS, FIFTEENTH DIVISION, COMMITTED A REVERSIBLE ERROR WHEN IT REVERSED AND SET ASIDE THE DECISION OF THE RTC BRANCH 59, LUCENA CITY, IN CIVIL CASE NO. 93-176 DECLARING THE AGREEMENT AND KASUNDUAN VOID AB INITIO FOR BEING CONTRARY TO LAW AND PUBLIC POLICY FOR BEING VIOLATIVE OF ART. 1491 OF THE NEW CIVIL CODE AND THE CANONS OF PROFESSIONAL RESPONSIBILITY.**<sup>40</sup>

### *The Court's Ruling*

We find the petition impressed with partial merit.

At the outset, it bears pointing out that the complaint for specific performance filed before the RTC sought only the enforcement of petitioners' rights and respondents' obligation under the *Kasunduan*. Although the answer filed by respondents also assailed the validity of the Agreement and TCT No. T-72026, the record shows that the RTC, in its order dated 18 July 1997, disallowed the filing of a third-party complaint

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<sup>38</sup> Respondents' 29 July 2005 Appellants' Brief id. at 93-122.

<sup>39</sup> CA's 23 January 2007 Decision, id. at 153-169.

<sup>40</sup> *Rollo*, p. 27.

against Atty. Zepeda on the ground that the causes of action in respect to said contract and title would be better threshed out in a separate action. As Atty. Zepeda's whereabouts were then unknown, the RTC also ruled that, far from contributing to the expeditious settlement of the case, the grant of respondents' motion to file a third-party complaint would only delay the proceedings in the case.<sup>41</sup> With the 1 October 1998 denial of their motion for reconsideration of the foregoing order, respondents subsequently filed a notice of appeal which was, however, denied due course on the ground that the orders denying their motion to file a third-party complaint and their motion for reconsideration were interlocutory and non-appealable.<sup>42</sup>

Absent a showing that the RTC's ruling on the foregoing issues was reversed and set aside, we find that the CA reversibly erred in ruling on the validity of the Agreement which respondents executed not only with petitioners' predecessor-in-interest, Manuel, but also with Atty. Zepeda. Since it is generally accepted that no man shall be affected by any proceeding to which he is a stranger,<sup>43</sup> the rule is settled that a court must first acquire jurisdiction over a party – either through valid service of summons or voluntary appearance – for the latter to be bound by a court decision.<sup>44</sup> The fact that Atty. Zepeda was not properly impleaded in the suit and given a chance to present his side of the controversy before the RTC should have dissuaded the CA from invalidating the Agreement and holding that attorney's fees should, instead, be computed on a *quantum meruit* basis. Admittedly, Article 1491 (5)<sup>45</sup> of the *Civil Code* prohibits lawyers from acquiring by purchase or assignment the property or rights involved which are the object of the litigation in which they intervene by virtue of their profession. The CA lost sight of the fact, however, that the prohibition applies only during the pendency of the suit<sup>46</sup> and generally does not cover contracts for contingent fees where the transfer takes effect only after the finality of a favorable judgment.<sup>47</sup>

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<sup>41</sup> Records, pp. 151-153.

<sup>42</sup> Id. at 197-198.

<sup>43</sup> *Orquiola v. Court of Appeals*, 435 Phil. 323, 332 (2002).

<sup>44</sup> *Padilla v. Court of Appeals*, 421 Phil. 883, 893 (2001).

<sup>45</sup> Art. 1491. The following persons cannot acquire by purchase, even at public or judicial auction, either in person or thru the mediation of another:

x x x x

(5) Justices, judges, prosecuting attorneys, clerks of superior and inferior courts, and other officers and employees connected with the administration of justice, the property and rights in litigation or levied upon an execution before the court within whose jurisdiction or territory they exercise their respective functions; this prohibition includes the act of acquiring by assignment and *shall apply to lawyers, with respect to the property and rights which may be the object of any litigation in which they may take part by virtue of their profession.*

<sup>46</sup> *Ramos v. Atty. Ngaseo*, 487 Phil. 40, 47 (2004).

<sup>47</sup> *Biascan v. Atty. Lopez*, 456 Phil. 173, 180 (2003).

Although executed on the same day, it cannot likewise be gainsaid that the Agreement and the *Kasunduan* are independent contracts, with parties, objects and causes different from that of the other. Defined as a meeting of the minds between two persons whereby one binds himself, with respect to the other to give something or to render some service,<sup>48</sup> a contract requires the concurrence of the following requisites: (a) consent of the contracting parties; (b) object certain which is the subject matter of the contract; and, (c) cause of the obligation which is established.<sup>49</sup> Executed in exchange for the legal services of Atty. Zepeda and the financial assistance to be extended by Manuel, the Agreement concerned respondents' transfer of 40% of the avails of the suit, in the event of a favorable judgment in Civil Case No. 8085. While concededly subject to the same suspensive condition, the *Kasunduan* was, in contrast, concluded by respondents with Manuel alone, for the purpose of selling in favor of the latter 60% of their share in the subject parcels for the agreed price of ₱180,000.00. Given these clear distinctions, petitioners correctly argue that the CA reversibly erred in not determining the validity of the *Kasunduan* independent from that of the Agreement.

Viewed in the light of the autonomous nature of contracts enunciated under Article 1306<sup>50</sup> of the *Civil Code*, on the other hand, we find that the *Kasunduan* was correctly found by the RTC to be a valid and binding contract between the parties. Already partially executed with respondents' receipt of ₱1,000.00 from Manuel upon the execution thereof, the *Kasunduan* simply concerned the sale of the former's 60% share in the subject parcel, less the 1,750-square meter portion to be retained, for the agreed consideration of ₱180,000.00. As a notarized document that carries the evidentiary weight conferred upon it with respect to its due execution,<sup>51</sup> the *Kasunduan* was shown to have been signed by respondents with full knowledge of its contents, as may be gleaned from the testimonies elicited from Philip<sup>52</sup> and Leovina.<sup>53</sup>

Although Philip had repeatedly claimed that respondents had been forced to sign the Agreement and the *Kasunduan*, his testimony does not show such vitiation of consent as would warrant the avoidance of the contract. He simply meant that respondents felt constrained to accede to the

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<sup>48</sup> *Perez v. Court of Appeals*, 380 Phil. 592, 598 (2000).

<sup>49</sup> *Jardine Davies, Inc. v. Court of Appeals*, 389 Phil. 204, 211 (2000).

<sup>50</sup> Art. 1306. The contracting parties may establish such stipulations, clauses, terms and conditions as they may deem convenient, provided they are not contrary to law, morals, good customs, public order, or public policy.

<sup>51</sup> *Potenciano v. Reynoso*, 449 Phil. 396, 406 (2003).

<sup>52</sup> TSN, 21 July 2003, pp. 4-18.

<sup>53</sup> TSN, 1 December 2003, pp. 8-16.

stipulations insisted upon by Atty. Zepeda and Manuel who were not otherwise willing to push through with said contracts.<sup>54</sup>

At any rate, our perusal of the record shows that respondents' main objection to the enforcement of the *Kasunduan* was the perceived inadequacy of the ₱180,000.00 which the parties had fixed as consideration for 60% of the subject parcels. Rather than claiming vitiation of their consent in the answer they filed *a quo*, respondents, in fact, distinctly averred that the *Kasunduan* was tantamount to unjust enrichment and "a clear source of speculative profit" at their expense since their remaining share in said properties had "a current market value of ₱9,594,900.00, more or less."<sup>55</sup> In their 22 March 1993 letter to petitioners, respondents also cited prices then prevailing for the sale of properties in the area and offered to sell their 60% share for the price of ₱500.00 per square meter<sup>56</sup> or a total of ₱15,991,500.00. In response to petitioners' insistence on the price originally agreed upon by the parties,<sup>57</sup> respondents even invoked the last paragraph<sup>58</sup> of the *Kasunduan* to the effect that the parties agreed to enter into such other stipulations as would be necessary to ensure the fruition of the sale.<sup>59</sup>

In the absence of any showing, however, that the parties were able to agree on new stipulations that would modify their agreement, we find that petitioners and respondents are bound by the original terms embodied in the *Kasunduan*. Obligations arising from contracts, after all, have the force of law between the contracting parties<sup>60</sup> who are expected to abide in good faith with their contractual commitments, not weasel out of them.<sup>61</sup> Moreover, when the terms of the contract are clear and leave no doubt as to the intention of the contracting parties, the rule is settled that the literal meaning of its stipulations should govern. In such cases, courts have no authority to alter a contract by construction or to make a new contract for the parties. Since their duty is confined to the interpretation of the one which the parties have made for themselves without regard to its wisdom or folly, it has been ruled that courts cannot supply material stipulations or read into the contract

<sup>54</sup> TSN, 21 July 2003, pp. 6-9.

<sup>55</sup> Records, p. 40.

<sup>56</sup> Folder of Exhibits, Exhibit "S," *id.* at 465-466.

<sup>57</sup> Exhibit "M," *id.* at 354.

<sup>58</sup> Na may laya ang bawa't panig sa kasulatang ito na magkaisa at magkasundo na madagdagan ang alinmang tuntunin na mababasa sa itaas nito upang ang kanilang kasunduan ukol sa pagbibilhang ito ay matupad at maganap, gayundin, sakaling ang alinmang tuntunin sa Kasunduang ito ay hindi masusunod sa dahilang labag sa batas o dili kaya ay hindi masusunod dahil sa pangyayaring hindi inaasahan at wala sa kapangyarihan ng bawa't panig dito, ay hindi sapat na dahilan upang mawalan ng bisa ang Kasunduang ito, kaya't ang magkabilang panig ay may laya na gumawa ng dagdag na tuntunin upang ang naulit na kasunduan ay matuloy at matupad. Exhibit "B-1," *id.* at 311.

<sup>59</sup> Exhibit "N," *id.* at 355-357.

<sup>60</sup> *Sarmiento v. Sps. Sun-Cabrido*, 449 Phil. 108, 115 (2003).

<sup>61</sup> *Metropolitan Manila Devt. Authority v. Jancom Environmental Corp.*, 425 Phil. 961, 981 (2002).

words it does not contain.<sup>62</sup> Indeed, courts will not relieve a party from the adverse effects of an unwise or unfavorable contract freely entered into.<sup>63</sup>

Our perusal of the *Kasunduan* also shows that it contains a penal clause<sup>64</sup> which provides that a party who violates any of its provisions shall be liable to pay the aggrieved party a penalty fixed at ₱50,000.00, together with the attorney's fees and litigation expenses incurred by the latter should judicial resolution of the matter becomes necessary.<sup>65</sup> An accessory undertaking to assume greater liability on the part of the obligor in case of breach of an obligation, the foregoing stipulation is a penal clause which serves to strengthen the coercive force of the obligation and provides for liquidated damages for such breach.<sup>66</sup> "The obligor would then be bound to pay the stipulated indemnity without the necessity of proof of the existence and the measure of damages caused by the breach."<sup>67</sup> Articles 1226 and 1227 of the *Civil Code* state:

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.

Art. 1227. The debtor cannot exempt himself from the performance of the obligation by paying the penalty, save in the case where this right has been expressly reserved for him. Neither can the creditor demand the fulfilment of the obligation and the satisfaction of the penalty at the same time, unless this right has been clearly granted to him. However, if after the creditor has decided to require the fulfilment of the obligation, the performance thereof should become impossible without his fault, the penalty may be enforced.

In the absence of a showing that they expressly reserved the right to pay the penalty in lieu of the performance of their obligation under the *Kasunduan*, respondents were correctly ordered by the RTC to execute and deliver a deed of conveyance over their 60% share in the subject parcels in

<sup>62</sup> *Sps. Barrera v. Sps. Lorenzo*, 438 Phil. 42, 49 (2002).

<sup>63</sup> *William Golangco Construction Corp. v. PCIB*, 520 Phil. 167, 172 (2006).

<sup>64</sup> Ang kasulatang ito ay isinagawa ng kusang loob ng bawa't panig dala ng kanilang malinis na hangarin at hindi upang ipanlinlang sa kaninoman, at ang alinmang panig na hindi susunod at lalabag sa kasunduang ito ay pananagutan ang lahat ng purwisyo ng panig na walang kasalanan, magbabayad ng halagang ₱50,000.00 bilang multa at babayaran pa rin ang gastos sa abogado at usapin ng walang tutol kung sakaling ang bagay na ito ay makaaabot sa Hukuman.

<sup>65</sup> Records, p. 310.

<sup>66</sup> *Ligutan v. Court of Appeals*, 427 Phil. 42, 51 (2002).

<sup>67</sup> *Florentino v. Supervalve, Inc.*, G.R. No. 172384, 12 September 2007, 533 SCRA 156, 166.

favor of petitioners. Considering that the *Kasunduan* stipulated that respondents would retain a portion of their share consisting of 1,750 square meters, said disposition should, however, be modified to give full effect to the intention of the contracting parties. Since the parties also fixed liquidated damages in the sum of ₱50,000.00 in case of breach, we find that said amount should suffice as petitioners' indemnity, without further need of compensation for moral and exemplary damages. In obligations with a penal clause, the penalty generally substitutes the indemnity for damages and the payment of interests in case of non-compliance.<sup>68</sup> Usually incorporated to create an effective deterrent against breach of the obligation by making the consequences of such breach as onerous as it may be possible, the rule is settled that a penal clause is not limited to actual and compensatory damages<sup>69</sup>

The RTC's award of attorney's fees in the sum of ₱50,000.00 is, however, proper. Aside from the fact that the penal clause included a liability for said award in the event of litigation over a breach of the *Kasunduan*, petitioners were able to prove that they incurred said sum in engaging the services of their lawyer to pursue their rights and protect their interests.<sup>70</sup>

**WHEREFORE**, premises considered, the Court of Appeals' assailed 23 January 2007 Decision is **REVERSED** and **SET ASIDE**. In lieu thereof, the RTC's 27 January 2005 Decision is **REINSTATED** subject to the following **MODIFICATIONS**: (a) the exclusion of a 1,750-square meter portion from the 60% share in the subject parcel respondents were ordered to convey in favor of petitioners; and (b) the deletion of the awards of moral and exemplary damages. The rights of the parties under the Agreement may be determined in a separate litigation.

**SO ORDERED.**

  
**JOSE PORTUGAL PEREZ**  
Associate Justice

<sup>68</sup> *Country Bankers Insurance Corporation v. Court of Appeals*, G.R. No. 85161, 9 September 1991, 201 SCRA 458, 465.

<sup>69</sup> *Yulo v. Chan Pe*, 101 Phil. 134, 138 (1957).

<sup>70</sup> Exhibit "W," records, pp. 474-475.

**WE CONCUR:**



**ARTURO D. BRION**

Associate Justice



**MARIANO C. DEL CASTILLO**

Associate Justice



**ESTELA M. PERLAS-BERNABE**

Associate Justice

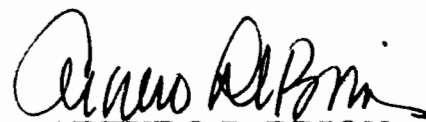


**MARVIC MARIO VICTOR F. LEONEN**

Associate Justice

**ATTESTATION**

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



**ARTURO D. BRION**

Associate Justice

Acting Chairperson, Second Division

**CERTIFICATION**

Pursuant to Section 13, Article VIII of the Constitution and the Division Acting Chairperson's Attestation, it is hereby certified that the conclusions in the above Decision were 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