

THIRD DIVISION

[G.R. NO. 164300, November 29, 2006]

**SPOUSES BENJAMIN AND AGRIFINA SIM, PETITIONERS, VS.
M.B. FINANCE CORPORATION, RESPONDENT.**

DECISION

CARPIO MORALES, J.:

On August 1, 1997, spouses Benjamin and Agrifina Sim (petitioners) purchased on installment basis a motor vehicle from Angus Motors Corporation (Angus), more particularly described as follows:

Make : Nissan Terrano Gasoline
Motor No. : Z24-972004Y
Serial No. : WNLYD21-G01634
Year Model : 1997

Petitioners thus executed a promissory note^[1] in favor of Angus in the amount of P1,105,344 to be paid in 36 consecutive monthly installments of P30,704, due and demandable on the first day of each month starting on September 1, 1997 until fully paid. The penalty for late payment was fixed at 5% a month based on installment in arrears.

To secure the payment of their obligation, petitioners executed a chattel mortgage^[2] over the vehicle. And they insured the vehicle with the Commonwealth Insurance Company (CIC) which issued Commercial Vehicle Policy No. 35823 for P895,000.^[3]

On August 14, 1997, Angus assigned its rights, title and interest over the promissory note and chattel mortgage to MB Finance Corporation (respondent).^[4]

Starting January 1998, petitioners defaulted in paying the monthly installments. On March 23, 1998, the vehicle was carnapped and was not recovered,^[5] prompting petitioners to file an insurance claim with the CIC which advised them, however, that it was respondent which was the beneficiary thereof.

Respondent opted to file a complaint against petitioners for sum of money with damages^[6] before the Regional Trial Court (RTC) of Makati.

By Decision of September 6, 2000,^[7] Branch 141 of the RTC Makati, discrediting petitioners' claim that payment of the proceeds of the insurance policy for the loss of the vehicle extinguished their obligation, held:

In the first place, there was no sufficient evidence to indicate that the car was insured. In the second place, there was no indication that the

insurance had actually paid [respondent]. More importantly, the car which was mortgaged was a mere collateral or security to the loan and the loss of the collateral is not one of the modes of extinguishing the loan obligation.^[8] (Underscoring supplied)

The trial court thus disposed:

WHEREFORE, judgment is hereby rendered ordering the [petitioners] jointly and severally to pay the [respondent] the sum of P983,593.72 as of 15 July 1998 plus penalty charge of 5% per month until fully paid, attorney's fees equivalent to 25% of the principal amount due and to pay the costs of this suit.^[9]

On petitioners' motion for reconsideration, the trial court, by Order of January 18, 2001,^[10] reduced the penalty charge of 5% per month as being unconscionable, citing *Medel v. Court of Appeals*.^[11]

The trial court thus pegged the penalty charge at 3% per month.

Petitioners appealed to the Court of Appeals, arguing that the insurance contract novated their obligation which should be computed on the basis of the principal amount of P716,000, and not P983,593.72 as held by the trial court, the latter sum having included interest and penalties whose rates are contrary to public policy; and that respondent is not entitled to attorney's fees, there being no existing obligation and, in any event, 25% of the amount due as such fees was exorbitant.

By Decision of February 5, 2004,^[12] the appellate court held that there was no novation. It reduced the penalty charge, however, to 1% interest per month or 12% percent per annum, citing Article 1229^[13] of the Civil Code. And it reduced too the award of attorney's fees to 10% of the principal amount due.

Thus, the appellate court disposed:

WHEREFORE, the Decision dated September 6, 2000 in Civil Case No. 98-2752 is AFFIRMED but modified in that the penalty interest per month on the unpaid installments is reduced to one percent (1%) per month or twelve percent (12%) per annum and the attorney's fees reduced to ten percent (10%) of the amount due. This ruling is without prejudice to pursuing whatever legal action Spouses Benjamin Sim and Agrifina Sim may have against Commonwealth Insurance Company pursuant to Commercial Vehicle Policy No. 35823, if so warranted.^[14]

Petitioners' Motion for Reconsideration having been denied, the present Petition for Review^[15] was filed, faulting the appellate court for

1. . . . fail[ure] to release petitioners from liability to the respondent.
2. . . . still holding petitioners liable for attorney's fees.^[16]

The appeal fails.

Fabrigas v. San Francisco del Monte, Inc. explains the nature of novation, viz: