

PHILIPPINE NATIONAL BANK, PLAINTIFF-APPELLEE, VS. UTILITY ASSURANCE & SURETY CO., INC. DEFENDANT-APPELLANT.

G.R. No. L-39215. September 01, 1989

Ponente: FELICIANO, J.

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FELICIANO, J.:

The Kangyo Bank Ltd., Tokyo, Japan, issued Letter of Credit No. 14-10272 in the amount of US\$28,150.00 in favor of the Pedro Bartolome Enterprises of Manila to cover an export shipment of logs to Japan. The beneficiary of the Letter of Credit assigned its rights to Lanuza Lumber. On 29 March 1960, Procopio Caderao, doing business under the trade name "Lanuza Lumber," obtained a loan of P25,000.00 from plaintiff-appellee Philippine National Bank (PNB) as evidenced by a promissory note on the security, among other things, of the proceeds of the Letter of Credit. The PNB in addition required Lanuza Lumber to submit a surety bond. Defendant-Appellant Utility Assurance & Surety Co., Inc. ("Utassco"), accordingly, executed Surety Bond No. B-123 in favor of PNB. It is useful to quote the terms of the Surety Bond in their entirety:

"SURETY BOND

Know All Men By These Presents:

That we, LANUZA LUMBER of Surigao, Surigao (532 Rosario St., Manila) as Principal, and the UTILITY ASSURANCE & SURETY CO., INC., a corporation duly organized and existing under and by virtue of the laws of the Philippines, with Head Office in the City of Manila, as Surety, are held and firmly bound unto PHILIPPINE NATIONAL BANK in the penal sum of TWENTY FIVE THOUSAND ONLY -- PESOS (P25,000.00) Philippine Currency, for the payment of which, well and truly to be made, we bind ourselves, our heirs, executors, administrators and successors and assigns, jointly and severally, firmly by these presents:

The conditions of this obligation are as follows:

Whereas, the Kangyo Bank, Ltd., Tokyo, Japan has granted a letter of credit No. 14-10272 in the amount of \$28,150.00 in favor of Pedro Bartolome Enterprises of 302 Salvacion Apt., 2504 Pennsylvania, Manila, to cover shipment of 500,000 board feet of logs to Shin Asshigawa Co., Ltd., Tokyo, Japan;

Whereas, on January 21, 1960 the beneficiary, Pedro Bartolome Enterprises assigned the aforementioned letter of credit to Lanuza Lumber of Surigao per attached Deed of Assignment;

Whereas, the correspondent Bank, Philippine National Bank requires the Lanuza Lumber to post a surety bond in the sum of Twenty Five Thousand (P25,000.00) Pesos, Philippine Currency, to guarantee full and faithful compliance by the beneficiary of the terms and conditions of the said letter of credit.

It is a special provision of this undertaking to guarantee the full payment of a loan not to exceed TWENTY FIVE THOUSAND PESOS (P25,000.00) that may be granted by the Philippine National Bank to Lanuza Lumber.

Whereas, said contract requires said Principal to give a good and sufficient bond in the above-stated sum to

secure the full and faithful performance on his part of said contract;

Now Therefore, if the Principal shall well and truly perform and fulfill all the undertakings, covenants, terms, conditions and agreements stipulated in said contract, then this obligation shall be null and void; otherwise to re-main in full force and effect.

The liability of the UTILITY ASSURANCE & SURETY CO., INC., on this bond will expire on March 17, 1961 and said bond will be cancelled TEN DAYS after its expiration, unless Surety is notified of any existing obligations thereunder.

In Witness Whereof, we have set our hands and signed our names at Manila on March 17, 1960.

Utility Assurance & Surety Co., Inc.

S/ Dalmacio Urtula, Jr.

DALMACIO URTULA, JR.

AUTHORIZED SIGNATURE

LANUZA LUMBER

S/ Procopio O. Caderao

General Manager

SIGNED IN THE PRESENCE OF:

(Sgd) ILLEGIBLE

(Sgd) ILLEGIBLE." (Underscoring supplied)

The surety bond was accompanied by an Endorsement No. B-60-3 which provided as follows:

"In lieu of the last paragraph of this bond, it is hereby declared and agreed that the following condition be incorporated in said bond and made an integral part thereof:

That, if the above bounden principal and surety shall, in all respects, duly and fully observe and perform all and singular terms and conditions of the aforementioned Letter of Credit, then this obligation shall be and become null and of no further force nor effect; in the contrary case, the same shall continue in full effect and be enforceable, as a joint and several obligation of the parties hereto in the manner provided by law so long as the account remains unpaid and outstanding in the books of the Bank either thru non-collection, extension, renewals or plans of payment with or without consent of the surety.

It is a special condition of this bond that the liability of the surety thereon shall, at all times, be enforceable simultaneously with that of the principal without the necessity of having the assets of the principal resorted to, or exhausted by, the creditor; Provided, however, that the liability of the surety shall be limited to the sum of TWENTY-FIVE THOUSAND PESOS (P25,000), Philippine Currency. Nothing herein contained shall be held to vary, alter, waive or change any of the terms, limits or conditions of the bond, except as herein-above set forth." (Underscoring supplied)

The promissory note executed by Lanuza Lumber became due and payable. Neither Lanuza Lumber nor Utassco paid the loan despite repeated demands by PNB for payment. Accordingly, PNB filed in the then Court of First Instance of Manila an action to recover the amount of the promissory note with interest as provided thereon plus attorney's fees.[1]

In its Answer to PNB's complaint, Utassco stated that it had "no knowledge or information sufficient to form a belief as to the truth of the allegations contained in [paragraphs 2, 3, 4 and 5] of the amended complaint and perforce [denied] the same."² At the same time, however, in setting out its affirmative defense, Utassco admitted that it had executed the surety bond and simultaneously pointed to the provisions of Endorsement No. B-60-3. In particular, Utassco contended that its obligation under the Surety Bond was to secure the performance of all the terms and conditions of the US\$28,150.00 Letter of Credit issued by Kangyo Bank Ltd. and had not guaranteed the performance of Lanuza Lumber's obligation under its P25,000.00 loan from PNB.

On 14 January 1971, upon motion of PNB, the trial court rendered judgment on the pleadings. The dispositive part of the judgment reads as follows:

"WHEREFORE, in the light of the foregoing considerations, judgment is hereby rendered ordering the defendant to pay the plaintiff the sum of P25,000.00, plus 6% interest per annum counted from May 19, 1962, the date of the filing of the original complaint until fully paid, plus attorney's fees equivalents to 10% of the principal obligation and the costs of the suit."

Its Motion for Reconsideration of the trial court's judgment on the pleadings having been denied, Utassco appealed that judgment to the Court of Appeals.

The Court of Appeals, by a Resolution dated 31 July 1974, certified the appeal to us as involving only questions of law.

Both before the Court of Appeals and this Court, Utassco claims that the trial court fell into error:

- (1) in granting the plaintiff-appellee's (PNB's) motion for judgment on the pleadings;
- (2) assuming the trial court could render judgment on the pleadings, in doing so prematurely; and
- (3) in awarding interest and attorney's fees in favor of plaintiff-appellee PNB.

We turn to the first alleged error. As noted earlier, Utassco had alleged in its answer that it had no knowledge or information sufficient to form a belief as to the truth of the allegations made by PNB in its complaint. Utassco, in other words, purported to deny those allegations and hence now contends that it had generated an issue of fact which the trial court should have first passed upon. Utassco, however, cannot be deemed to have denied the allegations of the amended complaint, considering that the truth of those allegations relating to the execution of the surety bond and the contents thereof was peculiarly within the knowledge of Utassco being the issuer of the bond and Endorsement No. B-60-3 itself. In *Equitable Banking Corporation v. Liwanag*,^[3] the Supreme Court rejected out of hand the same argument which Utassco now seeks to make:

"This pretense is manifestly devoid of merit. Although the Rules of Court permit a litigant to file an answer alleging lack of knowledge to form a belief as to the truth of certain allegations in the complaint, this form of denial 'must be availed of with sincerity and in good faith, -- certainly neither for the purpose of delay.' Indeed, it has been held that said mode of denial is unavailing 'where the fact as to which want of knowledge is asserted is to the knowledge of the court so plainly and necessarily within the defendant's knowledge that his averment of ignorance must be palpably untrue.' Thus, under conditions almost identical to those obtaining in the case at bar, this Court, speaking through Mr. Justice Villamor, upheld a judgment on the pleadings in *Capitol Motors vs. Nemesio L. Yabut* (G.R. No. L-28140, March 19, 1970) from which we quote:

"We agree with the defendant-appellant that one of the modes of specific denial contemplated in Section 10, Rule 8, is a denial by stating that the defendant is without knowledge or information sufficient to form a belief as to the truth of a material averment in the complaint. The question, however, is whether paragraph 2 of defendant-appellant's answer constitutes a specific denial under the said rule. We do not think so. In *Warner*

Barnes & Co. Ltd. vs. Reyes, et al. G.R. No L-9531, May 14, 1958 (103 Phil. 662), this Court said that the rule authorizing an answer to the effect that the defendant has no knowledge or information sufficient to form a belief as to the truth of an averment and giving such answer the effect of a denial, does not apply where the fact as to which want of knowledge is asserted, is so plainly and necessarily within the defendant's knowledge that his averment of ignorance must be palpably untrue.

In said case the suit was one for foreclosure of mortgage, and a copy of the deed of mortgage was attached to the complaint: thus, according to this Court, it would have been easy for the defendants to specifically allege in their answer whether or not they had executed the alleged mortgage. The same thing can be said in the present case, where a copy of the promissory note sued upon was attached to the complaint. The doctrine in Warner Barnes & Co. Ltd. was reiterated in J.P. Juan & Sons, Inc. v. Lianga Industries, Inc., G.R. No. L-25137, July 28, 1969 (28 SCRA 807) x x x." (Underscoring supplied)

At the same time that Utassco pretended to have denied the allegations of PNB's amended complaint, it admitted in the affirmative defense section of its answer that it had indeed executed the Surety Bond and Endorsement No. B-60-3 in favor of PNB; Utassco must be deemed thereby to have admitted the due execution of the Bond and the Endorsement. Its affirmative defense in fact consisted of pleading the very provisions of the Surety Bond upon which PNB based its cause of action. Thus, the issues raised by the amended complaint and the answer were not genuine issues of fact on which evidence would have had to be submitted. Those pleadings raised, rather, questions concerning the proper interpretation of the provisions of the Surety Bond and Endorsement No. B-60-3, i.e., the determination of whether the surety bond and the endorsement had, as contended by the PNB, guaranteed the payment by Lanuza Lumber of its P25,000.00 loan from PNB; or whether, as maintained by Utassco, the surety bond and its endorsement served merely to secure the performance of the terms and conditions of the Letter of Credit No. 14-10272. We hold, therefore, that under these circumstances, the trial court correctly rendered judgment on the pleadings.

We turn to the second error imputed by Utassco to the trial court: that the judgment on the pleadings, while it may have been within the jurisdiction of the trial court, was prematurely issued. This argument appears to us even more tenuous than the first assigned error. Utassco claims that the trial court should have withheld judgment on the pleadings until after the third party action brought by Utassco against the owner of Lanuza Lumber on the indemnity agreement executed between them, had gone forward to judgment. The third party complaint could, of course, have been prosecuted quite separately from the principal action between PNB and Utassco. Indeed, there was no reason at all why the trial court should have deferred rendering judgment on the pleadings in the principal action, considering that the PNB was not interested at all in the outcome of the third party complaint. Under Section 12, Rule 6 of the Revised Rules of Court, the purpose of a third party complaint is to enable a defending party to obtain contribution, indemnity, subrogation or other relief from a person not a party to the action. Thus, notwithstanding the judgment on the pleadings, Utassco could still proceed with the prosecution of its third party complaint.

Before passing on to the third error assigned by Utassco, it is important to note that Utassco did not really dispute the correctness of the conclusion reached by the trial court in respect of the substantive issue raised before it: whether the bond issued by Utassco secured the obligations of Lanuza Lumber to repay the P25,000.00 loan obtained from PNB, or whether the bond had secured the Letter of Credit. The trial court held that the surety bond was intended to secure the repayment of Lanuza Lumber's loan from PNB. We believe and so hold that the trial court was correct in so holding. In the first place, the surety bond explicitly stated that the P25,000.00 loan was being secured by the bond:

"It is a special provision of this undertaking to guarantee the full payment of a loan not to exceed TWENTY

FIVE THOUSAND PESOS (P25,000.00) that may be granted by the Philippine National Bank to Lanuza Lumber."

In the second place, while the bond and the endorsement had referred to the Letter of Credit, Lanuza Lumber had no obligations under the Letter of Credit. As noted earlier, Lanuza Lumber was beneficiary-assignee of the Letter of Credit. Thus, Utassco's view would reduce the terms and conditions of the Surety Bond to nonsense. Such view would also mean that Utassco, in its own reading of the bond, was never at risk since there were no obligations to secure and that Utassco was in fact collecting premiums for issuing the bond under which it had no liabilities. The principle of effectiveness is basic in contract interpretation: where two (2) interpretations of the same contract language are possible, one interpretation having the effect of rendering the contract meaningless (and one of the parties merely dishonest for receiving consideration thereunder without parting with any), while the other interpretation would give effect to the contract as a whole, the latter interpretation must be adopted.[4]

In the instant case, the reference to the Letter of Credit in the surety bond and the endorsement was either merely inadvertent surplusage or, alternatively, merely indication of ineptness on the part of the draftsman of the bond and the endorsement. It is not disputed by Utassco that the endorsement was intended to replace the final paragraph of the original bond, which paragraph limited the life of the bond to one year from issuance. The endorsement had the important effect of giving the bond continuing life so long as "the account" remained unpaid and outstanding on the books of PNB. The term "account" here could only refer to the account of the principal debtor, Lanuza Lumber, with PNB. The endorsement also made it clear that the liability of Lanuza Lumber and Utassco was joint and several in nature, and that Utassco had waived any benefit of excussion that it might otherwise have had. Finally, on a very practical level, it is difficult to understand how Utassco could have reasonably supposed that its bond in the amount of RPP25,000.00 was intended only (or even principally) to secure performance of the obligations of the issuer -- Kangyo Bank - under the Letter of Credit which had a face value of US\$28,150.00, many times the face value of the bond.

We come to the final error assigned by Utassco: that the trial court should not have granted interest and attorney's fees in favor of PNB, considering the clause in the endorsement limiting the liability of Utassco to P25,000.00. The issue here presented is not a new one. It was extensively discussed and Utassco's submission decisively rejected by this Court in *Plaridel Surety and Insurance Co., Inc. v. P.L. Galang Machinery Co., Inc.*, [5]

There, the Court held:

"Petitioner objects to the payment of interest and attorney's fees because: (1) they were not mentioned in the bond; and (2) the surety would become liable for more than the amount stated in the contract of suretyship.

"In support of its objection petitioner dwells on the proposition that a surety's liability can not be extended beyond the terms of his undertaking, citing articles 1956 and 2208 of the New Civil Code which provide as follows:

'ART. 1956. No interest shall be due unless it has been expressly stipulated in writing.'

'ART. 2208. In the absence of stipulation, attorney's fees and expenses of litigation, other than judicial costs, cannot be recovered, except: x x x.'

"The objection has to be overruled, because as far back as the year 1922 this Court held in *Tagawa vs. Aldanese*, 43 Phil. 852, that creditors suing on a suretyship bond may recover from the surety as part of their damages, interest at the legal rate even if the surety would thereby become liable to pay more than the total amount stipulated in the bond. 'The theory is that interest is allowed only by way of damages for delay upon the part of the sureties in making payment after they should have done. In some states, the interest has been charged from the date of the judgment of the appellate court. In this jurisdiction, we rather prefer to follow the

general practice which is to order that interest begin to run from the date when the complaint was filed in court, x x x.'

Such theory aligned with Sec. 510 of the Code of Civil Procedure which was subsequently recognized in the Rules of Court (Rule 53, Section 6) and with Article 1108 of the Civil Code (now Art. 2209 of the New Civil Code).

"In other words the surety is made to pay interest, not by reason of the contract, but by reason of its failure to pay when demanded and for having compelled the plaintiff to resort to the courts to obtain payment. It should be observed that interest does not run from the time the obligation became due, but from the filing of the complaint.

"As to attorney's fees. Before the enactment of the New Civil Code, successful litigants could not recover attorney's fees as part of the damages they suffered by reason of the litigation. Even if the party paid thousands of pesos to his lawyers, he could not charge the amount to his opponent.

"However, the New Civil Code permits recovery of attorney's fees in eleven cases enumerated in Article 2208, among them 'where the court deem it just and equitable that attorney's fees and expenses of litigation should be recovered' or 'when the defendant acted in gross and evident bad faith in refusing to satisfy the plaintiff's plainly valid, just and demandable claim.' This gives the courts discretion in apportioning attorney's fees.

"Now, considering, in this case, that the principal debtor had openly and expressly admitted his liability under the bond, and the surety knew it (p. 123 R.A.), we can not say there was abuse of lower court's discretion in the way of awarding fees, specially when the indemnity agreement x x x afforded the surety adequate protection. (100 Phil. 681-682)." (Underscoring supplied)

WHEREFORE, the Court Resolved to DISMISS the appeal by defendant-appellant Utility Assurance & Surety Co., Inc. for lack of merit, and to AFFIRM the judgment of the trial court dated 14 January 1971. No pronouncement as to costs. This Resolution is immediately executory.

SO ORDERED.

Fernan, C.J., (Chairman), Gutierrez, Jr., Bidin, and Cortes, JJ., concur.

[1] Utassco thereafter filed a third-party complaint against Procopio O. Caderao, Alberto T. Aguja and Daniel Romualdez, praying that in the event judgment be rendered in favor of PNB and against it, the third-party defendants should in turn be jointly and severally liable to it for whatever amount it would be ordered to pay PNB, plus attorney's fees. On further motion by Utassco, the trial court declared Alberto D. Aguja in default as third-party defendant; the complaint against third-party defendant Procopio O. Caderao meanwhile was dismissed without prejudice.

[2] Record on Appeal, pp. 19-20.

[3] 32 SCRA 293 (1970).

[4] Art. 1373, Civil Code; and Rule 130, Sec. 9, Revised Rules of Court. Federation of United Namarco Distributors, Inc. v. National Marketing Corporation, 114 Phil. 802 (1962).

[5] 100 Phil. 679 (1957).

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