

**EULALIO PRUDENCIO AND ELISA T. PRUDENCIO, PETITIONERS, VS.
THE HONORABLE COURT OF APPEALS, THE PHILIPPINE NATIONAL
BANK, RAMON C. CONCEPCION AND MANUEL M. TAMAYO,
PARTNERS OF TH...**

G.R. No. L-34539. July 14, 1986

Ponente: GUTIERREZ, JR., J.

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GUTIERREZ, JR., J.:

This is a petition for review seeking to annul and set aside the decision of the Court of Appeals, now the Intermediate Appellate Court, affirming the order of the trial court which dismissed the petitioners' complaint for cancellation of their real estate mortgage and held them jointly and severally liable with the principal debtors on a promissory note which they signed as accommodation makers.

The factual background of this case is stated in the decision of the appellate court:

"Appellants are the registered owners of a parcel of land located in Sampaloc, Manila, and covered by T.C.T. 35161 of the Register of Deeds of Manila. On October 7, 1954, this property was mortgaged by the appellants to the Philippine National Bank, hereinafter called PNB, to guarantee a loan of P1,000.00 extended to one Domingo Prudencio.

"Sometime in 1955, the Concepcion & Tamayo Construction Company, hereinafter called Company, had a pending contract with the Bureau of Public Works, hereinafter called the Bureau, for the construction of the municipal building in Puerto Princesa, Palawan, in the amount of P36,800.00 and, as said Company needed funds for said construction, Jose Toribio, appellants' relative, and attorney-in-fact of the Company, approached the appellants asking them to mortgage their property to secure the loan of P10,000.00 which the Company was negotiating with the PNB.

"After some persuasion appellants signed on December 23, 1955 the 'Amendment of Real Estate Mortgage', mortgaging their said property to the PNB to guaranty the loan of P10,000.00 extended to the Company. The terms and conditions of the original mortgage for P1,000.00 were made integral part of the new mortgage for P10,000.00 and both documents were registered with the Register of Deeds of Manila. The promissory note covering the loan of P10,000.00 dated December 29, 1955, maturing on April 27, 1956, was signed by Jose Toribio, as attorney-in-fact of the Company, and by the appellants. Appellants also signed the portion of the promissory note indicating that they are requesting the PNB to issue the Check covering the loan to the Company. On the same date (December 23, 1955) that the 'Amendment of Real Estate' was executed, Jose Toribio, in the same capacity as attorney-in-fact of the Company, executed also the 'Deed of Assignment' assigning all payments to be made by the Bureau to the Company on account of the contract for the construction of the Puerto Princesa building in favor of the PNB.

"This assignment of credit to the contrary notwithstanding, the Bureau, with approval, of the PNB, conditioned, however that they should be for Labor and materials, made three payments to the Company on account of the contract price totalling P11,234.40. The Bureau's last request for P5,000.00 on June 20, 1956,

however, was denied by the PNB for the reason that since the loan was already overdue as of April 28, 1956, the remaining balance of the contract price should be applied to the loan.

"The Company abandoned the work, as a consequence of which on June 30, 1956, the Bureau rescinded the construction contract and assumed the work of completing the building. On November 14, 1958, appellants wrote the PNB contending that since the PNB authorized payments to the Company instead of on account of the loan guaranteed by the mortgage there was a change in the conditions of the contract without the knowledge of appellants, which entitled the latter to a cancellation of their mortgage contract.

"Failing in their bid to have the real estate mortgage cancelled, appellants filed on June 27, 1959 this action against the PNB, the Company, the latter's attorney-in-fact Jose Toribio, and the District Engineer of Puerto Princesa, Palawan, seeking the cancellation of their real estate mortgage. The complaint was amended to exclude the Company as defendant, it having been shown that its life as a partnership had already expired and, in lieu thereof, Ramon Concepcion and Manuel M. Tamayo, partners of the defunct Company, were impleaded in their private capacity as defendants."

After hearing, the trial court rendered judgment, denying the prayer in the complaint that the petitioners be absolved from their obligation under the mortgage contract and that the said mortgage be released or cancelled. The petitioners were ordered to pay jointly and severally with their co-makers Ramon C. Concepcion and Manuel M. Tamayo the sum of P11,900.19 with interest at the rate of 6% per annum from the date of the filing of the complaint on June 27, 1959 until fully paid and P1,000.00 attorney's fees.

The decision also provided that if the judgment was not satisfied within 90 days from its receipt, the mortgaged properties together with all the improvements thereon belonging to the petitioners would be sold at public auction and applied to the judgment debt.

The Court of Appeals affirmed the trial court's decision in toto stating that, as accommodation makers, the petitioners' liability is that of solidary co-makers and that since "the amounts released to the construction company were used therein and, therefore, were spent for the successful accomplishment of the work constructed for, the authorization made by the Philippine National Bank of partial payments to the construction company which was also one of the solidary debtors cannot constitute a valid defense on the part of the other solidary debtors. Moreover, those who rendered services and furnished materials in the construction are preferred creditors and have a lien on the price of the contract." The appellate court further held that PNB had no obligation whatsoever to notify the petitioners of its authorizing the three payments in the total amount of P11,234.00 in favor of the Company because aside from the fact that the petitioners were not parties to the deed of assignment, there was no stipulation in said deed making it obligatory on the part of the PNB to notify the petitioners everytime it authorizes payment to the Company. It ruled that the petitioners cannot ask to be released from the real estate mortgage.

In this petition, the petitioners raise the following issues which they present in the form of errors:

I. First Assignment of Error.

THE HONORABLE COURT OF APPEALS ERRED IN HOLDING THAT HEREIN PETITIONERS WERE SOLIDARY CO-DEBTORS INSTEAD OF SURETIES.

II. Second Assignment of Error.

THE HONORABLE COURT OF APPEALS ERRED IN HOLDING THAT PETITIONERS WERE NOT RELEASED FROM THEIR OBLIGATION TO THE RESPONDENT PNB, WHEN THE PNB, WITHOUT THE KNOWLEDGE AND CONSENT OF PETITIONERS, CHANGED THE TENOR AND CONDITION OF THE ASSIGNMENT OF PAYMENTS MADE BY THE PRINCIPAL DEBTOR, CONCEPCION &

TAMAYO CONSTRUCTION COMPANY, AND RELEASED TO SUCH PRINCIPAL DEBTOR PAYMENTS FROM THE BUREAU OF PUBLIC WORKS WHICH WERE MORE THAN ENOUGH TO WIPE OUT THE INDEBTEDNESS TO THE PNB.

The petitioners contend that as accommodation makers, the nature of their liability is only that of mere sureties instead of solidary co-debtors such that "a material alteration in the principal contract, effected by the creditor without the knowledge and consent of the sureties, completely discharges the sureties from all liability on the contract of suretyship." They state that when respondent PNB did not apply the initial and subsequent payments to the petitioner's debt as provided for in the deed of assignment, they were released from their obligation as sureties and, therefore, the real estate mortgage executed by them should have been cancelled.

Section 29 of the Negotiable Instrument Law provides:

"Liability of accommodation party. - An accommodation party is one who has signed the instrument as maker, drawer, acceptor, or indorser, without receiving value therefor, and for the purpose of lending his name to some other person. Such a person is liable on the instrument to a holder for value, notwithstanding such holder at the time of taking the instrument knew him to be only an accommodation party."

In the case of *Philippine Bank of Commerce v. Aruego* (102 SCRA 530, 539), we held that "x x x in lending his name to the accommodated party, the accommodation party is in effect a surety. x x x." However, unlike in a contract of suretyship, the liability of the accommodation party remains not only primary but also unconditional to a holder for value such that even if the accommodated party receives an extension of the period for payment without the consent of the accommodation party, the latter is still liable for the whole obligation and such extension does not release him because as far as a holder for value is concerned, he is a solidary co-debtor.

Expounding on the nature of the liability of an accommodation party under the aforequoted section, we ruled in *Ang Tiong v. Ting* (22 SCRA 713, 716):

"3. That the appellant, again assuming him to be an accommodation indorser, may obtain security from the maker to protect himself against the danger of insolvency of the latter, cannot in any manner affect his liability to the appellee, as the said remedy is a matter of concern exclusively between accommodation indorser and accommodated party. So that the appellant stands only as a surety in relation to the maker, granting this to be true for the sake of argument, is immaterial to the claim of the appellee, and does not at all diminish nor defeat the rights of the latter who is a holder for value. The liability of the appellant remains primary and unconditional. To sanction the appellant's theory is to give unwarranted legal recognition to the patent absurdity of a situation where an indorser, when sued on an instrument by a holder in due course and for value, can escape liability on his indorsement by the convenient expedient of interposing the defense that he is a mere accommodation indorser."

There is, therefore, no question that as accommodation makers, petitioners would be primarily and unconditionally liable on the promissory note to a holder for value, regardless of whether they stand as sureties or solidary co-debtors since such distinction would be entirely immaterial and inconsequential as far as a holder for value is concerned. Consequently, the petitioners cannot claim to have been released from their obligation simply because the time of payment of such obligation was temporarily deferred by PNB without their knowledge and consent. There has to be another basis for their claim of having been freed from their obligation. The question which should be resolved in this instant petition, therefore, is whether or not PNB can be considered a holder for value under Section 29 of the Negotiable Instruments Law such that the petitioners must be necessarily barred from setting up the defense of want of consideration or some other personal defenses which may be set up against a party who is not a holder in due course.

A holder for value under Section 29 of the Negotiable Instruments Law is one who must meet all the requirements

of a holder in due course under Section 52 of the same law except notice of want of consideration. (Agbayani, Commercial Laws of the Philippines, 1964, p. 208). If he does not qualify as a holder in due course then he holds the instrument subject to the same defenses as if it were non-negotiable (Section 58, Negotiable Instruments Law).

In the case at bar, can PNB, the payee of the promissory note be considered a holder in due course?

Petitioners contend that the payee PNB is an immediate party and, therefore, is not a holder in due course and stands on no better footing than a mere assignee.

In those cases where a payee was considered a holder in due course, such payee either acquired the note from another holder or has not directly dealt with the maker thereof. As was held in the case of Bank of Commerce and Savings v. Randell (186 North-Western Reporter 71):

"We conclude, therefore, that a payee who receives a negotiable promissory note, in good faith, for value, before maturity, and without any notice of any infirmity, from a holder, not the maker, to whom it was negotiated as a completed instrument, is a holder in due course within the purview of a Negotiable Instruments law, so as to preclude the defense of fraud and failure of consideration between the maker and the holder to whom the instrument was delivered."

Similarly, in the case of Stone v. Goldberg & Lewis (60 Southern Reporter 748) on rehearing and quoting Daniel on Negotiable Instruments, it was held:

"It is a general principle of the law merchant that, as between the immediate parties to a negotiable instrument - the parties between whom there is a privity - the consideration may be inquired into; and as to them the only superiority of a bill or note over other unsealed evidence of debt is that it prima facie imports a consideration."

Although as a general rule, a payee may be considered a holder in due course we think that such a rule cannot apply with respect to the respondent PNB. Not only was PNB an immediate party or in privity to the promissory note, that is, it had dealt directly with the petitioners knowing fully well that the latter only signed as accommodation makers but more important, it was the Deed of Assignment executed by the Construction Company in favor of PNB which principally moved the petitioners to sign the promissory note also in favor of PNB. Petitioners were made to believe and on that belief entered into the agreement that no other conditions would alter the terms thereof and yet; PNB altered the same. The Deed of Assignment specifically provided that Jose F. Toribio, on behalf of the Company, "have assigned, transferred and conveyed and by these presents, do assign, transfer and convey unto the said Philippine National Bank, its successors and assigns all payments to be received from the Bureau of Public Works on account of contract for the construction of the Puerto Princesa Municipal Building in Palawan, involving the total amount of P36,000.00" and that "This assignment shall be irrevocable and subject to the terms and conditions of the promissory note and or any other kind of documents which the Philippine National Bank have required or may require the assignor to execute to evidence the above-mentioned obligation."

Under the terms of the above Deed, it is clear that there are no further conditions which could possibly alter the agreement without the consent of the petitioners such as the grant of greater priority to obligations other than the payment of the loan due to the PNB and part of which loan was guaranteed by the petitioners in the amount of P10,000.00.

This, notwithstanding, PNB approved the Bureau's release of three payments directly to the Company instead of paying the same to the Bank. This approval was in violation of the Deed of Assignment and without any notice to the petitioners who stood to lose their property once the promissory note falls due without the same having been paid because the PNB, in effect, waived payments of the first three releases. From the foregoing circumstances,

PNB can not be regarded as having acted in good faith which is also one of the requisites of a holder in due course under Section 52 of the Negotiable Instruments Law. The PNB knew that the promissory note which it took from the accommodation makers was signed by the latter because of full reliance on the Deed of Assignment, which, PNB had no intention to comply with strictly. Worse, the third payment to the Company in the amount of P4,293.60 was approved by PNB although the promissory note was almost a month overdue, an act which is clearly detri-mental to the petitioners.

We, therefore, hold that respondent PNB is not a holder in due course. Thus, the petitioners can validly set up their personal defense of release from the real estate mortgage against PNB. The latter, in authorizing the third payment to the Company after the promissory note became due, in effect, extended the term of the payment of the note without the consent of the accommodation makers who stand as sureties to the accommodated party and to all other parties who are not holders in due course or who do not derive their right from the same, including PNB.

It may be argued that the Prudencios could have mortgaged their property even without the promissory note. The records show, however, that they would not have mortgaged the lot were it not for the sake of the Company whose attorney-in-fact was their relative. The spouses did not need the money for themselves.

The attorney-in-fact tried twice to convince the Prudencios to mortgage their property in order to secure a loan in favor of the Company but the Prudencios refused. It was only when the deed of assignment was shown to the spouses that they consented to the mortgage and signed the promissory note in the Bank's favor.

Article 2085 of the Civil Code enumerates the requisites of a valid mortgage contract. Petitioners do not dispute the validity of the mortgage. They only want to have it cancelled because the Bank violated the deed of assignment and extended the period of time of payment of the promissory note without the petitioners' consent and to the latter's detriment.

The mortgage cannot be separated from the promissory note for it is the latter which is the basis of determin-ing whether the mortgage should be foreclosed or cancelled. Without the promissory note which determines the amount of indebtedness there would have been no basis for the mort-gage.

True, if the Bank had not been the assignee, then the petitioners would be obliged to pay the Bank as their cre-ditor on the promissory note, irrespective of whether or not the deed of assignment had been violated. However, the assignee and the creditor in this case are one and the same - the Bank itself. When the Bank violated the deed of assignment, it prejudiced itself because its very violation was the reason why it was not paid on time in its capacity as creditor in the promissory note. It would be unfair to make the petitioners now answer for the debt or to foreclose on their property.

Neither can PNB justify its acts on the ground that the Bureau of Public Works approved the deed of assignment with the condition that the wages of laborers and materials needed in the construction work must take precedence over the payment of the promissory note. In the first place, PNB did not need the approval of the Bureau. But even if it did, it should have informed the petitioners about the amendment of the deed of assignment. Secondly, the wages and materials have already been paid. That issue is academic. What is in dispute is who should bear the loss in this case. As between the petitioners and the Bank, the law and the equities of the case favor the petitioners. And thirdly, the wages and materials constitute a lien only on the constructed building but do not enjoy pre-ference over the loan unless there is a liquidation pro-ceeding such as in insolvency or settlement of estate. (See *Philippine Savings Bank v. Lantin*, 124 SCRA 476). There were remedies available at the time if the laborers and the creditors had not been paid. The fact is, they have been paid. Hence, when the PNB accepted the condition imposed by the Bureau without the knowledge or consent of the petitioners, it amended the deed of assign-ment which, as stated earlier, was the principal reason why the petitioners consented to become

accommodation makers.

WHEREFORE, the petition is GRANTED. The decision of the Court of Appeals affirming the decision of the trial court is hereby REVERSED and SET ASIDE and a new one entered absolving the petitioners from liability on the promissory note and under the mortgage contract. The Philippine National Bank is ordered to release the real estate mortgage constituted on the property of the petitioners and to pay the amount of THREE THOUSAND PESOS (P3,000.00) as attorney's fees.

SO ORDERED.

Feria, (Chairman), Fernan, Alampay, and Paras, JJ., concur.

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