INTRA-STRATA ASSURANCE CORPORATION AND PHILIPPINE HOME ASSURANCE CORPORATION, PETITIONERS, VS. REPUBLIC OF THE PHILIPPINES, REPRESENTED BY THE BUREAU OF CUSTOMS, RESPONDENT.

G.R. No. 156571. July 09, 2008

Ponente: BRION, J.

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BRION, J.:

Before this Court is the Petition for Review on Certiorari under Rule 45 of the Rules of Court filed by Intra-Strata Assurance Corporation (Intra-Strata) and Philippine Home Assurance Corporation (PhilHome), collectively referred to as "petitioners."

The petition seeks to set aside the decision dated November 26, 2002 of the Court of Appeals[1] (CA) that in turn affirmed the ruling of the Regional Trial Court (RTC), Branch 20, Manila in Civil Case No. 83-15071. [2] In its ruling, the RTC found the petitioners liable as sureties for the customs duties, internal revenue taxes, and other charges due on the importations made by the importer, Grand Textile Manufacturing Corporation (Grand Textile). [3]

BACKGROUND FACTS

Grand Textile is a local manufacturing corporation. In 1974, it imported from different countries various articles such as dyestuffs, spare parts for textile machinery, polyester filament yarn, textile auxiliary chemicals, trans open type reciprocating compressor, and trevira filament. Subsequent to the importation, these articles were transferred to Customs Bonded Warehouse No. 462. As computed by the Bureau of Customs, the customs duties, internal revenue taxes, and other charges due on the importations amounted to P2,363,147.00. To secure the payment of these obligations pursuant to Section 1904 of the Tariff and Customs Code (Code),[4] Intra- Strata and PhilHome each issued general warehousing bonds in favor of the Bureau of Customs. These bonds, the terms of which are fully quoted below, commonly provide that the goods shall be withdrawn from the bonded warehouse "on payment of the legal customs duties, internal revenue, and other charges to which they shall then be subject."[5]

Without payment of the taxes, customs duties, and charges due and for purposes of domestic consumption, Grand Textile withdrew the imported goods from storage.[6] The Bureau of Customs demanded payment of the amounts due from Grand Textile as importer, and from Intra-Strata and PhilHome as sureties. All three failed to pay. The government responded on January 14, 1983 by filing a collection suit against the parties with the RTC of Manila.

LOWER COURT DECISIONS

After hearing, the RTC rendered its January 4, 1995 decision finding Grand Textile (as importer) and the petitioners (as sureties) liable for the taxes, duties, and charges due on the imported articles. The dispositive portion of this decision states: [7]

> WHEREFORE, premises considered, the Court RESOLVES directing:

(1)

the defendant Grand Textile Manufacturing Corporation to pay plaintiff, the sum of P2,363,174.00, plus interests at the legal rate from the filing of the Complaint until fully paid;

(2)

the defendant Intra-Strata Assurance Corporation to pay plaintiff, jointly and severally, with defendant Grand, the sum of P2,319,211.00 plus interest from the filing of the Complaint until fully paid; and the defendant Philippine Home Assurance Corporation to pay plaintiff the sum of P43,936.00 plus interests to be computed from the filing of the Complaint until fully paid;

(3)

the forfeiture of all the General Warehousing Bonds executed by Intra- Strata and PhilHome; and

(4)

all the defendants to pay the costs of suit.

SO ORDERED.

The CA fully affirmed the RTC decision in its decision dated November 26, 2002. From this CA decision, the petitioners now come before this Court through a petition for review on certiorari alleging that the CA decided the presented legal questions in a way not in accord with the law and with the applicable jurisprudence.

ASSIGNED ERRORS
The petitioners present the following points as the conclusions the CA should have made:

- that they were released from their obligations under their bonds when Grand Textile withdrew the imported goods without payment of taxes, duties, and other charges; and

- that their non-involvement in the active handling of the warehoused items from the time they were stored up to their withdrawals substantially increased the risks they assumed under the bonds they issued, thereby releasing them from liabilities under these bonds.[8]

In their arguments, they essentially pose the legal issue of whether the withdrawal of the stored goods, wares, and merchandise - without notice to them as sureties - released them from any liability for the duties, taxes, and charges they committed to pay under the bonds they issued. They additionally posit that they should be released from any liability because the Bureau of Customs, through the fault or negligence of its employees, allowed the withdrawal of the goods without the payment of the duties, taxes, and other charges due.

The respondent, through the Solicitor General, maintains the opposite view.

THE COURT'S RULING
We find no merit in the petition and consequently affirm the CA decision.

Nature of the Surety's Obligations

Section 175 of the Insurance Code defines a contract of suretyship as an agreement whereby a party called the surety guarantees the performance by another party called the principal or obligor of an obligation or undertaking in favor of another party called the obligee, and includes among its various species bonds such as those issued pursuant to Section 1904 of the Code.[9] Significantly, "pertinent provisions of the Civil Code of the Philippines shall be applied in a suppletory character whenever necessary in interpreting the provisions of a contract of

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suretyship."[10] By its very nature under the terms of the laws regulating suretyship, the liability of the surety is joint and several but limited to the amount of the bond, and its terms are determined strictly by the terms of the contract of suretyship in relation to the principal contract between the obligor and the obligee.[11]

The definition and characteristics of a suretyship bring into focus the fact that a surety agreement is an accessory contract that introduces a third party element in the fulfillment of the principal obligation that an obligor owes an obligee. In short, there are effectively two (2) contracts involved when a surety agreement comes into play - a principal contract and an accessory contract of suretyship. Under the accessory contract, the surety becomes directly, primarily, and equally bound with the principal as the original promissor although he possesses no direct or personal interest over the latter's obligations and does not receive any benefit therefrom.[12]

The Bonds Under Consideration

That the bonds under consideration are surety bonds (and hence are governed by the above laws and rules) is not disputed; the petitioners merely assert that they should not be liable for the reasons summarized above. Two elements, both affecting the suretyship agreement, are material in the issues the petitioners pose. The first is the effect of the law on the suretyship agreement; the terms of the suretyship agreement constitute the second.

A feature of the petitioners' bonds, not stated expressly in the bonds themselves but one that is true in every contract, is that applicable laws form part of and are read into the contract without need for any express reference. This feature proceeds from Article 1306 of the Civil Code pursuant to which we had occasion to rule:

> It is to be recognized that a large degree of autonomy is accorded the contracting parties. Not that it is unfettered. They may, according to Article 1306 of the Civil Code "establish such stipulations, clauses, terms, and conditions as they may deem convenient, provided that they are not contrary to law, morals, good customs, public order, or public policy." The law thus sets limits. It is a fundamental requirement that the contract entered into must be in accordance with, and not repugnant to, an applicable statute. Its terms are embodied therein. The contracting parties need not repeat them. They do not even have to be referred to. Every contract thus contains not only what has been explicitly stipulated but also the statutory provisions that have any bearing on the matter."[13]

Two of the applicable laws, principally pertaining to the importer, are Sections 101 and 1204 of the Tariff and Customs Code which provide that:

> Sec 101. Imported Items Subject to Duty - All articles when imported from any foreign country into the Philippines shall be subject to duty upon such importation even though previously exported from the Philippines, except as otherwise specifically provided for in this Code or in clear laws.
>
> x x x x
>
> Sec. 1204. Liability of Importer for Duties - Unless relieved by laws or regulations, the liability for duties, taxes, fees, and other charges attaching on importation constitutes a personal debt due from the importer to the government which can be discharged only by payment in full of all duties, taxes, fees, and other charges legally accruing. It also constitutes a lien upon the articles imported which may be enforced which such articles are in custody or subject to the control of the government.

The obligation to pay, principally by the importer, is shared by the latter with a willing third party under a suretyship agreement under Section 1904 of the Code which itself provides:

> Section 1904. Irrevocable Domestic Letter of Credit or Bank Guarantee or Warehousing Bond - After articles declared in the entry of warehousing shall have been examined and the duties, taxes, and other charges shall have been determined, the Collector shall require from the importer, an irrevocable domestic letter of credit, bank guarantee, or bond equivalent to the amount of such duties, taxes, and other charges conditioned upon the

> withdrawal of the articles within the period prescribed by Section 1908 of this Code and for payment of any duties, taxes, and other charges to which the articles shall then be subject and upon compliance with all legal requirements regarding their importation.

We point these out to stress the legal basis for the submission of the petitioners' bonds and the conditions attaching to these bonds. As heretofore mentioned, there is, firstly, a principal obligation belonging to the importer-obligor as provided under Section 101; secondly, there is an accessory obligation, assumed by the sureties pursuant to Section 1904 which, by the nature of a surety agreement, directly, primarily, and equally bind them to the obligee to pay the obligor's obligation.

The second element to consider in a suretyship agreement relates to the terms of the bonds themselves, under the rule that the terms of the suretyship are determined by the suretyship contract itself.[14] The General Warehousing Bond [15] that is at the core of the present dispute provides:

> KNOW ALL MEN BY THESE PRESENTS:
>
> That I/we GRAND TEXTILE MANUFACTURING CORPORATION - Km. 21, Marilao, Bulacan, as Principal, and PHILIPPINE HOME ASSURANCE as the latter being a domestic corporation duly organized and existing under and by virtue of the laws of the Philippines, as Surety, are held and firmly bound unto the Republic of the Philippines, in the sum of PESOS TWO MILLION ONLY (P2,000,000.00), Philippine Currency, to be paid to the Republic of the Philippines, for the payment whereof, we bind ourselves, our heirs, executors, administrators and assigns, jointly and severally, firmly by these presents:
>
> WHEREAS, the above-bounden Principal will from time to time make application to make entry for storing in customs-internal revenue bonded warehouse certain goods, wares, and merchandise, subject to customs duties and special import tax or internal revenue taxes or both;
>
> WHEREAS, the above principal in making application for storing merchandise in customs-internal revenue bonded warehouse as above stated, will file this in his name as principal, which bond shall be approved by the Collector of Customs or his Deputy; and
>
> WHEREAS, the surety hereon agrees to accept all responsibility jointly and severally for the acts of the principal done in accordance with the terms of this bond.
>
> NOW THEREFORE, the condition of this obligation is such that if within six (6) months from the date of arrival of the importing vessel in any case, the goods, wares, and merchandise shall be regularly and lawfully withdrawn from public stores or bonded warehouse on payment of the legal customs duties, internal revenue taxes, and other charges to which they shall then be subject; or if at any time within six (6) months from the said date of arrival, or within nine (9) months if the time is extended for a period of three (3) months, as provided in Section 1903 of the Tariff and Customs Code of the Philippines, said importation shall be so withdrawn for consumption, then the above obligation shall be void, otherwise, to remain in full force and effect.
>
> Obligations hereunder may only be accepted during the calendar year 1974 and the right to reserve by the corresponding Collector of Customs to refuse to accept further liabilities under this general bond, whenever, in his opinion, conditions warrant doing so.
>
> IN WITNESS WHEREOF, we have signed our names and affixed our seals on this 20[th] day of September, 1974 at Makati, Rizal, Philippines.

Considered in relation with the underlying laws that are deemed read into these bonds, it is at once clear that the bonds shall subsist - that is, "shall remain in full force and effect" - unless the imported articles are "regularly and lawfully withdrawn. . .on payment of the legal customs duties, internal revenue taxes, and other charges to which

they shall be subject...." Fully fleshed out, the obligation to pay the duties, taxes, and other charges primarily rested on the principal Grand Textile; it was allowed to warehouse the imported articles without need for prior payment of the amounts due, conditioned on the filing of a bond that shall remain in full force and effect until the payment of the duties, taxes, and charges due. Under these terms, the fact that a withdrawal has been made and its circumstances are not material to the sureties' liability, except to signal both the principal's default and the elevation to a due and demandable status of the sureties' solidary obligation to pay. Under the bonds' plain terms, this solidary obligation subsists for as long as the amounts due on the importations have not been paid. Thus, it is completely erroneous for the petitioners to say that they were released from their obligations under their bond when Grand Textile withdrew the imported goods without payment of taxes, duties, and charges. From a commonsensical perspective, it may well be asked: why else would the law require a surety when such surety would be bound only if the withdrawal would be regular due to the payment of the required duties, taxes, and other charges?

We note in this regard the rule that a surety is released from its obligation when there is a material alteration of the contract in connection with which the bond is given, such as a change which imposes a new obligation on the promising party, or which takes away some obligation already imposed, or one which changes the legal effect of the original contract and not merely its form. A surety, however, is not released by a change in the contract which does not have the effect of making its obligation more onerous.[16]

We find under the facts of this case no significant or material alteration in the principal contract between the government and the importer, nor in the obligation that the petitioners assumed as sureties. Specifically, the petitioners never assumed, nor were any additional obligation imposed, due to any modification of the terms of importation and the obligations thereunder. The obligation, and one that never varied, is - on the part of the importer , to pay the customs duties, taxes, and charges due on the importation, and on the part of the sureties, to be solidarily bound to the payment of the amounts due on the imported goods upon their withdrawal or upon expiration of the given terms. The petitioners' lack of consent to the withdrawal of the goods, if this is their complaint, is a matter between them and the principal Grand Textile; it is a matter outside the concern of government whose interest as creditor-obligee in the importation transaction is the payment by the importer-obligor of the duties, taxes, and charges due before the importation process is concluded. With respect to the sureties who are there as third parties to ensure that the amounts due are paid, the creditor-obligee's active concern is to enforce the sureties' solidary obligation that has become due and demandable. This matter is further and more fully explored below.

The Need for Notice to Bondsmen

To support the conclusion that they should be released from the bonds they issued, the petitioners argue that upon the issuance and acceptance of the bonds, they became direct parties to the bonded transaction entitled to participate and actively intervene, as sureties, in the handling of the imported articles; that, as sureties, they are entitled to notice of any act of the bond obligee and of the bond principal that would affect the risks secured by the bond; and that otherwise, the door becomes wide open for possible fraudulent conspiracy between the bond obligee and principal to defraud the surety.[17]

In taking these positions, the petitioners appear to misconstrue the nature of a surety relationship, particularly the fact that two types of relationships are involved, that is, the underlying principal relationship between the creditor (government) and the debtor (importer), and the accessory surety relationship whereby the surety binds itself, for a consideration paid by the debtor, to be jointly and solidarily liable to the creditor for the debtor's default. The creditor in this latter relationship accepts the surety's solidary undertaking to pay if the debtor does not pay.[18] Such acceptance, however, does not change in any material way the creditor's relationship with the principal

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debtor nor does it make the surety an active party to the principal creditor-debtor relationship. The contract of surety simply gives rise to an obligation on the part of the surety in relation with the creditor and is a one- way relationship for the benefit of the latter.[19]

In other words, the surety does not, by reason of the surety agreement, earn the right to intervene in the principal creditor-debtor relationship; its role becomes alive only upon the debtor's default, at which time it can be directly held liable by the creditor for payment as a solidary obligor. A surety contract is made principally for the benefit of the creditor-obligee and this is ensured by the solidary nature of the sureties' undertaking.[20] Under these terms, the surety is not entitled as a rule to a separate notice of default,[21] nor to the benefit of excussion,[22] and may be sued separately or together with the principal debtor.[23] The words of this Court in Palmares v. CA[24] are worth noting:

> Demand on the surety is not necessary before bringing the suit against them. On this point, it may be worth mentioning that a surety is not even entitled, as a matter of right, to be given notice of the principal's default. Inasmuch as the creditor owes no duty of active diligence to take care of the interest of the surety, his mere failure to voluntarily give information to the surety of the default of the principal cannot have the effect of discharging the surety. The surety is bound to take notice of the principal's default and to perform the obligation. He cannot complain that the creditor has not notified him in the absence of a special agreement to that effect in the contract of suretyship.

Significantly, nowhere in the petitioners' bonds does it state that prior notice is required to fix the sureties' liabilities. Without such express requirement, the creditor's right to enforce payment cannot be denied as the petitioners became bound as soon as Grand Textile, the principal debtor, defaulted. Thus, the filing of the collection suit was sufficient notice to the sureties of their principal's default.

The petitioners' reliance on Visayan Surety and Insurance Corporation v. Pascual[25] and Aguasin v. Velasquez[26] does not appear to us to be well taken as these cases do not squarely apply to the present case. These cases relate to bonds issued as a requirement for the issuance of writs of replevin. The Rules of Court expressly require that before damages can be claimed against such bonds, notice must be given to the sureties to bind them to the award of damages. No such requirement is evident in this case as neither the Tariff and Customs Code nor the issued bonds require prior notice to sureties.

The petitioners' argument focusing on the additional risks they incur if they cannot intervene in the handling of the warehoused articles must perforce fail in light of what we have said above regarding the nature of their obligation as sureties and the relationships among the parties where a surety agreement exists. We add that the petitioners have effectively waived as against the creditor (the government) any such claim in light of the provision of the bond that "the surety hereon agrees to accept all responsibility jointly and severally for the acts of the principal done in accordance with the terms of this bond."[27] Any such claim including those arising from the withdrawal of the warehoused articles without the payment of the requisite duties, taxes and charges is for the principal and the sureties to thresh out between or among themselves.

Government is Not Bound by Estoppel

As its final point, the petitioners argue that they cannot be held liable for the unpaid customs duties, taxes, and other charges because it is the Bureau of Customs' duty to ensure that the duties and taxes are paid before the imported goods are released from its custody and they cannot be made to pay for the error or negligence of the Bureau's employees in authorizing the unlawful and irregular withdrawal of the goods.

It has long been a settled rule that the government is not bound by the errors committed by its agents. Estoppel does not also lie against the government or any of its agencies arising from unauthorized or illegal acts of public

officers.[28] This is particularly true in the collection of legitimate taxes due where the collection has to be made whether or not there is error, complicity, or plain neglect on the part of the collecting agents.[29] In CIR v. CTA,[30] we pointedly said:

> It is axiomatic that the government cannot and must not be estopped particularly in matters involving taxes. Taxes are the lifeblood of the nation through which the government agencies continue to operate and with which the State effects its functions for the welfare of its constituents. Thus, it should be collected without unnecessary hindrance or delay.

We see no reason to deviate from this rule and we shall not do so now.

WHEREFORE, premises considered, we hereby DENY the petition and AFFIRM the Decision of the Court of Appeals. Costs against the petitioners.

SO ORDERED.

Quisumbing, (Chairperson), Tinga, Reyes, and Leonardo-De Castro,. JJ., concur.

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* Designated as additional member of the Second Division per Special Order No. 504 dated May 15, 2008.

** Designated as additional member of the Second Division per Special Order No. 505 dated May 15, 2008.

[1] In CA G.R. CV. No. 54346, penned by Associate Justice Elvi John Asuncion (dismissed) with Associate Justices Conrado Vasquez and Sergio Pestaño, concurring; r ollo, pp. 24-30.

[2] Id., pp. 31-44.

[3] Id., p. 44.

[4] Section 1904. Irrevocable Domestic Letter of Credit or Bank Guarantee or Warehousing Bonds. - After articles declared in the entry for warehousing shall have been determined, the Collector shall require from the importer, an irrevocable domestic letter of credit, bank guarantee or bond equivalent to the amount of such duties, taxes and other charges conditioned upon the withdrawal of the articles within the period prescribed by section nineteen hundred eight of this Code and for payment of any duties, taxes and other charges to which the articles shall be then subject and upon compliance with all legal requirements regarding their importation.

[5] Fully quoted at pages 7 and 8; infra, at note 15.

[6] Rollo, p. 25.

[7] Id, p. 44.

[8] Id., p. 11.

[9] Supra, at note 4.

[10] INSURANCE CODE, Section 178.

[11] CIVIL CODE, Article 2047.

[12] Garcia v. CA and Lasal Development Corporation, G.R. No. 80201, November 20, 1990, 191 SCRA 493.

[13] Maritime Company of the Philippines v. Reparations Commission, G.R. No. L-29203, July 26, 1971, 40 SCRA 70.

[14] Umali v. Court of Appeals, G.R. No. 89561, September 13, 1960, 189 SCRA 529.

[15] OIC Bond No. C (12) - 00563, Exh. "W" of the Plaintiff, Record, p. 484.

[16] NASSCO v. Torrento, G.R. No. L-21109, June 26, 1967, 20 SCRA 427.

[17] Par. 20 of the Petitioners' Memorandum; rollo, p. 142.

[18] See: Government v. Marcelino Tizon, et al., G.R. No. L-22108, August 30, 1967, 20 SCRA 1182.

[19] De Leon, H., Comments and Cases on Credit Transaction, 2002 ed., p. 234.

[20] CIVIL CODE, Article 1216.

[21] 74 Am. Jur. §35.

[22] Manila Surety & Fidelity Co, Inc. v. Batu Construction & Co., 101 Phil. 494 (1957).

[23] Supra, notes 16 and 20.

[24] G.R. No. 126490, March 31, 1998, 288 SCRA 422, 439.

[25] 85 Phil. 779 (1950).

[26] 88 Phil. 357 (1951).

[27] PhilHome Bond No. 7415378, Exhibit "1" of Defendant, Record, p. 555; OIC Bond No. C(12)-00563, Exhibit "W" of Plaintiff, Record, p. 484.

[28] Republic of the Philippines v. Heirs of Felix Caballero, G.R. No. L-27473, September 30, 1977, 208 SCRA 726.

[29] Caltex Philippines v. COA, G.R. No. 92585, May 8, 1992, 208 SCRA 726.

[30] G.R. No. 106611, July 21, 1994, 243 SCRA 348.

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