

**ASSOCIATED INSURANCE & SURETY COMPANY, INC.,
PLAINTIFF, VS. ISABEL IYA, ADRIANO VALINO AND LUCIA VALINO,
DEFENDANTS.**

G.R. Nos. 10837-38. May 30, 1958

Ponente: FELIX, J.

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FELIX, J.:

Adriano Valino and Lucia A. Valino, husband and wife, were the owners and possessors of a house of strong materials constructed on Lot No. 3, Block No. 80 of the Grace Park Subdivision in Caloocan, Rizal, which they purchased on installment basis from the Philippine Realty Corporation. On November 6, 1951, to enable her to purchase on credit rice from the NARIC, Lucia A. Valino filed a bond in the sum of P11,000.00 (AISCO Bond No. G-971) subscribed by the Associated Insurance & Surety Co., Inc., and as counter-guaranty therefor, the spouses Valino executed an alleged chattel mortgage on the aforementioned house in favor of the surety company, which encumbrance was duly registered with the Chattel Mortgage Register of Rizal on December 6, 1951. It is admitted that at the time said undertaking took place, the parcel of land on which the house is erected was still registered in the name of the Philippine Realty Corporation. Having completed payment on the purchase price of the lot, the Valinos were able to secure on October 18, 1958, a certificate of title in their name (T.C.T. No. 27884). Subsequently, however, or on October 24, 1952, the Valinos, to secure payment of an indebtedness in the amount of P12,000.00, executed a real estate mortgage over the lot and the house in favor of Isabel Iya, which was duly registered and annotated at the back of the certificate of title.

On the other hand, as Lucia A. Valino, failed to satisfy her obligation to the NARIC, the surety company was compelled to pay the same pursuant to the undertaking of the bond. In turn, the surety company demanded reimbursement from the spouses Valino, and as the latter likewise failed to do so, the company foreclosed the chattel mortgage over the house. As a result thereof, a public sale was conducted by the Provincial Sheriff of Rizal on December 26, 1952, wherein the property was awarded to the surety company for P8,000.00, the highest bid received therefor. The surety company then caused the said house to be declared in its name for tax purposes (Tax Declaration No. 25128).

Sometime in July, 1953, the surety company learned of the existence of the real estate mortgage over the lot covered by T.C.T. No. 26884 together with the improvements thereon; thus, said surety company instituted Civil Case No. 2162 of the Court of First Instance of Manila naming Adriano and Lucia Valino and Isabel Iya, the mortgagee, as defendants. The complaint prayed for the exclusion of the residential house from the real estate mortgage in favor of defendant Iya and the declaration and recognition of plaintiff's right to ownership over the same in virtue of the award given by the Provincial Sheriff of Rizal during the public auction held on December 26, 1952. Plaintiff likewise asked the Court to sentence the spouses Valino to pay said surety moral and exemplary damages, attorney's fees and costs. Defendant Isabel Iya filed her answer to the complaint alleging among other things, that in virtue of the real estate mortgage executed by her co-defendants, she acquired a real right over the lot and the house constructed thereon; that the auction sale allegedly conducted by the Provincial

Sheriff of Rizal as a result of the foreclosure of the chattel mortgage on the house was null and void for non-compliance with the form required by law. She, therefore, prayed for the dismissal of the complaint and annulment of the sale made by the Provincial Sheriff. She also demanded the amount of P5,000.00 from plaintiff as counterclaim, the sum of P5,000.00 from her co-defendants as cross-claim, for attorney's fees and costs.

Defendants spouses in their answer admitted some of the averments of the complaint and denied the others. They, however, prayed for the dismissal of the action for lack of cause of action, it being alleged that plaintiff was already the owner of the house in question, and as said defendants admitted this fact, the claim of the former was already satisfied.

On October 29, 1953, Isabel Iya filed another civil action against the Valinos and the surety company (Civil Case No. 2504 of the Court of First Instance of Manila) stating that pursuant to the contract of mortgage executed by the spouses Valino on October 24, 1952, the latter undertook to pay a loan of P12,000.00 with interest at 12% per annum or P120.00 a month, which indebtedness was payable in 4 years, extendible for only one year; that to secure payment thereof, said defendants mortgaged the house and lot covered by T.C.T. No. 27884 located at No. 67 Baltazar St., Grace Park Subdivision, Caloocan, Rizal; that the Associated Insurance & Surety Co., Inc., was included as a party defendant because it claimed to have an interest, on the residential house also covered by said mortgage; that it was stipulated in the aforesaid real estate mortgage that default in the payment of the interest agreed upon would entitle the mortgagee to foreclose the same even before the lapse of the 4-year period; and as defendant spouses had allegedly failed to pay the interest for more than 6 months, plaintiff prayed the Court to order said defendants to pay the sum of P12,000.00 with interest thereon at 12% per annum from March 25, 1953, until fully paid; for an additional sum equivalent to 20% of the total obligation as damages, and for costs. As an alternative in case such demand may not be met and satisfied plaintiff prayed for a decree of foreclosure of the land, building and other improvements thereon to be sold at public auction and the proceeds thereof applied to satisfy the demands of plaintiff; that the Valinos, the surety company and any other person claiming interest on the mortgaged properties be barred and foreclosed of all rights, claims or equity of redemption in said properties; and for deficiency judgment in case the proceeds of the sale of the mortgaged property would be insufficient to satisfy the claim of plaintiff.

Defendant surety company, in answer to this complaint insisted on its right over the building, arguing that as the lot on which the house was constructed did not belong to the spouses at the time the chattel mortgage was executed, the house might be considered only as a personal property and that the encumbrance thereof and the subsequent foreclosure proceedings made pursuant to the provisions of the Chattel Mortgage Law were proper and legal. Defendant therefore prayed that said building be excluded from the real estate mortgage and its right over the same be declared superior to that of plaintiff, for damages, attorney's fees and costs.

Taking side with the surety company, defendant spouses admitted the due execution of the mortgage upon the land but assailed the allegation that the building was included thereon, it being contended that it was already encumbered in favor of the surety company before the real estate mortgage was executed, a fact made known to plaintiff during the preparation of said contract and to which the latter offered no objection. As a special defense, it was asserted that the action was premature because the contract was for a period of 4 years, which had not yet elapsed.

The two cases were jointly heard upon agreement of the parties, who submitted the same on a stipulation of facts, after which the Court rendered judgment dated March 8, 1956, holding that the chattel mortgage in favor of the Associated Insurance & Surety Co., Inc., was preferred and superior over the real estate mortgage subsequently executed in favor of Isabel Iya. It was ruled that as the Valinos were not yet the registered owner of the land on which the building in question was constructed at the time the first encumbrance was made, the building then was

still a personalty and a chattel mortgage over the same was proper. However, as the mortgagors were already the owners of the lot at the time the contract with Isabel Iya was entered into, the building was transformed into a real property and the real estate mortgage created thereon was likewise adjudged as proper. It is to be noted in this connection that there is no evidence on record to sustain the allegation of the spouses Valino that at the time they mortgaged their house and lot to Isabel Iya, the latter was told or knew that part of the mortgaged property, i.e., the house, had previously been mortgaged to the surety company.

The residential building was, therefore, ordered excluded from the foreclosure prayed for by Isabel Iya, although the latter could exercise the right of a junior encumbrancer. So the spouses Valino were ordered to pay the amount demanded by said mortgagee or in their default to have the parcel of land subject of the mortgage sold at public auction for the satisfaction of Iya's claim.

There is no question as to appellant's right over the land covered by the real estate mortgage; however, as the building constructed thereon has been the subject of 2 mortgages ; controversy arise as to which of these encumbrances should receive preference over the other. The decisive factor in resolving the issue presented by this appeal is the determination of the nature of the structure litigated upon, for where it be considered a personalty, the foreclosure of the chattel mortgage and the subsequent sale thereof at public auction, made in accordance with the Chattel Mortgage Law would be valid and the right acquired by the surety company therefrom would certainly deserve prior recognition; otherwise, appellant's claim for preference must be granted. The lower Court, deciding in favor of the surety company, based its ruling on the premise that as the mortgagors were not the owners of the land on which the building is erected at the time the first encumbrance was made, said structure partook of the nature of a personal property and could properly be the subject of a chattel mortgage. We find reason to hold otherwise, for as this Court, defining the nature or character of a building, has said:

"* * * while it is true that generally, real estate connotes the land and the building constructed thereon, it is obvious that the inclusion of the building, separate and distinct from the land, in the enumeration of what may constitute real properties (Art. 415, new Civil Code) could only mean one thing-that a building is by itself an IMMOVABLE PROPERTY, * * *. Moreover, and in view of the absence of any specific provision to the contrary, a building is an immovable property irrespective of whether or not said structure and the land on which it is adhered to belong to the same owner." (Lopez vs. Orosa, G.R. Nos. L-10817 - L-10818, Feb. 28, 1958).

A building certainly cannot be divested of its character of a realty by the fact that the land on which it is constructed belongs to another. To hold it the other way, the possibility is not remote that it would result in confusion, for to cloak the building with ,an uncertain status made dependent on the ownership of the land, would create a situation where a permanent fixture changes its nature or character as the ownership of the land changes hands. In the case at bar, as personal properties could only be the subject of a chattel mortgage (Section 1, Act 3952) and as obviously the structure in question is not one, the execution of the chattel mortgage covering said building is clearly invalid and a nullity. While it is true that said document was correspondingly registered in the Chattel Mortgage Register of Rizal, this act produced no effect whatsoever for where the interest conveyed is in the nature of a real property, the registration of the document in the registry of chattels is merely a futile act. Thus, the registration of the chattel mortgage of a building of strong materials produce no effect as far as the building is concerned (Leung Yee vs. Strong Machinery Co., 37 Phil., 644). Nor can we give any consideration to the contention of the surety that it has acquired ownership over the property in question by reason of the sale conducted by the Provincial Sheriff of Rizal, for as this Court has aptly pronounced:

"A mortgage creditor who purchases real properties at an extra-judicial foreclosure sale thereof by virtue of a chattel mortgage constituted in his favor, which mortgage has been declared null and void with respect to said real properties, acquires no right thereto by virtue of said sale" (De la Riva vs. Ah Kee, 60 Phil., 899).

Wherefore, the portion of the decision of the lower Court in these two cases appealed from holding the rights of the surety company over the building superior to that of Isabel Iya and excluding the building from the foreclosure prayed for by the latter is reversed and appellant Isabel Iya's right to foreclose not only the land but also the building erected thereon is hereby recognized, and the proceeds of the sale thereof at public auction (if the land has not yet been sold), shall be applied to the unsatisfied judgment in favor of Isabel Iya. This decision however is without prejudice to any right that the Associated Insurance & Surety Co., Inc., may have against the spouses Adriano and Lucia Valino on account of the mortgage of said building they executed in favor of said surety company. Without pronouncement as to costs. It is so ordered.

Paras, C.J., Bengzon, Montemayor, Reyes, A., Bautista Angelo, Labrador, Concepcion, Reyes, J.B.L., and Endencia, JJ., concur.

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