

FIRST DIVISION

[G.R. No. 175350, June 13, 2012]

**EQUITABLE BANKING CORPORATION, PETITIONER, VS. SPECIAL
STEEL PRODUCTS, INC. AND AUGUSTO L. PARDO,
RESPONDENTS.**

D E C I S I O N

DEL CASTILLO, J.:

A crossed check with the notation "account payee only" can only be deposited in the named payee's account. It is gross negligence for a bank to ignore this rule *solely* on the basis of a third party's oral representations of having a good title thereto.

Before the Court is a Petition for Review on *Certiorari* of the October 13, 2006 Decision of the Court of Appeals (CA) in CA-G.R. CV No. 62425. The dispositive portion of the assailed Decision reads:

WHEREFORE, premises considered, the May 4, 1998 Decision of the Regional Trial Court of Pasig City, Branch 168, in Civil Case No. 63561, is hereby **AFFIRMED**.

SO ORDERED.^[1]

Factual Antecedents

Respondent Special Steel Products, Inc. (SSPI) is a private domestic corporation selling steel products. Its co-respondent Augusto L. Pardo (Pardo) is SSPI's President and majority stockholder.^[2]

International Copra Export Corporation (Interco) is its regular customer.^[3]

Jose Isidoro^[4] Uy, *alias* Jolly Uy (Uy), is an Interco employee, in charge of the purchasing department, and the son-in-law of its majority stockholder.^[5]

Petitioner Equitable Banking Corporation (Equitable or bank) is a private domestic corporation engaged in banking^[6] and is the depository bank of Interco and of Uy.

In 1991, SSPI sold welding electrodes to Interco, as evidenced by the following sales invoices:

Sales Invoice No. 65042 dated February 14, 1991 for P325,976.34^[7]

Sales Invoice No. 65842 dated April 11, 1991 for P345,412.80^[8]

Sales Invoice No. 65843 dated April 11, 1991 for P313,845.84^[9]

The due dates for these invoices were March 16, 1991 (for the first sales invoice) and May 11, 1991 (for the others). The invoices provided that Interco would pay interest at the rate of 36% per annum in case of delay.

In payment for the above welding electrodes, Interco issued three checks payable to the order of SSPI on July 10, 1991,^[10] July 16, 1991,^[11] and July 29, 1991.^[12] Each check was crossed with the notation "account payee only" and was drawn against Equitable. The records do not identify the signatory for these three checks, or explain how Uy, Interco's purchasing officer, came into possession of these checks.

The records only disclose that Uy presented each crossed check to Equitable on the day of its issuance and claimed that he had good title thereto.^[13] He demanded the deposit of the checks in his personal accounts in Equitable, Account No. 18841-2 and Account No. 03474-0.^[14]

Equitable acceded to Uy's demands on the assumption that Uy, as the son-in-law of Interco's majority stockholder,^[15] was acting pursuant to Interco's orders. The bank also relied on Uy's status as a valued client.^[16] Thus, Equitable accepted the checks for deposit in Uy's personal accounts^[17] and stamped "ALL PRIOR ENDORSEMENT AND/OR LACK OF ENDORSEMENT GUARANTEED" on their dorsal portion.^[18] Uy promptly withdrew the proceeds of the checks.

In October 1991, SSPI reminded Interco of the unpaid welding electrodes, amounting to P985,234.98.^[19] It reiterated its demand on January 14, 1992.^[20] SSPI explained its immediate need for payment as it was experiencing some financial crisis of its own. Interco replied that it had already issued three checks payable to SSPI and drawn against Equitable. SSPI denied receipt of these checks.

On August 6, 1992, SSPI requested information from Equitable regarding the three checks. The bank refused to give any information invoking the confidentiality of deposits.^[21]

The records do not disclose the circumstances surrounding Interco's and SSPI's eventual discovery of Uy's scheme. Nevertheless, it was determined that Uy, not SSPI, received the proceeds of the three checks that were payable to SSPI. Thus, on June 30, 1993 (twenty-three months after the issuance of the three checks), Interco finally paid the value of the three checks to SSPI, plus a portion of the accrued interests. Interco refused to pay the entire accrued interest of P767,345.64 on the ground that it was not responsible for the delay. Thus, SSPI was unable to collect P437,040.35 (at the contracted rate of 36% per annum) in interest income.^[22]

SSPI and its president, Pardo, filed a complaint for damages with application for a writ of preliminary attachment against Uy and Equitable Bank. The complaint alleged that the three crossed checks, all payable to the order of SSPI and with the notation "account payee only," could be deposited and encashed by SSPI only. However, due to Uy's fraudulent representations, and Equitable's indispensable connivance or gross negligence, the restrictive nature of the checks was ignored and the checks were deposited in Uy's account. Had the defendants not diverted the

three checks in July 1991, the plaintiffs could have used them in their business and earned money from them. Thus, the plaintiffs prayed for an award of actual damages consisting of the unrealized interest income from the proceeds of the checks for the two-year period that the defendants withheld the proceeds from them (from July 1991 up to June 1993).^[23]

In his personal capacity, Pardo claimed an award of P3 million as moral damages from the defendants. He allegedly suffered hypertension, anxiety, and sleepless nights for fear that the government would charge him for tax evasion or money laundering. He maintained that defendants' actions amounted to money laundering and that it unfairly implicated his company in the scheme. As for his fear of tax evasion, Pardo explained that the Bureau of Internal Revenue might notice a discrepancy between the financial reports of Interco (which might have reported the checks as SSPI's income in 1991) and those of SSPI (which reported the income only in 1993). Since Uy and Equitable were responsible for Pardo's worries, they should compensate him jointly and severally therefor.^[24]

SSPI and Pardo also prayed for exemplary damages and attorney's fees.^[25]

In support of their application for preliminary attachment, the plaintiffs alleged that the defendants are guilty of fraud in incurring the obligation upon which the action was brought and that there is no sufficient security for the claim sought to be enforced in this action.^[26]

The trial court granted plaintiffs' application.^[27] It issued the writ of preliminary attachment on September 20, 1993,^[28] upon the filing of plaintiffs' bond for P500,000.00. The sheriff served and implemented the writ against the personal properties of both defendants.^[29]

Upon Equitable's motion and filing of a counter-bond, however, the trial court eventually discharged the attachment^[30] against it.^[31]

Equitable then argued for the dismissal of the complaint for lack of cause of action. It maintained that interest income is due only when it is expressly stipulated in writing. Since Equitable and SSPI **did not enter into any contract**, Equitable is not liable for damages, in the form of unobtained interest income, to SSPI.^[32] Moreover, SSPI's acceptance of Interco's payment on the sales invoices is a **waiver or extinction** of SSPI's cause of action based on the three checks.^[33]

Equitable further argued that it is not liable to SSPI because it accepted the three crossed checks in good faith.^[34] Equitable averred that, due to Uy's close relations with the drawer of the checks, the bank had basis to assume that the drawer authorized Uy to countermand the original order stated in the check (that it can only be deposited in the named payee's account). Since only Uy is responsible for the fraudulent conversion of the checks, he should reimburse Equitable for any amounts that it may be made liable to plaintiffs.^[35]

The bank counter-claimed that SSPI is liable to it in damages for the wrongful and malicious attachment of Equitable's personal properties. The bank maintained that

SSPI knew that the allegation of fraud against the bank is a falsehood. Further, the bank is financially capable to meet the plaintiffs' claim should the latter receive a favorable judgment. SSPI was aware that the preliminary attachment against the bank was unnecessary, and intended only to humiliate or destroy the bank's reputation.^[36]

Meanwhile, Uy answered that the checks were negotiated to him; that he is a holder for value of the checks and that he has a good title thereto.^[37] He did not, however, explain how he obtained the checks, from whom he obtained his title, and the value for which he received them. During trial, Uy did not present any evidence but adopted Equitable's evidence as his own.

Ruling of the Regional Trial Court ^[38]

The RTC clarified that SSPI's cause of action against Uy and Equitable is for quasi-delict. SSPI is not seeking to enforce payment on the undelivered checks from the defendants, but to recover the damage that it sustained from the wrongful non-delivery of the checks.^[39]

The crossed checks belonged solely to the payee named therein, SSPI. Since SSPI did not authorize anyone to receive payment in its behalf, Uy clearly had no title to the checks and Equitable had no right to accept the said checks from Uy. Equitable was negligent in permitting Uy to deposit the checks in his account without verifying Uy's right to endorse the crossed checks. The court reiterated that banks have the duty to scrutinize the checks deposited with it, for a determination of their genuineness and regularity. The law holds banks to a high standard because banks hold themselves out to the public as experts in the field. Thus, the trial court found Equitable's explanation regarding Uy's close relations with the drawer unacceptable.^[40]

Uy's conversion of the checks and Equitable's negligence make them liable to compensate SSPI for the actual damage it sustained. This damage consists of the income that SSPI failed to realize during the delay.^[41] The trial court then equated this unrealized income with the interest income that SSPI failed to collect from Interco. Thus, it ordered Uy and Equitable to pay, jointly and severally, the amount of P437,040.35 to SSPI as actual damages.^[42]

It also ordered the defendants to pay exemplary damages of P500,000.00, attorney's fees amounting to P200,000.00, as well as costs of suit.^[43]

The trial court likewise found merit in Pardo's claim for moral damages. It found that Pardo suffered anxiety, sleepless nights, and hypertension in fear that he would face criminal prosecution. The trial court awarded Pardo the amount of P3 million in moral damages.^[44]

The dispositive portion of the trial court's Decision reads:

WHEREFORE, judgment is hereby rendered in favor of plaintiffs Special Steel Products, Inc., and Augusto L. Pardo and against defendants

Equitable Banking Corporation [and] Jose Isidoro Uy, alias "Jolly Uy," ordering defendants to jointly and severally pay plaintiffs the following:

1. P437,040.35 as actual damages;
2. P3,000,000.00 as moral damages to Augusto L. Pardo;
3. P500,000.00 as exemplary damages;
4. P200,000.00 as attorney's fees; and
5. Costs of suit.

Defendant EBC's counterclaim is hereby DISMISSED for lack of factual and legal basis.

Likewise, the crossclaim filed by defendant EBC against defendant Jose Isidoro Uy and the crossclaim filed by defendant Jose Isidoro Uy against defendant EBC are hereby DISMISSED for lack of factual and legal basis.

SO ORDERED.

Pasig City, May 4, 1998.^[45]

The trial court denied Equitable's motion for reconsideration in its Order dated November 19, 1998.^[46]

Only Equitable appealed to the CA,^[47] reiterating its defenses below.

Appealed Ruling of the Court of Appeals^[48]

The appellate court found no merit in Equitable's appeal.

It affirmed the trial court's ruling that SSPI had a cause of action for quasi-delict against Equitable.^[49] The CA noted that the three checks presented by Uy to Equitable were crossed checks, and strictly made payable to SSPI only. This means that the checks could only be deposited in the account of the named payee.^[50] Thus, the CA found that Equitable had the responsibility of ensuring that the crossed checks are deposited in SSPI's account only. Equitable violated this duty when it allowed the deposit of the crossed checks in Uy's account.^[51]

The CA found factual and legal basis to affirm the trial court's award of moral damages in favor of Pardo.^[52]

It likewise affirmed the award of exemplary damages and attorney's fees in favor of SSPI.^[53]

Issues

1. Whether SSPI has a cause of action against Equitable for quasi-delict;
2. Whether SSPI can recover, as actual damages, the stipulated 36% per annum interest from Equitable;