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**RIGHT OF THE DRAWEE BANK TO RECOVER FROM THE  
COLLECTING BANK THE AMOUNT PAID ON A MATERIALLY  
ALTERED CHECK NOT RETURNED WITHIN THE "24-HOUR CLEAR-  
ING PERIOD"**

**Introduction**

Article 8 of the Civil Code provides that: "Judicial decisions applying or interpreting the laws or the Constitution shall form a part of the legal system of the Philippines." This is of course the statutory expression of the very well-known doctrine of *stare decisis*, the reason for such doctrine being to preserve the certainty, stability and symmetry of our jurisprudences [L. D. Wilcutt & Sons Co. v. Driscoll<sup>1</sup>]. Sadly, however, court decisions even by the highest one, in certain cases are unsound and unrealistic, because at times the parties-litigants themselves do not present the facts and the arguments in support of their cases, as properly as they should. For this reason some jurists have remarked that blind adherence to the doctrine of the *stare decisis* can lead to perpetuation of erroneous rulings.

**The Ruling Subject of this Article**

Late last year, the Supreme Court rendered its decision in the case of *Metropolitan Bank and Trust Company v. The First National City Bank and the Court of Appeals*<sup>2</sup>, reversing the decision of the Court of Appeals, which affirmed the decision of the Court of First Instance of Manila in favor of the First National City Bank. The decision of the Supreme Court merely reiterated its previous rulings in the case of *Hongkong and Shanghai Banking Corporation v. People's Bank and Trust Company*.

The facts of the earlier case of *Hongkong & Shanghai Bank vs. People's Bank and Trust Company* are as follows:

"On March 8, 1965, the Philippine Long Distance Telephone Company drew the check \* \* \* on the Hongkong & Shanghai Banking Corporation and in favor of the same bank in the sum of P14,608.05. This check was sent by mail to the payee. Somehow or other, the check fell in the hands of a certain Florentino Changco, who was able to erase the name of the payee Bank and instead typed his own name

on the check. Four days before, Changco had opened a current account with Defendant People's Bank and Trust Company and on March 16, 1965, he deposited the altered check in his name. This check was presented by the People's Bank for clearing wherein the People's Bank made the following indorsement: 'For clearance, clearing office. All prior endorsements and / or lack of endorsements guaranteed. People's Bank and Trust Company.' The check was duly cleared by the Hongkong Shanghai Bank, so that the People's Bank credited Changco with the amount of the check. Beginning March 17, 1965, Changco began to withdraw from his account and on March 31, 1965 he closed his account. In the meantime, the cancelled check went the route of the regular routine and on April 12, 1965 it was returned to the Philippine Long Distance Telephone Company when the alteration in the name of the payee was discovered. On that same date, People's Bank was notified of the alteration, so that the Hongkong Shanghai Bank requested People's Bank to refund to it the sum of P14,608.05 which had been previously credited by Plaintiff Bank in favor of Defendant Bank. Upon its refusal to do so, this case has been filed."<sup>4</sup>

On the basis of these facts the Supreme Court ruled as follows:

"The complaint was therefore dismissed, resulting in this appeal to us on a question of law, which, as set forth in the principal assigned error is predicated on the inapplicability of the 24-hour clearing house rule of the Central Bank. Plaintiff does not deny that in Republic vs. Equitable Banking Corporation, this Honorable Court, through the then Justice, now Chief Justice Concepcion, applied the '24-hour' clearing house rule issued by the Central Bank in accordance with its rule-making authority. As noted in the aforesaid decision, its adoption came after a conference with representatives and officials of different banking institutions in the Philippines. It is embodied in section 4, subsection (c) of Circular No. 9 of the Central Bank dated February 17, 1949, as amended by the then Governor of the Central Bank on June 4, 1949, and reads thus: 'items which should be returned for any reason whatsoever shall be returned directly to the bank, institution or entity from which the item was received. For this purpose, the Receipt for Returned Checks (Cash Form No. 9) should be used. The original and duplicate copies of said Receipt shall be given to the bank, institution or entity which returned the items and the triplicate copy should be retained by the bank, institution or entity whose demand is being returned. At the following clearing, the original of the Receipt for Returned Checks shall be presented through the Clearing Office as a demand against the bank, institution or entity whose item has been returned. Nothing in this section shall prevent the returned items from being settled by direct reimbursement to the bank, institution or entity returning the items. All items cleared at 11:00 o'clock a.m. shall be returned not later than 2:00 o'clock p.m. on the same day

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*and all items cleared at 3:00 o'clock p.m. shall be returned not later than 8:30 a.m. of the following business day, except for items cleared on Saturday which may be returned not later than 8:30 of the following day.* (Italics supplied) It is apparent from the above that the attempted distinction sought to be made by plaintiff to the effect that it refers to forged, but not to altered checks is not warranted. The circular is clear and comprehensive; the facts of the present case fall within it. The lower court acted correctly in relying on the doctrine announced in the above Republic v. Equitable Banking Corporation decision.<sup>5</sup>

In the later Metropolitan Bank case, the facts are as follows:

"On August 25, 1964, Check No. 7166 dated July 8, 1964 -- for P50,000.00, payable to CASH, drawn by Joaquin Cunanan & Company on First National City Bank (FNCB for brevity) was deposited with Metropolitan Bank and Trust Company (Metro Bank for short) by a certain Salvador Sales. Earlier that day, Sales had opened a current account with Metro Bank depositing P500.00 in cash. Metro Bank immediately sent the cash check to the Clearing House of the Central Bank with the following words stamped at the back of the check:

"Metropolitan Bank and Trust Company Cleared (illegible) office. All prior endorsements and or lack endorsements Guaranteed."

"The check was cleared the same day. Private respondent paid petitioner through clearing the amount of P50,000.00, and Sales was credited with the said amount in his deposit with Metro Bank.

"On August 26, 1964, Sales made his first withdrawal of P480.00 from his current account. On August 28, 1964, he withdrew P32, 100.00 Then on August 31, 1964, he withdrew the balance of P17, 920.00 and closed his account with Metro Bank.

"On September 3, 1964, or nine (9) days later, FNCB returned cancelled Check No. 7166 to drawer Joaquin Cunanan & Company, together with the monthly statement of the company's account with FNCB. That same day, the company notified FNCB that the check had been altered. The actual amount of P50.00 was raised to P50, 000.00, and over the name of the payee, Manila Polo Club, was superimposed the word CASH.

"FNCB notified Metro Bank of the alteration by telephone, confirming it the same day with a letter, which was received by Metro Bank on the following day, September 4, 1964.

"On September 10, 1964, FNCB wrote Metro Bank asking for reimbursement of the amount of P50,000.00. The latter did not oblige so that FNCB reiterated its request on September 29, 1964. Metro Bank was adamant in its refusal.

"On June 29, 1965, FNCB filed in the Court of First Instance of Manila, Branch VIII, Civil Case No. 61488 against Metro Bank for recovery of the amount of P50,000.00.

"On January 27, 1975, the Trial Court rendered its Decision ordering Metro Bank to reimburse FNCB the amount of P50,000.00 with legal rate of interest from June 25, 1965 until fully paid, to pay attorney's fees of P5,000.00, and costs.

"Petitioner appealed said Decision to the Court of Appeals (CA-G. R. No. 57129-R). On August 29, 1980, respondent Appellate Court affirmed in toto the judgment of the Trial Court."<sup>6</sup>

The Supreme Court, following its ruling in the earlier case, stated that:

"The facts of this case fall within said Circular. Under the procedure prescribed, the drawee bank receiving the check for clearing from the Central Bank Clearing House must return the check to the collecting bank within the 24-hour period if the check is defective for any reason.

"Metro Bank invokes this 24-hour regulation of the Central Bank as its defense. FNCB on the other hand, relies on the guarantee of all previous endorsements made by Metro Bank which guarantee had allegedly misled FNCB into believing that the check in question was regular and the payee's endorsements genuine; as well as on "the general rule of law founded on equity and justice that a drawee or payor bank which in good faith pays the amount of materially altered check to the holder thereof is entitled to recover its payment from the said holder, even if he be an innocent holder.

"The validity of the 24-hour clearing house regulation has been upheld by this Court in Republic vs. Equitable Banking Corporation, 10 SCRA 8 (1964). As held therein, since both parties are part of our banking system, and both are subject to the regulation of the Central Bank, they are bound by the 24-hour clearing house rule of the Central Bank.

"In this case, the check was not returned to Metro Bank in accordance with the 24-hour clearing house period, but was cleared by FNCB. Failure of FNCB, therefore, to call the attention of Metro Bank to the

alteration of the check in question until after the lapse of nine days, negates whatever right it might have had against Metro Bank in the light of the said Central Bank Circular. Its remedy lies not against Metro Bank, but against the party responsible for changing the name of the payee and the amount on the face of the check.”<sup>7</sup>

The pronouncements of the Supreme Court in the above-quoted two cases, are synthesized as follows:

1. The failure of a drawee bank to return a check bearing a material alteration of the name of the payee and of the amount within 24 hours after the check was sent for clearing deprives the drawee bank of its right to recover the amount of the check from the collecting bank in view of Sec. 4 (c) of the Clearing Regulations in force at the time of the occurrence of the facts of the case;

2. The remedy of the drawee bank under such a situation is against the parties responsible for the alteration of the name of the payee and of the amount of the check; and

3. The guaranty of “all prior indorsements and or lack of indorsements” stamped by the collecting bank at the back of the check sent for clearing is actionable only by the drawee bank within the 24-hour clearing period. Once the 24-hour clearing period is over, the liability of the collecting bank on such guaranty “of all prior indorsements and / or lack of indorsements” ceases.

When the Motion for Reconsideration of the private respondent, First National City Bank, in the Metropolitan Bank case was pending in the Supreme Court, the Philippine Clearing House Corporation through the writer, as its Legal Counsel, filed a Motion for Leave to Comment on the Decision of the Honorable Supreme Court sought to be reconsidered by the private respondent. Unfortunately, the motion was denied. So the views therein stated were never ventilated. This article is a restatement, with minor revisions, of the comments which this writer as Legal Counsel of the Philippine Clearing House Corporation, would have filed had the Supreme Court granted him leave to do so.

#### History of the Application of Section 4 Par. (C) of the Clearing Regulation, C. B. Circular No. 9 Series of 1949

As can be seen, the two cases above discussed involved the interpretation of Sec. 4 (c) of C. B. Circular No. 9 Series of 1949, otherwise known as the Clearing Regulations. To appreciate fully the rulings in the two cases, it is necessary to trace the history of the application of this particular provision of the Clearing Regulation.

The very first case in which the Supreme Court applied this particular provision of the Clearing Regulation was in the case of *Republic of the Philippines vs. Equitable Banking Corporation*<sup>8</sup>, which was relied upon

both by the *Hongkong & Shanghai Bank* and the *Metropolitan Bank* cases as precedent for the particular ruling being commented on.

The facts in *Republic vs. Equitable Banking Corporation* are as follows:

“The four (4) warrants involved therein were deposited with the Equitable Bank by persons known thereto as its depositors or customers, namely, Robert Wong, Lu Chiu Kau and Chung Ching; that, in due course, the Equitable Bank cleared said warrants, thru the Clearing Office, then collected the corresponding amounts from the Treasurer and thereafter credited said amounts to the accounts of the respective depositors; that on January 15, 1953, the Treasurer notified the Equitable Bank of the alleged defect of said warrants and demanded reimbursement of the amounts thereof; and that this demand was rejected by the Equitable Bank. Hence, the institution of G. R. No. L-15-895 (Civil Case No. 19599 of the Court of First Instance of Manila), against the PI Bank, for the recovery of P342,767.63, and of G. R. No. L-15894 (Civil Case No. 19600 of the Court of First Instance of Manila), against the Equitable Bank for the recovery of P17,100.00”<sup>9</sup>

The defendant Equitable Banking Corporation contended that since the National Treasury did not return the warrants “within the 24-hour clearing period” it could not anymore be allowed to return the warrants and consequently cannot also recover their amounts.

The particular provision of the Clearing Regulation relied upon by the Equitable Banking Corporation, Sec. 4 (c) of C. B. Circular No. 9, Series of 1949 and copied verbatim in the decision, reads:

“Items which should be returned for any reason whatsoever shall be returned directly to the bank, institution or entity from which the item was received.”<sup>9a</sup> — For this purpose, the Receipt for Returned Checks (Cash Form No. 9) should be used. The original and duplicate copies of said Receipt shall be given to the bank, institution or entity which returned the items and the triplicate copy should be retained by the bank, institution or entity whose demand is being returned. At the following clearing, the original of the Receipt for Returned Checks shall be presented through the Clearing Office as a demand against the bank, institution or entity whose item has been returned. Nothing in this section shall prevent the returned items from being settled by direct reimbursement to the bank, institution or entity returning the items. *All items cleared at 11:00 o'clock shall be returned not later than 2:00 o'clock p.m. on the same day and all items cleared at 3:00 o'clock p.m. shall be returned not later than 8:30 a.m. of the following business day, except for items cleared on Saturday which may be returned not later than 8:30 of the following day.*” (Italics supplied)<sup>10</sup>

The National Treasury contended that it was not bound by this rule because it was not a bank and that the National Treasurer had objected to the application of this rule to his office. The Supreme Court rejected this argument saying:

"This contention, however, is untenable for, admittedly, the Treasury is a member of the aforementioned Clearing Office and Exh. A clearly shows that the former 'has agreed to clear its clearable items through' the latter 'subject to the rules and regulations of the Central Bank.' Besides, the above-quoted rule applies not only to banks, but, also, to the institutions and entities therein alluded to. Then, too, the opposition of the Treasurer to the '24-hour clearing house rule' is not sufficient to exempt the Treasury from the operation thereof." (Words in parenthesis supplied)<sup>11</sup>

The true rationale of the decision in this case, however, is stated by our Supreme Court as follows:

"At any rate, the aforementioned twenty-eight (28) warrants were cleared and paid by the Treasurer, in view of which the PI Bank and the Equitable Bank credited the corresponding amounts to the respective depositors of the warrants and then honored their checks for said amounts. Thus, the Treasury had not only been negligent in clearing its own warrant, but had, also, thereby induced the PI Bank and the Equitable Bank to pay the amounts thereof to said depositors. The gross nature of the negligence of the Treasury becomes more apparent when we consider that each one of the twenty-four (24) warrants involved in G. R. No. L-15895 was for over P5,000.00, and, hence beyond the authority of the auditor of the Treasury — whose signature thereon had been forged — to approve. In other words, the irregularity of said warrants was apparent on the face thereof, from the viewpoint of the Treasury. Moreover, the same had not advertised the loss of genuine forms of its warrants. Neither had the PI Bank nor the Equitable Bank been informed of any irregularity in connection with any of the warrants involved in these two (2) cases, until after December 23, 1952 — or after the warrants had been cleared and honored — when the Treasury gave notice of the forgeries adverted to above. As a consequence, the loss of the amounts thereof is mainly imputable to acts and omissions of the Treasury, for which the PI Bank and the Equitable Bank should not and cannot be penalized."<sup>12</sup>

The facts of the Equitable Banking Corporation case above narrated clearly show that the defects of the warrants involved were the following: 1) the drawers' signatures were forged; and (2) amounts were far in excess of the authority of the officers whose purported signatures appeared in them. These defects only the National Treasury was in a position and bound to notice or discover. Hence, its failure to notice

or discover these defects and return the warrants within the "24-hour clearing period" was clear negligence on its part. Because of such negligence the collecting banks, the Bank of the Philippine Islands and Equitable Banking Corporation were induced to credit the accounts of their depositors with the amounts of the warrants and then honor their checks for those amounts.

The conclusion of the Supreme Court in this Equitable Banking Corporation case was justified not only by the then peculiar wording of the particular Clearing Regulation involved in that case, Sec. 4 (c) of C. B. Circular No. 9 dated February 17, 1949 as amended on June 4, 1949, which required that: "Item which should be returned for any reason whatsoever shall be returned directly to the bank, institution or entity from which the items was received," but also by the fact that the defect of the warrants which the National Treasury failed to return "within the 24-hour clearing period" were defects which only the National Treasury was in a position and was bound to discover within the "24-hour clearing period."

The case of Republic of the Philippines vs. Equitable Banking Corporation cannot properly be the precedent for the rulings in the cases of Hongkong & Shanghai Bank and Metropolitan Bank.

The decision in the case of Republic vs. Equitable Banking Corporation can hardly be considered as correct precedent for the rulings laid down by the Supreme Court in the case of Hongkong & Shanghai Bank vs. People's Bank and Trust Company, because Section 4 (c) of C. B. Circular No. 9 was amended on January 30, 1962 by C. B. Circular No. 138 to read as follows:

*"SECTION 4. Clearing Procedure  
(c) Procedure for Returned Items*

Items which should be returned for any reason whatsoever shall be delivered to and received through the Clearing Office in special red envelopes and shall be considered and accounted as debits to the banks to which the items are returned. Nothing in this section shall prevent the returned items from being settled by direct reimbursement to the bank, institution or entity returning the items. All items cleared during both deliveries, shall be returned not later than 9:00 o'clock A. M. on the following business day.

"Missorts or items misdirected through Clearing shall be returned at the next scheduled clearing in special yellow envelopes and shall be considered and accounted as debits to the Bank which had misdirected the items." (Underscored Supplied)

It will be noted from the underscored portion in the above-quoted provision of the Clearing House Rule that the amended provision requires the item to be returned for any reason whatsoever "to and received through the Clearing Office" of the Central Bank, not later than 9 o'clock a.m. on the following business day instead of requiring said return of the cleared items for any reason whatsoever "directly to the bank, institution or entity from which said item was received", as provided in the original circular. Unfortunately, the Supreme Court did not notice the change in wording when it rendered its decision in the case of *Hongkong & Shanghai Bank vs. People's Bank and Trust Company*, the facts of which occurred in 1965, long after the above-quoted amendment had already been made. Thus, in the *Hongkong and Shanghai Bank* case (obviously because counsel for the Hongkong and Shanghai Bank did not point out to the court that the original provision of Section 4 (c) of C. B. Circular No. 9, Series of 1949 had already been amended) the Supreme Court merely copied verbatim<sup>13</sup> the original provision which was the subject matter of and quoted in full<sup>14</sup> in the decision of the *Republic vs. Equitable Banking Corporation* case. The facts of the *Equitable Banking Corporation* case occurred in 1952, and of course had to be governed by the provision of Sec. 4 (c) of C. B. Circular No. 9 Series of 1949 as originally worded.

It is not unreasonable to suppose that the Central Bank adopted the amendment at the instance of the National Treasury which had by then already lost the case of the *Republic vs. Equitable Banking Corporation* in the Court of First Instance of Manila. (As a matter of fact, the National Treasury in its Memorandum - Circular No. 14-69 dated October 6, 1969 still maintains up to now that it has the right to return treasury warrants "found to have been paid to the wrong party, tampered, and otherwise tainted with fraud beyond the "24-hour clearing period", and the Commission on Audit has upheld this opinion of the National Treasury). This amendment cannot therefore be considered inconsequential but must be assumed to have been adopted for a very important purpose.

The significance of this change in Section 4 (c) of the Clearing Regulation requiring delivery of any cleared item for any reason whatsoever not later than the next clearing "to and received through the Clearing Office" of the Central Bank, instead of being "returned directly to the bank, institution or entity from which said item was received" is to make the right to return the cleared item to the Clearing Office of the Central Bank distinct and separate from the right to recover the amount of the cleared item in the action which the drawee bank may later on institute against the collecting bank. The distinction between the right to return

the cleared items and the right to recover from the collecting bank has a legal basis.

First of all, what the Clearing Regulations provide for is merely the right of a drawee bank to return any item for any reason whatsoever "to the Clearing Office not later than the next regular clearing." If the drawee bank fails to comply with this requirement it loses that right to return the item (for any reason whatsoever) to the clearing office. The clearing regulation does not at all even attempt to prescribe any rule as to whether or not the drawee bank loses also its right to recover the amount of defective item it received from and is returning to the sending bank, because such right is supposed to be governed by the pertinent provisions of the Negotiable Instruments Law, the other substantive laws, and settled jurisprudence on the matter, under which the drawee may or may not be entitled to recover said amount depending upon the facts and circumstances shown by the evidence presented in the case which the drawee bank may file in court. This is so because the only power and function of the Central Bank in promulgating the clearing regulations was "to establish nationwide facilities, to provide interbank clearing"<sup>15</sup>. To sustain the interpretation made by the Supreme Court of the provision of the Clearing Regulations would be to empower the Central Bank to legislate and amend or modify the Negotiable Instrument Law and other laws pertinent to the subject by creating a condition precedent to a drawee bank's cause of action against the collecting bank, where none is provided by substantive law so that the Clearing Rule provision in question is made the ultimate and sole determining factor in resolving the rights and obligations of the drawee and collecting bank involved in the clearing of checks. This interpretation of the rule is neither justified by the wording nor by its purpose. The only purpose of the clearing house regulations is to provide rules so that bank balances may be tentatively settled:

"The clearing house settlement between the banks is only a tentative arrangement of balances for the facilitation of business, and the refunding of money or credit received in the course of such a preliminary settlement is no more than a step in the correction of errors in bookkeeping, temporarily tolerated in the interests of expedition."<sup>16</sup>

This is especially true nowadays where because of the tremendous number of checks (reaching up to 368,000 items on peak days) sent for clearing by a total of 49 commercial and thrift banks in Metro Manila, their 997 branches in the area and 3 government entities, computers have to be employed to read and sort them instead of the old method

of human hands and eyes doing the work of reading and inspecting the checks.

The requirement that the drawee bank must return to the clearing office the item it sent through clearing within 24-hours after it was sent for clearing is only for the purpose of enabling the drawee bank to automatically get back the amount of the check which was previously debited from the clearing account it maintains with the Central Bank.<sup>17</sup> The credit the drawee bank gets for that amount is simultaneous with the debit made against the clearing account of the bank to which the cleared item is returned. In other words:

"Up to that time prescribed by the clearing regulations for the return of checks the *drawee bank* has, so far as the collecting bank is concerned, *the absolute right to return it and automatically get back the amount of said check*. It is legally immaterial what its reason for so doing may be and it therefore makes no difference that it gave a reason which had no foundation in fact."<sup>18</sup>

On the other hand, if the drawee bank fails to return the cleared item through the clearing office by the next clearing day, the clear implication of the rule is that the drawee bank is not entitled to return the item through the clearing office. Therefore it would not get the benefit of the automatic restoration of the amount of the cleared item to its clearing account. It would have to wait for either: a) the conformity of the bank to which it intended to return the item to the debit of the latter's clearing account of the amount of the check intended to be returned; to be correspondingly credited to the account of the returning bank; or b) if the bank to which the return was intended refuses to accept the said returned item, then, for the decision of the court (or as presently agreed upon by all banks and entities participating in the clearing operations in Metro Manila by the arbitration committee) in the action it may have to file for the amount of the returned item, to become final and executory. This by itself is sufficient penalty for the negligent delay of the drawee bank in returning the check beyond the 24-hour period, for then it has to wait, sometimes years, before being able to get back the money it could automatically had gotten back had it returned the item within 24 hours. In such action the court (or the arbitration committee) is to apply the law and jurisprudence (Sections 23 and 124 of the Negotiable Instruments Law governing forgery and material alteration respectively and the well settled rule in *Great Eastern Insurance Co. v. Hongkong and Shanghai Banking Corporations*<sup>19</sup> and the other pertinent cases) on the facts of the case and not merely decide it by determining the sole question of whether or not the drawee bank returned the cleared item within

the time prescribed by the clearing rules. The provision of the clearing house rules in question could not have been intended to reduce the function of the court (or the arbitration committee) in such an action by the drawee bank against the collecting bank to a mere counter of hours and minutes, which seems to be what the decision of the Supreme Court relegated the court (or the Arbitration Committee) to do in such a case. Such an interpretation of the Clearing Rule provision in question which produces said result is faulty.

"It is universally provided by clearing house rules that all checks presented shall be provisionally charged to the bank on which they are drawn; and that the bank, if it desires to repudiate them, must do so within a limited time, usually a specified hour on the same day. This right of a member of the clearing house to return items not properly charged against it is an especial compensation for the provisional charge before inspection. Under such a rule, the provisional charge of a check against the bank on which it is drawn does not constitute a payment of such check, and the bank may repudiate it within the time allowed by the rules; *when the time for inspection has been had, the special rules cease to govern, and the rights of the paying bank rest upon the general principles of law.*"<sup>20</sup>

The interpretation of the particular provision of the Clearing Regulation the Supreme Court adopted would moreover make such rule also govern the rights of the drawer and the payee of the checks sent for clearing. The denial of the drawee's right of recovery would certainly carry with it the result that the drawer should not be made to recover from the drawee and that the payee who deposited the check and who is legally presumed to be the forger could not then be held liable by the collecting bank. The clearing house rules were never intended to have such a far-reaching effect.

"The rules of a clearing house, as such, do not govern the rights of a drawer or payee of a check who is not a member of the clearing house and does not contract with express references to such rules."<sup>21</sup>

On the other hand, if the interpretation suggested in this article were adopted, the function of the court in the action which the drawee bank may file against the collecting bank would not only be as a mere counter of hours and minutes but rather as a trier of facts and of law with due regard to the equities of the case arising from the facts and circumstances, especially relating to the negligence or criminal acts of either of the parties, leading to the change of position or prejudice of the other. The result of the action should be based upon this criterion and not merely

on whether or not the cleared item was returned within the 24-hour period.

To illustrate, apply the ruling that "the failure of the drawee bank to return the item sent for clearing within the 24-hour period prescribed in the clearing regulations deprives it of any right to recover the amount of said check from the collecting bank" laid down by our Supreme Court in the Metropolitan Bank case to a very obvious example. Thus, suppose the depositor of Metropolitan Bank and Trust Company Salvador Sales, right after depositing the altered check was arrested by the authorities, not necessarily for the falsification of the check involved in the case, and was not able to withdraw a single centavo of the amount of the check. When the First National City Bank returned the check nine (9) days after it had been sent for clearing, the money represented by the check collected by Metropolitan Bank and Trust Company from First National City Bank was still in the checking account of Salvador Sales. Under the ruling of the Supreme Court, the First National City Bank, the drawee bank, cannot recover from Metropolitan Bank and Trust Company, the collecting bank, simply because the drawee did not return the check within 24 hours after it was sent for clearing. Such an unjust result discredits the theory upon which it is founded. It would not at all help bolster the ruling to say that the drawee bank under such a changed situation should be allowed to recover from the Metropolitan Bank and Trust Company because of the change in the facts. Such a statement by itself shows the fallacy of the rule since the main factual basis of the Supreme Court's conclusion in the case, i.e., that the drawee bank failed to return the check within 24 hours after it was sent for clearing, was not changed at all. As a matter of fact, such statement would show that the basis for allowing the drawee bank to recover under the circumstances is that the collecting bank still has the amount of the check with it and therefore has not changed its position or has not suffered any prejudice because of the failure of the drawee to return the check within the 24-hour period. The failure of the drawee bank to return the check within 24 hours is therefore not the true and correct basis for denying the right of recovery from the collecting bank.

Neither would it be correct to deny such right of recovery on the ground of the drawee's failure to return the check within 24 hours and the added fact that the amount of the check had been fully withdrawn by the depositor from the collecting bank, because such failure to make the return within the 24-hour period is not that kind of negligence which will bar recovery. The true and correct basis for denying recovery in an action by a drawee bank against a collecting bank to recover money paid out on a materially altered instrument is the negligence to notify the

collecting bank within a reasonable time after having learned of the material alteration, if such negligence resulted in the prejudice of the collecting bank. Thus, where the check in question contains a material alteration an eminent text writer says:

*"Negligence on the part of the drawee in not discovering the alteration was not a bar to the drawee's right to restitution.*

*"But upon the drawee's learning that the instrument had been altered, a failure to give notice thereof to the party to whom payment was made as a result of which such party lost some right against a prior party, including the one who altered the instrument, the drawee's right of restitution was barred." 22*

There is, however, another reason why the decision in the case of *Republic vs. Equitable Banking Corporation* cannot be properly considered as precedent for the rulings laid down in the two cases of *Hongkong and Shanghai Banking vs. People's Bank and Metropolitan Bank Trust Company vs. First National City Bank*. One of the defects of the treasury warrants involved in the *Equitable Bank* case which the National Treasury failed to return "within the 24-hour clearing period" was that the drawers' signatures appearing in the warrants were forged, a defect which only the National Treasury, as drawee of the warrants was in a position and therefore bound to discover "within said 24-hour clearing period." In the cases of *Hongkong & Shanghai Banking Corporation vs. People's Bank*, the defect of the check in question was that the payee's name was altered and then the substitute payee indorsed the check. In the *Metropolitan Bank* case, the defects of the check involved therein was that the payee's name was also altered and the amount was raised from P200.00 to P2,000,000.00. Afterward, the substitute payee indorsed the said check.

Since the defect in the warrants involved in the *Equitable Bank* case consisted in the forgery of the drawer's signature, it merely followed the well-established rule that the drawee of such instrument is conclusively presumed to know the signature of its depositor (*San Carlos Milling Co. vs. Bank of Philippine Islands*)<sup>23</sup> and therefore should bear the loss if it pays or honors such instrument without discovering such forgery. This legal presumption is based on the realization that should the rule be otherwise no person would entrust his money to the banks. The actual business practice is that banks have in their files no less than three specimens of the signatures of their depositors-drawers of the checks drawn against them. Before the drawee bank clears or honors any check drawn against it, it has to compare and verify the genuineness of the sig-

nature of the drawer of the check with two specimen signatures on its files. This ultimately is the reason why the cases hold that the drawee must discover within the 24-hour clearing period any forgery of the drawer's signature on the checks drawn against it and that if it fails to do so, it cannot recover the amount of the check from the person who received the payment. [Price v. Neal<sup>24</sup> and a host of cases following the ruling in said case both before and after the adoption of the Negotiable Instruments Law. (See also *Philippine National Bank v. Court of Appeals* <sup>25</sup>)]

Of course, illustrious Mr. Justice Claro M. Recto suggested in the case of *Philippine National Bank v. First National City Bank of New York*<sup>26</sup> that the doctrine in this old English case of *Price v. Neal*" is fast fading into the misty past, where it belongs." A closer scrutiny, however, of the ruling in said case merely confirms the rule laid down in said case of *Price v. Neal* because the result reached by our Supreme Court in that case enunciated the exception to the rule, (long recognized also by the authorities which adhere to the *Price v. Neal* doctrine) the recipient of the payment is itself negligent in the acquisition of the instrument honored or paid by the drawee, then the latter can recover the amount paid from such negligent recipient of the payment.<sup>27</sup> The reason for such exception is that the negligence of the drawee which pays the check without discovering the forgery of the drawer's signature is merely constructive negligence, while that of the recipient of the payment is actual negligence in acquiring the instrument from a stranger.

In the case of *Philippine National Bank v. First National City Bank of New York*, the Supreme Court held only the Motor Service Company liable to the drawee Philippine National Bank and (the case against the First National City Bank of New York was dismissed) because according to the facts of the case, the Motor Service Company was clearly negligent in acquiring the two checks in question from a stranger. It is quite clear that a drawee bank which fails to discover the forgery of the drawer's signature and consequently fails to return the item within the next 24-hour clearing period thereby inducing the collecting bank to allow its depositor to withdraw against said check deposited cannot certainly be allowed to recover from the collecting bank as the Supreme Court correctly held in the case of *Republic v. Equitable Banking Corporation*.

The facts, however, in the *Hongkong & Shanghai Bank* and *Metropolitan Bank* cases are different. As already above stated, the checks involved in these two cases contained material alterations of the payee's name, the rule is that the drawee bank in said cases, the *Hongkong and Shanghai Banking Corporation* and the *First National City Bank*, cannot be considered more negligent than the collecting bank for not discovering such alterations. Thus as stated by the authorities:

"x x x In the case of money paid on a raised or otherwise altered check, there is no greater obligation upon the drawee bank than upon the holder to know the correct amount of the check or the name of the payee. 10 Zollmann, *Banks and Banking* 7371; *Crawford v. West Side Bank* (1885) 100 N. Y. 50, 2 N. E. 881; 7 Am. Jur., *Banks* 587. One reason for this rule is that the drawee bank and the holder have equal opportunities to consult with the drawer regarding the genuineness of the check. *Espy. v. Bank of Cincinnati* (1873) 18 Wall. 604, 21 L. ed. 947. " <sup>28</sup>

The well-established rule therefore is that in accordance with the accepted quasi-contract doctrine permitting recovery of money paid out under a mutual mistake of material fact, the drawee who paid a materially altered check can recover the money so paid to the holder, in the absence of any negligent act of the drawee other than its failure to discover by itself such alteration.<sup>29</sup>

This should be especially true with respect to instruments the payee of which has been materially altered, as in the two cases commented on, because the rule governing the right of the drawee to recover money paid out under a forged indorsement laid down in the well-known case of *Great Eastern Insurance Co. v. Hongkong & Shanghai Banking Corporation* 43 Phil. 678, should apply. As the authorities say, under Sec. 124 of the Negotiable Instruments Law, which provides that even in the hands of a holder in due course, a materially altered instrument may be enforced only according to its original tenor, the endorsement of such a check by the substituted payee is in fact a forgery of the indorsement of the original payee.<sup>30</sup>

Actual banking experience furthermore shows how unrealistic is the interpretation of the Clearing Rule provision adopted by the Supreme Court. The promulgation of the decision in the *Hongkong and Shanghai Bank* case on September 30, 1970 sowed confusion in the banking community.

Because the drawee banks, not wanting to take a chance on whether or not the checks received by them through clearing bore forged indorsements or contained material alteration, which they were helpless to discover within the 24-hour period required in said decision, returned all the checks drawn against them within 24 hours after receiving the same from clearing regardless of whether or not they actually bore forged indorsements or contained material alterations, because under the decision, they could not then anymore rely on the guarantee of all prior indorsements and / or lack of indorsements after the lapse of said 24-hour period after clearing. Upon the request of the banking community, the Central Bank therefore on December 23, 1970 amended this



Sec. 4 (c) of the C. B. Circular No. 9 as amended by C. B. Circular Nos. 138 and 169, by C. B. Circular No. 317 to read as follows:

**"SECTION 4. Clearing Procedures —**

"Items which should be returned for any reason whatsoever shall be delivered to and received through the Clearing Office in the special red envelopes and shall be considered and accounted as debits to the banks, institutions or entities to which the items are returned and credits to the returning banks, institutions and entities. Nothing in this section shall prevent the returned items from being settled by reimbursement to the bank, institution or entity returning the items. All items to be returned shall be presented to the Clearing Office not later than 3:30 p.m. on the following business day. *However, items which have been the subject of a material alteration shall be returned within twenty-four (24) hours after discovery of the material alteration* but in no event beyond 180 days from the date of receipt thereof from the Clearing Office. Items bearing a forged indorsement, when such endorsement is necessary for negotiation, *shall also be returned within twenty-four (24) hours after discovery of the forgery* but in no event beyond the period fixed or provided by law for the filing of a legal action by the returning bank, institution or entity against the bank, institution or entity sending the same."

The Central Bank found the above-quoted amendment inadequate so it further amended the wording of C. B. Circular No. 317 by adopting C. B. Circular No. 580 on September 19, 1977, which reads as follows:

"items which have been the subject of a material alteration or items bearing a forged indorsement when such indorsement is necessary for negotiation shall be returned within twenty-four (24) hours after discovery of the alteration or the forgery but in no event beyond the period fixed or provided by law for filing of a legal action by the returning bank / branch, institution or entity sending the same."

In time the above-quoted Clearing House provision gave rise to the "pingpong" checks. Checks claimed by the drawee bank to bear forged indorsements and / or material alterations and returned beyond the 24-hour clearing period were refused by the collecting bank, who also returned them through the clearing house. The checks were sent back and forth through the clearing house by the drawee and collecting banks, because neither of them would want to be in the position of holding the empty bag, should it be the one to file the case in court to determine the question of whether there was really a forgery of the indorsement or alteration of the check. In its annual stockholders' meeting of April 13, 1982 the stockholders amended the above provision to read as follows.

**"SEC. 23 — SPECIAL RETURN ITEMS BY DIRECT PRESENTATION —**

"Items which have been the subject of a material alteration or items bearing a forged endorsement when such endorsement is necessary for negotiation shall be returned by direct presentation or demand to the collecting bank and not through the regular clearing house facilities within the period prescribed by law for the filing of a legal action by the returning bank/ branch, institution or entity against the bank/ branch, institution or entity sending the same."

The holding that the remedy of the drawee bank in this case is only against the depositor of the collecting bank is not in accord with the authorities.

The holding of the Supreme Court in its decision in the *Metropolitan Bank* case and also in the *Hongkong & Shanghai Bank* decision, is to the effect that the remedy of the drawee bank lies not against the collecting bank but against the party responsible for the changing of the name of the payee and the amount of the check.<sup>31</sup> If based merely on the failure of the drawee bank to return the check in question within 24 hours, and not on any other act or omission which caused prejudice to the collecting bank, this ruling contradicts the well settled and accepted rule laid down by one Supreme Court in the often cited case of *Great Eastern Insurance Co. v. Hongkong & Shanghai Banking Corporations*<sup>32</sup>

In that case, the Great Eastern Insurance Company issued a check for ₱2,000.00 payable to the order of a certain Melicor. This check fell into the hands of a certain Maasim, who forged the signature of Melicor on the check and then indorsed the same to the Philippine National Bank, where he deposited it. In due course the Philippine National Bank collected the amount from the Hongkong and Shanghai Banking Corporation, the drawee bank. About four months after the check had been honored, the Great Eastern Insurance Company discovered the forgery of the signature of the payee and thus made a claim for reimbursement from the drawee bank. The drawee bank refused Great Eastern Insurance Company which therefore filed an action against the drawee bank and the drawee bank in turn, impleaded the Philippine National Bank. On these facts, the Supreme Court decided in favor of the drawer, the Great Eastern Insurance Company, and against the drawee bank. The drawee bank was also allowed to recover against the collecting bank. The only remedy of the collecting bank was against its depositor Maasim. Thus, the Supreme Court said in that case:

"It is admitted that the Philippine National Bank cashed the check upon a forged signature, and placed the money to the credit of Maasim, who was the forger. That the Philippine National Bank then endorsed the check and forwarded it to the Shanghai Bank by whom it was paid. The Philippine National Bank had no license or authority to pay the money to Maasim or anyone else upon a forged signature. *It was its legal duty to know that Melicor's endorsement was genuine before cashing the check. Its remedy is against Maasim to whom it paid the money.*"<sup>33</sup>

The facts of the Metropolitan Bank and Hongkong and Shanghai Bank cases are identical in that both cases involve the alteration of the payee's name. As previously stated, if the name of the payee to whose order a check is made payable is altered with the name of another and the instrument is thereafter indorsed by a person other than the original payee, such indorsement is a forgery because under Section 124 of the Negotiable Instruments Law such materially altered instrument even in the hands of a holder in due course, which can be conceded to be the status of the collecting banks, can be enforced only "according to its original tenor" and therefore should have been indorsed by the original payee. This being the case, the settled and accepted rule enunciated by the Supreme Court in the above cited Great Eastern Insurance Co. case should also apply to the two cases. Even if the drawee bank returns the check bearing the forged indorsement beyond the 24-hour period stated in the clearing regulations, the drawee bank should be allowed to recover against the collecting bank in the absence of any other fact which would preclude it from such recovery, and the remedy of the collecting bank should be against its depositor.

The reason why the drawee bank must be allowed not only 24 hours within which to discover the forgery of indorsements or alterations of the payee's name or any other alterations on the check, is quite obvious and is clearly explained by a text writer as follows:

"The delay in giving notice of a forged indorsement, of which the drawee may be guilty, is a delay which cannot take place until after the drawee has learned that he paid the instrument under a forged indorsement. The drawee is not likely to learn that he paid the instrument under a forged indorsement. The drawee is not likely to learn that fact by his own investigation. Now is there any duty upon the drawee to look for forged indorsements? *The drawee will likely first learn of the forgery from the drawer. The drawer normally learns, of forged indorsement on instruments issued by him, from the holder whose indorsement was forged.* Thus the information concerning the forged indorsement, as a rule, originates with the loser, who informs the drawer, the drawer then informs the drawee and the drawee then notifies the person to whom he paid. Not until the drawee learns

the fact of forgery is there any duty on him to report to the party to whom he paid."<sup>34</sup>

As previously stated, the situation in which the indorsement on the check is forged or where the check contains an alteration has to be distinguished from the situation in which the signature of the drawer of the check is forged. In the latter situation, the drawee has the means and therefore is under obligation to know and discover within 24 hours whether or not the check bears a forged signature of the drawer, because the specimen signatures of the drawer are on file with the drawee. This is the same as when the check is drawn against insufficient funds or payment of the check has been stopped. These kind of checks are what the authorities call "not good checks" and are understood by them to be the checks required to be returned within 24 hours after the same had been sent for clearing, because it would be pure negligence on the part of the drawee if it fails to discover such defect within such time. This is the reason why the ruling in the case of Republic of the Philippines v. Equitable Banking Corporation<sup>34</sup> is covered because the defects of the cleared items involved in said case were exclusively within the means of the drawee to determine and therefore ought to have been returned within 24 hours after clearing.

On the other hand, the drawee bank does not have its files specimen signatures of the payee of the check drawn against it. Indeed, it would be requiring the impossible for banks to have such files.

The rule that the remedy of the drawee bank should only be against the depositor of the collecting bank laid down by the Supreme Court in the Metropolitan Bank and Hongkong and Shanghai Bank cases is not in consonance with law. To be able to exercise such right of action, the drawee would have to know the address of the depositor. This could only be available from the records of the collecting bank, who in the first place is the one who entertained such depositor and got its address. Under Republic Act No. 1405, the collecting bank, or any bank for that matter, is prohibited from disclosing "any information concerning any deposit" with it. How then can the drawee bank file suit against the collecting bank's depositor? Even if the drawee bank is able to get the name and address of the collecting bank's depositor, both the name and address will in all probability be fictitious. If this indeed be the law, would it not be reasonable to say that the same would encourage fraudulent schemes?

The fraudulent scheme could operate as follows. A, with a deposit in X Bank as follows connives with B, who opens a deposit in Y Bank. A issues to him a check for eight thousand pesos payable to bearer supposedly to pay for an article bought by A from B. B would then add the letter "y" to the word "Eight" and another "0" to the figures P8000.00 so

as to make it ₱80,000.00 and then deposit the check to his account in "Y" Bank. Very likely, the alteration is not discovered by X Bank within the 24-hour clearing period and so X Bank will not return the check to Y Bank within that period. A then waits for the end of the month when he receives his cancelled checks from X Bank and then claims for the refund of ₱72,000.00, the difference of the ₱80,000.00 and the ₱8,000.00 he originally wrote in his check. Since it is assumed that he is in conspiracy with B, he, of course, has his proofs ready to show that the amount of his check is really originally for only ₱8,000.00, and so X Bank has no choice but to pay him the ₱72,000.00. If, as held by the Supreme Court, in this **Metro Bank** case, the remedy of X Bank should be only against B and not against Y Bank, the fraudulent scheme would in all probability go unpunished, indeed even uninvestigated, because the scheme would invariably be that B would have given a fictitious name and address to Y Bank when he opened his account. Since the decision of the Supreme Court absolves Y Bank from any liability, it would not in any way have any interest in pursuing the investigation as to who B is, how he was able to open the account, and where he could be located. A ruling which permits such an easy way for a very shallow scheme to succeed cannot be correct.

On the other hand, if the rule be as it should be that the drawee bank has a right to recover from the collecting bank in this class of cases, then the banks would then be on notice that they cannot allow the opening of any account, whether checking or savings, in the name of strangers or what the banking community refer to as "walk-in-clients," which in most cases is the main source of this kind of bank fraud, but would instead invariably require identification by responsible persons.

Another reason why this particular ruling of the Supreme Court is unrealistic is that under Sec. 66 of the Negotiable Instrument Law, the warranty of depositor of the collecting Bank when it indorsed its check for deposit runs only in favor of "all subsequent holders in due course" and the drawee bank certainly is not a holder in due course. It is rather a payor.

"It is our opinion, therefore, that the drawee is not such a holder in due course, as will permit it to recover under Section 62 of the Negotiable Instruments Law (Section 8167, General Code), Section 63, Negotiable Instruments Law (Section 8168, General Code), or Section 52 of the Negotiable Instruments Law (Section 8157, General Code)."<sup>35</sup>

**The ruling of the supreme court that the guarantee of all prior indorsements made by the collecting bank at the back of the check it sends for clearing must be read together with the 24-hour regulation of the clear-**

ing house and that therefore once that 24-hour period is over, the liability of the collecting bank on such guarantee ceases, is unrealistic and is not in accord with the authorities.

The Supreme Court, reiterating its ruling in **Hongkong and Shanghai Banking Corporation v. People's Bank and Trust Company**, stated in the **Metropolitan Bank** case:

"x x x But plaintiff bank insists that defendant bank is liable on its indorsement during clearing house operations. The indorsement, itself, is very clear when it begins with words '*For clearance, clearing office*' \* \* \* In other words, such an indorsement must be read together with the 24-hour regulation on clearing house operations of the Central Bank. Once the 24-hour period is over, the liability on such an indorsement has ceased. This being so, plaintiff bank has not made out a case for relief."

Such ruling will render the guarantee of prior indorsements of no use whatsoever, because if the drawee bank, not wanting to take any chance whatsoever, were to return the check within 24 hours through the clearing house, it does not have to rely on the guarantee of all prior indorsements made by the collecting bank. By returning it through the clearing house within such time the clearing account of the drawee bank immediately gets credited with the amount of the returned check. It does not have to file any court action and rely on the guarantee to get back the amount of the check it returns. As a matter of fact, the credit in its clearing account is effected without the aid of human hands but by the computer when the returned check is read and passed thru the computer. On the other hand, if it does not return the check within 24 hours, according to this ruling of the Supreme Court, the guarantee of prior indorsements has no more binding force. It is obvious therefore, that under the ruling of the Supreme Court the guarantee is useless.

It is not unreasonable to assume that the Supreme Court did not intend, by the above-quoted ruling, to render useless a long standing practice adopted by the banks undoubtedly based on their experience and jurisprudence on the matter to protect their interest in situations such as those which happened in the **Metropolitan Bank** case.

Let us consider the following facts of a case which actually happened and which exemplifies a new but very common fraudulent scheme perpetrated against banks nowadays. Mr. D. an employee in the Accounting Department of X & Co. opened a savings account with P Bank. He was introduced to the bank by his cousin, Mr. M, who was then employed as General Accounting Clerk of P Bank. Mr. D deposited in his

savings account a certain unfunded and worthless check, which on its face shows to be for the amount of P280,000.00. After the check was deposited, his cousin Mr. M, being the General Accounting Clerk of P Bank and acting in collusion and conspiracy with Mr. D, substituted the worthless check deposited by Mr. D. in his savings account with a good check which Mr. D. had previously stolen from X & Co. This latter check is also for P280,000.00, payable to the order of the "City Treasurer of Manila" and crossed "For Deposit in the Payee's Account Only." After the substitution, the substitute check which was naturally funded and properly drawn was then encoded by Mr. M for clearing so as to make it appear that it came from P Bank. Mr. M stamped at the back of the check P Bank's guaranty "of all prior indorsements and or lack of indorsements" and thus caused the substitute check to be sent to and be cleared by R Bank. After clearing, Mr. D's savings account with P Bank was credited with the amount of the substitute check in the amount of P280,000.00. He then withdrew the money little by little until one month later, when the fraud was discovered, the credit balance in his savings account was only the very minimal amount of P55.00. After the fraud was discovered, X & Co., having been made to issue another check to the City Treasurer of Manila, demanded from R Bank the refund of the amount of P280,000.00, which had been paid to Mr. D., a person other than the named payee. R Bank had no choice but to refund the P280,000.00 and R Bank now claims reimbursement against the P Bank; and the latter now raises the defense that despite the fact that the criminal act of its employee Mr. M, in stamping at the back of the check in question the guarantee of "all prior indorsements and/or lack of indorsements" was binding on it, under the rule of the Supreme Court in the Metropolitan Bank and the Hongkong & Shanghai Bank cases, this guaranty is only good during the "24-hour clearing period", since the check in question which was honored by R Bank was not returned within 24 hours, the action on the breach of the guaranty could not anymore be availed of by R Bank. The statement of this contention in effect converts the clearing house rule as well as the decision of the Supreme Court interpreting it as a shield for fraud. If as a result of any transaction damage is suffered by any of the two persons, the one whose criminal or negligent act was the efficient cause of the loss must suffer the loss. R Bank should be allowed to recover the amount of the check from P Bank, because the act of the employee of P Bank is not only negligent but criminal, while no employee of R Bank is guilty of any negligence or criminal participation whatsoever. The only reason it honored the check, even if it did not contain any indorsement, was its reliance on the guaranty "of all prior indorsements and/or lack of indorsements" stamped at the back of the check. Yet,

if the ruling of the Supreme Court in the aforementioned two cases were to be applied, there is no choice but to rule that R Bank cannot recover from P Bank in this case. How then can such palpable injustice be avoided? The only way is to interpret the stamp of guaranty "of all prior indorsements and or lack of indorsements" just like any contract of indorsements, the breach of which is actionable within the ordinary period of prescription provided by law and not only within the 24-hour clearing period as stated by the Supreme Court.

As a matter of fact, the present dilemma presented to the bankers by this unrealistic ruling of the Supreme Court that the guaranty "of all prior indorsements and / or lack of indorsements" is actionable only within the 24-hour clearing period has been solved by the Philippine Clearing House Corporation, whose stockholders are all the various commercial and savings banks. The Philippine Clearing House Corporation is the entity now in charge of conducting the clearing operations in Metro Manila; it provides in its Clearing House rule that:

"SEC. 17 - BANK GUARANTEE -

All checks cleared through the PCHC shall bear the guarantee affixed thereto by the collecting branch / office which shall read as follows: "All prior endorsements and / or lack of endorsements guaranteed. Checks accepted by drawee banks to which said guarantee has not been affixed shall, nevertheless, be deemed guaranteed by the collecting bank as to all prior endorsements and / or lack of endorsements.

It will be noted that the ruling of the Supreme Court in the case of *Hongkong & Shanghai Bank* reiterated in the *Metro Bank* case regarding the duration of this guaranty "of all prior indorsements and/or lack of indorsements" is based mainly on the wording of the guaranty stamped at the back of the check involved in the former case which begins with the words "For clearance, clearing office." Thus, the Supreme Court in the above two cases stated:

"But Plaintiff Bank insists that Defendant Bank is liable on its indorsement during clearing house operations. *The indorsement, itself, is very clear when it begins with the words 'For Clearance, clearing office \* \* \*'*: In other words, such an indorsement must be read together with the 24-hour regulation on Clearing House Operations of the Central Bank. Once that 24-hour period is over, the liability on such an indorsement has ceased. This being so, Plaintiff Bank has not made out a case for relief."

When the Philippine Clearing House Corporation formulated the above-

quoted Sec. 17 of the Clearing House Rules and Regulations, prescribing the wording of the guaranty, it deleted from such guaranty required to be stamped the words "For clearance, clearing office" which the Supreme Court in the two above-mentioned cases relied upon heavily in holding that the guaranty of "prior indorsements and/or lack of indorsements" is for clearance purposes only and can only be availed of within the 24-hour clearing period after the check in question was received from clearing. The intention of the bank stockholders of the Philippine Clearing House Corporation in wording such rule was to avoid the interpretation of the previous rule adopted by our Supreme Court in the said *Hongkong and Shanghai Bank* case, an interpretation which the various bank stockholders because of their experience found to be unrealistic. The meaning of this change therefore is that this guaranty "of all prior indorsements and or lack of indorsements" is just like any other contract of indorsement. The action to recover based on breach of such written contract is available to the party in whose favor the guaranty is made within the period of prescription provided by law for written contracts, because undeniably the stamped guaranty is a written contract.

From the above discussion, it appears that the long established rule that a drawee bank has the right to recover from the collecting bank the money paid out on a materially altered instrument, especially if the alteration included the name of the payee should have been the one followed by our Supreme Court in the cases of *Hongkong and Shanghai Banking Corporation vs. People's Banking and Trust Company* and *Metropolitan Bank and Trust Company vs. First National City Bank*. Such rule should not be affected by the operation of the Clearing Regulation, which was intended to govern only the right of the drawee bank to return a cleared item but not the right to recover the amount thereof from the collecting bank.

#### CONCLUSION:

It could be probably said that in the light of the amendments to the clearing house rule in question, the rulings of the Supreme Court in the above-mentioned two cases are no longer applicable at least with respect to checks bearing forged indorsements or material alterations.

With respect, however, to checks bearing the forged signature of the drawer checks drawn against insufficient funds, checks the payment of which has been stopped, cashier's checks which has been materially altered, and checks which are visibly incomplete or irregular upon their face, if the drawee bank has the means to discover by itself the defects and therefore be legally obliged to return the checks to the collecting bank within the 24-hour clearing period, it is submitted that

the rulings in the two cases commented on should be qualified so that:

"If the collecting bank has not changed its position or been damaged in any way by the delay (in the return of the check) or the rights of third parties have not intervened, the (drawee) bank can still return the instrument without incurring liability." <sup>36</sup>

1. 200 Mass. 110, 85 NE., 897, 23 LRA (NS) 1236.
2. 118 SCRA 537
3. 35 SCRA 140.
4. 35 SCRA 142
5. 35 SCRA pp. 143-144
6. 118 SCRA 539-540
7. 118 SCRA
8. 10 SCRA p. 8
9. Id at p. 11
10. Id at p. 12
11. Id. at p. 12-13
- 9-a Underscoring in the first sentence ours.
12. Id at p. 13-14
13. at 35 SCRA p. 144
14. at 10 SCRA p. 12
15. Sec. 107 Rep. Act. No. 365
16. *Sneider v. Bank of Italy*, 184 Cal. 595, 194 Pac. 1021. 12 A. L. R. 998
17. As part of the reserve requirement under Sec. 100 of the Central Bank Law.
18. *In re Smith, Lockhart & Co.*, 3 Fed. 2 d 444, 447.
19. 43 Phil. p. 678
20. 10 Am. Jur. 2d, 809
21. *Sneider v. Bank of Italy*, 184 Cal. 595; 1954, P1021. 12 ALR 993
22. *Britton on Bills and Notes*, pp. 651-652 citing *Third Nat. Bank of St. Louis V. Allen*, 69 Mo. 310.
23. 59 Phil. p. 59.
24. 3 Burr. 1355, 97 Eng. Rep. 871
25. SCRA 693

26. 63 Phil. p. 711
27. Citizen' Bank of Fayette v. i. Black & Sons Inc., 228 Ala. 246, 153 So. 404; Hutches ware Co. v. Planters State Bank, 26 Ga. App. 321, 105 SE 854; and numerous cases cited in II Patons Digest 1809.
28. 1 Paton's Digest 120
29. Birmingham National Bank v. Bradley (1893) 103 Ala. 109,15 So. 440; Espy v. Bank of Cincinnati, cited above; Redington v. Woods (1973) 45 Cal. 406, 13 Am. Rep. 190; Trust Co. v. Bank (1923) 29 Ga. App. 472, 116 S. E. 204; Continental National Bank v. Metropolitan National Bank (1903) 107 III. Ap. 455; Merchant's Bank v. Exchange Bank (1840) 16 La. 457; Third National Bank v. Allen (1875) 59 Mo. 310; Parke v. Roser (19867) 6 Ind. 500, 33 Am. Rep. 102; Bank v. Jewelry Co. (1920) 203 Mo. App. 646, 220 S. W. 511; Rapp v. National Security Bank v. State Bank (1888) 22 Neb. 769, 36 N. W. 289, 3 Am. St. Rep. 294 77, 7 Am. Rep. 310, National Bank of Commerce v Manufacturer's Bank (1980) 122 N. Y. 307, 25 N. E. 353.
30. Fourth National Bank of Macon vs. Lattimor, 168 Ga. 547, 138, 396. To the same effect is the ruling in the case of Andrew vs. Sibley, 220 Mass. 10, 107 N. E. 395 and First Nat. Bank v. Cridley, 112 Div. 398, 98 N. E. Supp. 445.
31. 35 SCRA pp. 145-146
32. 43 Phil. 678
33. Id. at pp. 683-683
34. Britton on Bills and Notes p. 657
34. 10 SCRA p. 8.
35. Britton on Bills and Notes, p. 645, citing State Planters Bank & Trust Co. of Richmond v. Fifth Third Union Trust Co., 1937, 56 Ohio App. 309, 10 N. E. 2d, 935.
36. Please see Patons Digest of Legal Opinions of the American Bankers Ass. p. 1203 citing National Bank of Baltimore v. Drover's & Mechanics' Merchants' National Bank 122 app. Div. 554, 112 N. Y. S. 937 (words in parenthesis supplied)

Atty. Raul S. Roco

## RECONCILIATION THROUGH THE RESTORATION OF RIGHTS

### Opening Statement

The search for a restoration of the rights of the Filipino people cannot be candid and meaningful without a discussion of Presidential Decrees 1834, 1835, 1836, 1877 and 1877-A, and Proclamation No. 2045 as amended by Proclamation No. 2045-A.

### Presidential Decree No. 1834

Presidential Decree No. 1834 increases the penalties for the crimes of rebellion, sedition and related crimes. To appreciate it, we must look to its legislative history.

Since January 1, 1932, the law prescribing penalties for crimes against public order was Act No. 3815 as amended, otherwise known as the Revised Penal Code. On June 10, 1976 however Presidential Decree No. 942 was issued on the basis of the following policy statements:

"WHEREAS, it is the primary goal of the martial law administration to restore peace, order and normalcy to Philippine conditions as early as possible;

WHEREAS, the attainment of this goal is greatly hampered by certain elements of society who continue to pursue acts and engage in activities destructive to the stability and security of the State;

WHEREAS, there is a pressing need to strengthen and reenforce the continuing campaign against subversion by increasing the penalties for crimes against public order and by treating as distinct other offenses committed in the course of the commission of such crimes."

Fundamentally, PD 942 increased by one degree the penalties imposed upon crimes against public order. Where the penalty under the Revised Penal Code was prison mayor or from six years and one day to twelve years imprisonment, the penalty was raised to reclusion temporal or from twelve years and one day to twenty years imprisonment. Where the crime was punishable by prison correccional or six months and one day to six years imprisonment, it was increased to prison mayor or six years and one day to twelve years.

Thus in 1976 when the state of martial law was subsisting, the President considered it necessary to increase the penalties for crimes against public order, more or less consistently by one degree. On January 16, 1981