

CHANROBLES PUBLISHING COMPANY

**SUPREME COURT
THIRD DIVISION**

**DEVELOPMENT BANK OF THE
PHILIPPINES,**

Petitioner,

-versus-

**G.R. No. 79351
November 28, 1989**

**THE HON. SECRETARY OF LABOR,
CRESENCIA DIFONTORUM, ET AL.,**

Respondents.

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DECISION

CORTES, J.:

Petitioner Development Bank of the Philippines seeks the nullification of an order dated July 29, 1987 and issued by the Undersecretary of Labor and Employment, affirming that of National Capital Region Officer-in-Charge Romeo A. Young, directing the petitioner to deliver the properties of Riverside Mills Corporation (RMC) which it had in its possession to the Ministry (now Department) of Labor and Employment (MOLE) for proper disposition in Case No. NCR-LSED-7-334-84 pursuant to Article 110 of the Labor Code.

Labor Case No. NCR-LSED-7-334-84 involves a complaint for illegal dismissal, unfair labor practice, illegal deductions from salaries and violation of the minimum wage law filed by private respondents herein against RMC. On July 3, 1985, a decision was rendered by Director Severo M. Pucan of the National Capital Region, MOLE, ordering RMC to pay private respondents backwages and separation benefits. A corresponding writ of execution was issued on October 22, 1985 directing the sheriff to collect the amount of ONE MILLION TWO HUNDRED FIFTY-SIX THOUSAND SIX HUNDRED SEVENTY-EIGHT PESOS AND SEVENTY SIX CENTAVOS (P1,256,678.76) from RMC and, in case of failure to collect, to execute the writ by selling the goods and chattel of RMC not exempt from execution or, in case of insufficiency thereof, the real or immovable properties of RMC.

However, on May 23, 1986, the writ of execution was returned unserved and unsatisfied, with the information that the company premises of RMC had been padlocked and foreclosed by petitioner. It appears that petitioner had instituted extra-judicial foreclosure proceedings as early as 1983 on the properties and other assets of RMC as a result of the latter's failure to meet its obligations on the loans it secured from petitioner.

Consequently, private respondents filed with the MOLE a "Motion for Delivery of Properties of the [RMC] in the Possession of the [DBP] to the [MOLE] for Proper Disposition," stating that pursuant to Article 110 of the Labor Code, they enjoy first preference over the mortgaged properties of RMC for the satisfaction of the judgment rendered in their favor notwithstanding the foreclosure of the same by petitioner as mortgage creditor [Rollo, pp. 16-17]. Petitioner filed its opposition.

In an order signed by Officer-in-Charge Romeo A. Young and dated December 11, 1986, private respondents' motion was granted based on the finding that Article 110 of the Labor Code and the ruling laid down in *Philippine Commercial and Industrial Bank vs. Natural Mines and Allied Workers' (NAMAWU-MIF)* [G.R. No. 50402, August 19, 1982, 115 SCRA 873] support the conclusion that private respondents still enjoyed a preferential lien for the payment of their backwages and separation benefits over the properties of RMC which were foreclosed by petitioner [Rollo, pp. 21-22].

Petitioner then filed its motion for reconsideration on December 24, 1986 contending that Article 110 of the Labor Code finds no application in the case at bar for the following reasons: (1) The properties sought to be delivered have ceased to belong to RMC in view of the fact that petitioner had foreclosed on the mortgage, and the properties have been sold and delivered to third parties; (2) The requisite condition for the application of Article 110 of the Labor Code is not present since no bankruptcy or insolvency proceedings over RMC properties and assets have been undertaken [Rollo, pp. 24-28]. In an order dated July 29, 1987, petitioner's motion for reconsideration was denied for lack of merit by Undersecretary Dionisio C. dela Serna.

Hence, petitioner filed this special civil action for certiorari with prayer for the issuance of a writ of preliminary injunction. On August 27, 1987, this Court issued a temporary restraining order enjoining public respondent from enforcing or carrying out its order dated July 29, 1987. After considering the allegations made and issues raised in the petition, comments thereto and reply, the Court, on March 14, 1988, resolved to give due course to the petition and to require the parties to submit their respective memoranda. Petitioner and private respondent submitted their memoranda, while public respondent adopted as its memorandum the comment it had previously submitted.

After a careful study of the various arguments adduced, as well as the legal provisions and jurisprudence on the matter, the Court finds the petition impressed with merit. Indeed, the assailed Order suffers from infirmities which must be rectified by the grant of a writ of certiorari in favor of petitioner.

Firstly, public respondent acted with grave abuse of discretion amounting to lack or excess of jurisdiction in enforcing private respondents' right of first preference under Article 110 of the Labor Code notwithstanding the absence of bankruptcy, liquidation or insolvency proceedings against RMC.

Article 110 of the Labor Code and Section 10, Rule VIII, Book III of the Omnibus Rules Implementing the Labor Code provide the following:

Article 110. WORKER PREFERENCE IN CASE OF BANKRUPTCY. — In the event of bankruptcy or liquidation of an employer's business, his workers shall enjoy first preference as regards wages due them for services rendered during the period prior to the bankruptcy or liquidation, any provision of law to the contrary notwithstanding. Unpaid wages shall be paid in full before other creditors may establish any claim to a share in the assets of the employer [Emphasis supplied].

Section 10. PAYMENT OF WAGES IN CASE OF BANKRUPTCY. — Unpaid wages earned by the employees before the declaration of bankruptcy or judicial liquidation of the employer's business shall be given first preference and shall be paid in full before other creditors may establish any claim to a share in the assets of the employer.

It is clear from the wording of the law that the preferential right accorded to employees and workers under Article 110 may be invoked only during bankruptcy or judicial liquidation proceedings against the employer. The law is unequivocal and admits of no other construction.

Respondents contend that the terms "bankruptcy" or "liquidation" are broad enough to cover a situation where there is a cessation of the operation of the employer's business as in the case at bar. However, this very same contention was struck down as unmeritorious in the case of *Development Bank of the Philippines vs. Hon. Labor Arbiter Ariel C. Santos* [G.R. Nos. 78261-62, March 8, 1989] involving a group of RMC employees which sought to enforce its preference of credit Article 110 against DBP over certain RMC real properties. In that case, the Court laid down the ruling that Article 110 of the Labor Code, which cannot be viewed in isolation of, and must always be reckoned with the provisions of the Civil Code on concurrence and preference of credits, may not be invoked by employees or workers of RMC, like private respondents herein, in the absence of a formal declaration of bankruptcy or a judicial liquidation order of RMC.

The rationale for making the application of Article 110 of the Labor Code contingent upon the institution of bankruptcy or judicial liquidation proceedings against the employer is premised upon the very nature of a preferential right of credit. A preference of credit bestows upon the preferred creditor an advantage of having his credit satisfied first ahead of other claims which may be established against the debtor. Logically, it becomes material only when the properties and assets of the debtor are insufficient to pay his debts in full; for if the debtor is amply able to pay his various creditors in full, how can the necessity exist to determine which of his creditors shall be paid first or whether they shall be paid out of the proceeds of the sale of the debtor's specific property? Indubitably, the preferential right of credit attains significance only after the properties of the debtor have been inventoried and liquidated, and the claims held by his various creditors have been established [Kuenzle & Streiff (Ltd.) vs. Villanueva, 41 Phil. 611 (1916); Barretto vs. Villanueva, G.R. No. L-14938, December 29, 1962, 6 SCRA 928; Philippine Savings Bank vs. Lantin, G.R. No. L-33929, September 2, 1983, 124 SCRA 476].

In this jurisdiction, bankruptcy, insolvency and general judicial liquidation proceedings provide the only proper venue for the enforcement of a creditor's preferential right such as that established in Article 110 of the Labor Code, for these are in rem proceedings binding against the whole world where all persons having any interest in the assets of the debtor are given the opportunity to establish their respective credits [Philippine Savings Bank vs. Lantin, supra; Development Bank of the Philippines vs. Santos supra].

Secondly, public respondent's Order directing petitioner to deliver to the MOLE the properties it had foreclosed from RMC for the purpose of executing the judgment rendered against RMC in Case No. NCR-LSED 7-334-84 violates the basic rule that the power of a court or tribunal in the execution of its judgment extends only over properties unquestionably belonging to the judgment debtor [Special Services Corporation vs. Centro La Paz, G.R. No. L-44100, April 28, 1983, 121 SCRA 748; National Mines and Allied Workers' Union vs. Vera, G.R. No. L-44230, November 19, 1984, 133 SCRA 295].

It appears on record, and remains undisputed by respondents, that petitioner had extra-judicially foreclosed the subject properties from

RMC as early as 1983 and purchased the same at public auction, and that RMC had failed to exercise its right to redeem. Thus, when Officer-in-Charge Young issued on December 11, 1986 the order which directed the delivery of these properties to the MOLE, RMC had ceased to be the absolute owner thereof [See *Dizon vs. Gaborra*, G.R. No. L-36821, June 22, 1978, 83 SCRA 688]. Consequently, the order was directed against properties which no longer belonged to the judgment debtor RMC.

However, respondents, in citing the case of *PCIB vs. NAMA-WU-MIF* [supra], argue that by virtue of Article 110 of the Labor Code, an “automatic first lien” was created in favor of private respondents on RMC properties — a “lien” which pre-dated the foreclosure of the subject properties by petitioner, and remained vested on these properties even after its sale to petitioner and other parties.

There is no merit to this contention. It proceeds from a misconception which must be corrected.

What Article 110 of the Labor Code establishes is not a lien, but a preference of credit in favor of employees [See *Republic vs. Peralta*, G.R. No. 56668, May 20, 1987, 150 SCRA 37]. This simply means that during bankruptcy, insolvency or liquidation proceedings involving the existing properties of the employer, the employees have the advantage of having their unpaid wages satisfied ahead of certain claims which may be proved therein.

It bears repeating that a preference of credit points out solely the order in which creditors would be paid from the properties of a debtor inventoried and appraised during bankruptcy, insolvency or liquidation proceedings. Moreover, a preference does not exist in any effective way prior to, and apart from, the institution of these proceedings, for it is only then that the legal provisions on concurrence and preference of credits begin to apply. Unlike a lien, a preference of credit does not create in favor of the preferred creditor a charge or proprietary interest upon any particular property of the debtor. Neither does it vest as a matter of course upon the mere accrual of a money claim against the debtor. Certainly, the debtor could very well sell, mortgage or pledge his property, and convey good

title thereon, to third parties free from such preference [Kuenzle & Streiff vs. Villanueva, supra].

Incidentally, the Court is not unmindful of the 1989 amendments to the article introduced by Section 1, R.A. No. 6715 [March 21, 1989]. Article 110 of the Labor Code as amended reads:

WORKER PREFERENCE IN CASE OF BANKRUPTCY. — In the event of bankruptcy or liquidation of an employer's business, his workers shall enjoy first preference as regards their unpaid wages and other monetary claims, any provision of law to the contrary notwithstanding. Such unpaid wages and monetary claims shall be paid in full before the claims of the Government and other creditors may be paid. [Amendments indicated.].

However, these amendments only relate to the scheme of concurrence and preference of credits; they do not affect the issues heretofore discussed regarding the applicability of Article 110 to the attendant facts.

WHEREFORE, considering the foregoing, the present petition is hereby **GRANTED**. The assailed order dated July 29, 1987 is **SET ASIDE** and the temporary restraining order issued by the Court on August 27, 1987 is made **PERMANENT**.

SO ORDERED.

Fernan, C.J., Gutierrez, Jr., Feliciano and Bidin, JJ., concur.