

THIRD DIVISION

[G.R. No. 161407, June 05, 2009]

**JOAQUIN VILLEGAS AND EMMA M. VILLEGAS, PETITIONERS, VS.
RURAL BANK OF TANJAY, INC., RESPONDENT.**

DECISION

NACHURA, J.:

This petition for review on *certiorari* under Rule 45 of the Rules of Court assails the Court of Appeals (CA) Decision^[1] in CA-G.R. CV No. 40613 which affirmed with modification the Regional Trial Court (RTC) Decision in Civil Case No. 9570.^[2]

The facts, as summarized by the CA, follow.

Sometime in June, 1982, [petitioners], spouses Joaquin and Emma Villegas, obtained an agricultural loan of P350,000.00 from [respondent] Rural Bank of Tanjay, Inc. The loan was secured by a real estate mortgage on [petitioners'] residential house and 5,229 - sq.m. lot situated in Barrio Bantayan, Dumaguete City and covered by TCT No. 12389.

For failure of [petitioners] to pay the loan upon maturity, the mortgage was extrajudicially foreclosed. At the foreclosure sale, [respondent], being the highest bidder, purchased the foreclosed properties for P367,596.16. Thereafter, the Sheriff executed in favor of [respondent] a certificate of sale, which was subsequently registered with the Registry of Deeds of Dumaguete City.

[Petitioners] failed to redeem the properties within the one-year redemption period.

In May, 1987, [respondent] and [petitioner] Joaquin Villegas, through his attorney-in-fact[,] Marilen Victoriano, entered into an agreement denominated as "Promise to Sell," whereby [respondent] promised to sell to [petitioners] the foreclosed properties for a total price of P713,312.72, payable within a period of five (5) years. The agreement reads in part:

PROMISE TO SELL

x x x x

WITNESSETH:

x x x x

2) That for and in consideration of SEVEN HUNDRED THIRTEEN THOUSAND AND THREE HUNDRED TWELVE & 72/100 PESOS (P713,312.72), the VENDOR do hereby promise to sell, transfer, and convey unto the VENDEE, their heirs, successors and assigns, all its rights, interests and participations over the above parcel of land with all the improvements thereon and a residential house.

3) That upon signing of this Promise To Sell, the VENDEE shall agree to make payment of P250,000.00 (Philippine Currency) and the balance of P463,312.72 payable in equal yearly installments plus interest based on the prevailing rate counting from the date of signing this Promise to Sell for a period of five (5) years.

X X X X

5) Provided further, that in case of a delay in any yearly installment for a period of ninety (90) days, this sale will become null and void and no further effect or validity; and provided further, that payments made shall be reimbursed (returned) to the VENDEE less interest on the account plus additional 15% liquidated damages and charges.

Upon the signing of the agreement, [petitioners] gave [respondent] the sum of P250,000.00 as down payment. [Petitioners], however, failed to pay the first yearly installment, prompting [respondent] to consolidate its ownership over the properties. Accordingly, TCT No. 12389 was cancelled and a new one, TCT No. 19042, (Exh. 14) was issued in [respondent's] name on November 8, 1989. Thereafter, [respondent] took possession of the properties. Hence, the action by [petitioners for declaration of nullity of loan and mortgage contracts, recovery of possession of real property, accounting and damages and, in the alternative, repurchase of real estate] commenced on January 15, 1990.

In resisting the complaint, [respondent] averred that [petitioners] have absolutely no cause of action against it, and that the complaint was filed only to force it to allow [petitioners] to reacquire the foreclosed properties under conditions unilaterally favorable to them.

X X X X

After trial on the merits, the [RTC] rendered a Decision dismissing the complaint, disposing as follows:

"In the light of the foregoing, it is considered opinion of this Court, that [petitioners] failed to prove by preponderance of evidence their case and therefore the herein complaint is ordered dismissed. [Petitioners] are ordered to pay [respondent] the sum of P3,000.00 as attorney's fees and to pay costs without pronouncement as to counterclaim.

SO ORDERED."^[3]

On appeal by both parties, the CA affirmed with modification the RTC's ruling, thus:

WHEREFORE, the appealed Decision is hereby **MODIFIED** by (a) **ORDERING** [respondent] to reimburse [petitioners] their down payment of P250,000.00 and (b) **DELETING** the award of attorney's fees to [respondent].

SO ORDERED.^[4]

Hence, this appeal by *certiorari* raising the following issues:

- (1) The Court of Appeals erred in not holding that the loan and mortgage contracts are null and void *ab initio* for being against public policy;
- (2) The Court of Appeals erred in not holding that, by reason of the fact that the loan and mortgage contracts are null and void *ab initio* for being against public policy, the doctrine of estoppel does not apply in this case;
- (3) The Court of Appeals erred in not finding that the addendum on the promissory notes containing an escalation clause is null and void *ab initio* for not being signed by petitioner Emma M. Villegas, wife of petitioner Joaquin Villegas, there being a showing that the companion real estate mortgage involves conjugal property. x x x.
- (4) The Court of Appeals erred in not finding that the addendum on the promissory notes containing an escalation clause is null and void *ab initio* for being so worded that the implementation thereof would deprive petitioners due process guaranteed by [the] constitution, the petitioners not having been notified beforehand of said implementation.^[5]

Notwithstanding petitioners' formulation of the issues, the core issue for our resolution is whether petitioners may recover possession of the mortgaged properties.

The petition deserves scant consideration and ought to have been dismissed outright. Petitioners are precluded from seeking a declaration of nullity of the loan and mortgage contracts; they are likewise barred from recovering possession of the subject property.

Petitioners insist on the nullity of the loan and mortgage contracts. Unabashedly, petitioners admit that the loan (and mortgage) contracts were made to appear as several sugar crop loans not exceeding P50,000.00 each - even if they were not - just so the respondent rural bank could grant and approve the same pursuant to Republic Act (R.A.) No. 720, the Rural Banks Act. Petitioners boldly enumerate the following circumstances that show that these loans were obtained in clear contravention of R.A. No. 720:

- (a) The petitioners never planted sugar cane on any parcel of agricultural land;
- (b) The mortgaged real estate is residential, with a house,

- located in the heart of Dumaguete City, with an area of only one-half (1/2) hectare;
- (c) Petitioners never planted any sugar cane on this one-half (1/2) hectare parcel of land;
 - (d) Petitioners were never required to execute any chattel mortgage on standing crops;
 - (e) To make it appear that the petitioners were entitled to avail themselves of loan benefits under Republic Act No. 720, Rural Banks Act, respondent made them sign promissory notes for P350,000.00 in split amounts not exceeding P50,000.00 each.^[6]

In short, petitioners aver that the sugar crop loans were merely simulated contracts and, therefore, without any force and effect.

Articles 1345 and 1346 of the Civil Code are the applicable laws, and they unmistakably provide:

Art. 1345. Simulation of a contract may be absolute or relative. The former takes place when the parties do not intend to be bound at all; the latter, when the parties conceal their true agreement.

Art. 1346. An absolutely simulated or fictitious contract is void. A relative simulation, when it does not prejudice a third person and is not intended for any purpose contrary to law, morals, good customs, public order or public policy binds the parties to their real agreement.

Given the factual antecedents of this case, it is obvious that the sugar crop loans were relatively simulated contracts and that both parties intended to be bound thereby. There are two juridical acts involved in relative simulation-- the *ostensible act* and the *hidden act*.^[7] The *ostensible act* is the contract that the parties pretend to have executed while the *hidden act* is the true agreement between the parties.^[8] To determine the enforceability of the actual agreement between the parties, we must discern whether the concealed or hidden act is lawful and the essential requisites of a valid contract are present.

In this case, the juridical act which binds the parties are the loan and mortgage contracts, *i.e.*, petitioners' procurement of a loan from respondent. Although these loan and mortgage contracts were concealed and made to appear as sugar crop loans to make them fall within the purview of the Rural Banks Act, all the essential requisites of a contract^[9] were present. However, the purpose thereof is illicit, intended to circumvent the Rural Banks Act requirement in the procurement of loans.^[10] Consequently, while the parties intended to be bound thereby, the agreement is void and inexistent under Article 1409^[11] of the Civil Code.

In arguing that the loan and mortgage contracts are null and void, petitioners would impute all fault therefor to respondent. Yet, petitioners' averments evince an obvious knowledge and voluntariness on their part to enter into the simulated contracts. We find that fault for the nullity of the contract does not lie at respondent's feet alone, but at petitioners' as well. Accordingly, neither party can maintain an action against the other, as provided in Article 1412 of the Civil Code:

Art. 1412. If the act in which the unlawful or forbidden cause consists does not constitute a criminal offense, the following rules shall be observed:

(1) When the fault is on the part of both contracting parties, neither may recover what he has given by virtue of the contract, or demand the performance of the other's undertaking;

(2) When only one of the contracting parties is at fault, he cannot recover what he has given by reason of the contract, or ask for the fulfillment of what has been promised him. The other, who is not at fault, may demand the return of what he has given without any obligation to comply with his promise.

Petitioners did not come to court with clean hands. They admit that they never planted sugarcane on any property, much less on the mortgaged property. Yet, they eagerly accepted the proceeds of the simulated sugar crop loans. Petitioners readily participated in the ploy to circumvent the Rural Banks Act and offered no objection when their original loan of P350,000.00 was divided into small separate loans not exceeding P50,000.00 each. Clearly, both petitioners and respondent are in *pari delicto*, and neither should be accorded affirmative relief as against the other.

In *Tala Realty Services Corp. v. Banco Filipino Savings and Mortgage Bank*,^[12] we held that when the parties are in *pari delicto*, neither will obtain relief from the court, thus:

The Bank should not be allowed to dispute the sale of its lands to Tala nor should Tala be allowed to further collect rent from the Bank. The clean hands doctrine will not allow the creation or the use of a juridical relation such as a trust to subvert, directly or indirectly, the law. Neither the bank nor Tala came to court with clean hands; neither will obtain relief from the court as one who seeks equity and justice must come to court with clean hands. By not allowing Tala to collect from the Bank rent for the period during which the latter was arbitrarily closed, both Tala and the Bank will be left where they are, each paying the price for its deception.

^[13]

Petitioners stubbornly insist that respondent cannot invoke the *pari delicto* doctrine, ostensibly because of our *obiter* in *Enrique T. Yuchengco, Inc., et al. v. Velayo*.^[14]

In *Yuchengco*, appellant sold 70% of the subscribed and outstanding capital stock of a Philippine corporation, duly licensed as a tourist operator, to appellees without the required prior notice and approval of the Department of Tourism (DOT). Consequently, the DOT cancelled the corporation's Local Tour Operator's License. In turn, appellees asked for a rescission of the sale and demanded the return of the purchase price.

We specifically ruled therein that the *pari delicto* doctrine is not applicable, because:

The obligation to secure prior Department of Tourism approval devolved upon the defendant (herein appellant) for it was he as the owner vendor who had the duty to give clear title to the properties he was conveying. It was he alone who was charged with knowing about rules attendant to a