

SECOND DIVISION

[G.R. No. 177886, November 27, 2008]

**SPOUSES LEOPOLDO S. VIOLA AND MERCEDITA VIOLA,
PETITIONERS, VS. EQUITABLE PCI BANK, INC., RESPONDENT.**

DECISION

CARPIO MORALES, J.:

Via a contract denominated as "CREDIT LINE AND REAL ESTATE MORTGAGE AGREEMENT FOR PROPERTY LINE"^[1] (*Credit Line Agreement*) executed on March 31, 1997, Leo-Mers Commercial, Inc., as the Client, and its officers spouses Leopoldo and Mercedita Viola (petitioners) obtained a loan through a credit line facility in the maximum amount of P4,700,000.00 from the Philippine Commercial International Bank (PCI Bank), which was later merged with Equitable Bank and became known as Equitable PCI Bank, Inc. (respondent).

The *Credit Line Agreement* stipulated that the loan would bear interest at the "prevailing PCIBank lending rate" per annum on the principal obligation and a "penalty fee of three percent (3%) per month on the outstanding amount."

To secure the payment of the loan, petitioners executed also on March 31, 1997 a "Real Estate Mortgage"^[2] in favor of PCIBank over their two parcels of land covered by Transfer Certificates of Title No. N-113861 (consisting of 300 square meters, more or less) and N-129036 (consisting of 446 square meters, more or less) of the Registry of Deeds of Marikina.

Petitioners availed of the full amount of the loan. Subsequently, they made partial payments which totaled P3,669,210.67. By respondent's claim, petitioner had since November 24, 2000 made no further payments and despite demand, they failed to pay their outstanding obligation which, as of September 30, 2002, totaled P14,024,623.22, broken down as follows:

- | | |
|---|---------------|
| (a) Principal obligation | P4,783,254.69 |
| (b) Past due interest from 11/24/00 to 09/30/02 at 15% interest | P1,345,290.38 |
| (c) Penalty at 3% per month from | P7,896,078.15 |

03/31/98 to
02/23/02

P14,024,623.22^[3] (Underscoring supplied)

Respondent thus extrajudicially foreclosed the mortgage before the Office of the Clerk of Court & Ex-Officio Provincial Sheriff of the Regional Trial Court (RTC) of Marikina City. The mortgaged properties were sold on April 10, 2003 for P4,284,000.00 at public auction to respondent, after which a Certificate of Sale dated April 21, 2003^[4] was issued.

More than five months later or on October 8, 2003, petitioners filed a complaint^[5] for annulment of foreclosure sale, accounting and damages before the Marikina RTC, docketed as Civil Case No. 2003-905-MK and raffled to Branch 192. Petitioners alleged, *inter alia*, that they had made substantial payments of P3,669,210.67 receipts of which were issued without respondent specifying "whether the payment was for interest, penalty or the principal obligation;" that based on respondent's statement of account, not a single centavo of their payments was applied to the principal obligation; that every time respondent sent them a statement of account and demand letters, they requested for a proper accounting for the purpose of determining their actual obligation, but all their requests were unjustifiably ignored on account of which they were forced to discontinue payment; that "the foreclosure proceedings and auction sale were not only irregularly and prematurely held but were null and void because the mortgage debt is only P2,224,073.31 on the principal obligation and P1,455,137.36 on the interest, or a total of only P3,679,210.67 as of April 15, 2003, but the mortgaged properties were sold to satisfy an inflated and erroneous principal obligation of P4,783,254.69, *plus 3% penalty fee per month or 33% per year and 15% interest per year, which amounted to P14,024,623.22 as of September 30, 2002*;" that "the parties never agreed and stipulated in the real estate mortgage contract" that the 15% interest per annum on the principal loan and the 3% penalty fee per month on the outstanding amount would be covered or secured by the mortgage; that assuming respondent could impose such interest and penalty fee, the same are "exorbitant, unreasonable, iniquitous and unconscionable, hence, must be reduced;" and that respondent is only allowed to impose the legal rate of interest of 12% per annum on the principal loan absent any stipulation thereon."^[6]

In its Answer, respondent denied petitioners' assertions, contending, *inter alia*, that the absence of stipulation in the mortgage contract securing the payment of 15% interest per annum on the principal loan, as well as the 3% penalty fee per month on the outstanding amount, is immaterial since the mortgage contract is "a mere accessory contract which must take its bearings from the principal *Credit Line Agreement*."^[7]

During the pre-trial conference, the parties defined as sole issue in the case whether the mortgage contract **also secured** the payment of 15% interest per annum on the principal loan of P4,700,000.00 and the 3% penalty fee per month on the outstanding amount, which interest and penalty fee are stipulated only in the *Credit Line Agreement*.^[8]

By Decision^[9] of September 14, 2005, the trial court sustained respondent's

affirmative position on the issue but found the questioned interest and penalty fee "excessive and exorbitant." Thus, it equitably reduced the interest on the principal loan from 15% to 12% per annum and the penalty fee per month on the outstanding amount from 3% to 1.5% per month.

Accordingly, the court nullified the foreclosure proceedings and the Certificate of Sale subsequently issued, "without prejudice" to the holding anew of foreclosure proceedings based on the "re-computed amount" of the indebtedness, "if the circumstances so warrant."

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

WHEREFORE, judgment is hereby rendered as follows:

1) The interest on the principal loan in the amount of Four Million Seven Hundred Thousand (P4,700,000.00) Pesos should be recomputed at 12% per annum;

2) The 3% per month penalty on delinquent account as stipulated by the parties in the Credit Line Contract dated March 31, 1997 is hereby REDUCED to 1.5% per month;

3) The foreclosure sale conducted on April 10, 2003 by the Clerk of Court and Ex-Officio Sheriff of Marikina, to satisfy the plaintiff's mortgage indebtedness, and the Certificate of Sale issued as a consequence of the said proceedings, are declared NULL and VOID, without prejudice to the conduct of another foreclosure proceedings on the basis of the re-computed amount of the plaintiff's indebtedness, if the circumstances so warrant.

No pronouncement as to costs.

SO ORDERED. (Underscoring supplied)

Petitioners filed a Motion for Partial Reconsideration,^[10] contending that the penalty fee per month on the outstanding amount should have been taken out of the coverage of the mortgage contract as it was not stipulated therein. By Order dated December 6, 2005, the trial court denied the motion.

On appeal by petitioners, the Court of Appeals, by Decision^[11] of February 21, 2007, dismissed the same for lack of merit, holding that "the Real Estate Mortgage **covers not only** the principal amount [of P4,700,000.00] but also the `interest and **bank charges**,' which [phrase bank charges] refers to the **penalty charges** stipulated in the Credit Line Agreement."^[12]

Petitioners' Motion for Reconsideration having been denied by Resolution^[13] of May 16, 2007, they filed the present Petition for Review on *Certiorari*, alleging that -

THE HONORABLE COURT OF APPEALS COMMITTED A REVERSIBLE ERROR IN DECIDING THE CASE NOT IN ACCORD WITH LAW AND APPLICABLE DECISIONS OF THE SUPREME COURT BY RULING THAT THERE IS NO AMBIGUITY IN CONSTRUING TOGETHER THE CREDIT LINE AND

MORTGAGE CONTRACTS WHICH PROVIDED CONFLICTING PROVISIONS
AS TO INTEREST AND PENALTY.^[14]

The only issue is whether the mortgage contract also secured the penalty fee per month on the outstanding amount as stipulated in the *Credit Line Agreement*.

The Court holds not.

A mortgage must "sufficiently describe the debt sought to be secured, which description must not be such as to mislead or deceive, and an obligation is not secured by a mortgage unless it comes fairly within the terms of the mortgage."^[15]

In the case at bar, the parties executed two separate documents on March 31, 1997 - the Credit Line Agreement granting the Client a loan through a credit facility in the maximum amount of P4,700,000.00, and the Real Estate Mortgage contract securing the payment thereof. Undisputedly, both contracts were prepared by respondent and written in fine print, single space.

The *Credit Line Agreement* contains the following stipulations on interest and delinquency charges:

A. CREDIT FACILITY

9. INTEREST ON AVAILMENTS

The CLIENT shall pay the BANK interest on each availment against the Credit Facility at the rate of:

PREVAILING PCIBANK LENDING RATE

for the first interest period as defined in A(10) hereof. x x x.

x x x x

15. DELINQUENCY

CLIENT's account shall be considered delinquent if the availments exceed the amount of the line and/or in case the Account is debited for unpaid interest and the Available Balance is insufficient to cover the amount debited. In such cases, the Available Balance shall become negative and the CLIENT shall pay the deficiency immediately in addition to collection expenses incurred by the BANK and a penalty fee of three percent (3%) per month of the outstanding amount to be computed from the day deficiency is incurred up to the date of full payment thereon.

x x x x.^[16] (Underscoring supplied)

The Real Estate Mortgage contract states its coverage, thus:

That for and in consideration of certain loans, credit and other banking facilities obtained x x x from the Mortgagee, the principal amount of which is PESOS FOUR MILLION SEVEN HUNDERED THOUSAND ONLY