Republic of the Philippines
Supreme Court
Manila

THIRD DIVISION

SPOUSES FLORENTINO T. MALLARI and AUREA V. MALLARI,
Petitioners,

- *versus* -

PRUDENTIAL BANK (now BANK OF THE PHILIPPINE ISLANDS),
Respondent.

G.R. No. 197861

Present:

VELASCO, JR., *J.*, *Chairperson*,
PERALTA,
ABAD,
MENDOZA, and
LEONEN, *JJ.*

Promulgated:

JUN 05 2013

x----------x

D E C I S I O N

PERALTA, *J.*:

Before us is a Petition for Review on *Certiorari* under Rule 45, assailing the Decision[1] dated June 17, 2010 and the Resolution[2] dated July 20, 2011 of the Court of Appeals (CA) in CA-G.R. CV No. 65993.

The antecedent facts are as follows:

On December 11, 1984, petitioner Florentino T. Mallari (Florentino) obtained from respondent Prudential Bank-Tarlac Branch (respondent bank), a loan in the amount of ₱300,000.00 as evidenced by Promissory Note (PN)

---

[1] Penned by Associate Justice Juan Q. Enriquez, Jr., with Associate Justices Ramon M. Bato, Jr. and Florito S. Macalino, concurring; *rollo*, pp. 30-37.

[2] *Id.* at 40-41.

No. BD 84-055.[3] Under the promissory note, the loan was subject to an interest rate of 21% per annum (p.a.), attorney's fees equivalent to 15% of the total amount due but not less than ₱200.00 and, in case of default, a penalty and collection charges of 12% p.a. of the total amount due. The loan had a maturity date of January 10, 1985, but was renewed up to February 17, 1985. Petitioner Florentino executed a Deed of Assignment[4] wherein he authorized the respondent bank to pay his loan with his time deposit with the latter in the amount of ₱300,000.00.

On December 22, 1989, petitioners spouses Florentino and Aurea Mallari (petitioners) obtained again from respondent bank another loan of ₱1.7 million as evidenced by PN No. BDS 606-89[5] with a maturity date of March 22, 1990. They stipulated that the loan will bear 23% interest p.a., attorney's fees equivalent to 15% p.a. of the total amount due, but not less than ₱200.00, and penalty and collection charges of 12% p.a. Petitioners executed a Deed of Real Estate Mortgage[6] in favor of respondent bank covering petitioners' property under Transfer Certificate of Title (TCT) No. T-215175 of the Register of Deeds of Tarlac to answer for the said loan.

Petitioners failed to settle their loan obligations with respondent bank, thus, the latter, through its lawyer, sent a demand letter to the former for them to pay their obligations, which when computed up to January 31, 1992, amounted to ₱571,218.54 for PN No. BD 84-055 and ₱2,991,294.82 for PN No. BDS 606-89.

On February 25, 1992, respondent bank filed with the Regional Trial Court (RTC) of Tarlac, a petition for the extrajudicial foreclosure of petitioners' mortgaged property for the satisfaction of the latter's obligation of ₱1,700,000.00 secured by such mortgage, thus, the auction sale was set by the Provincial Sheriff on April 23, 1992.[7]

On April 10, 1992, respondent bank's Assistant Manager sent petitioners two (2) separate Statements of Account as of April 23, 1992, *i.e.*, the loan of ₱300,000.00 was increased to ₱594,043.54, while the ₱1,700,000.00 loan was already ₱3,171,836.18.

On April 20, 1992, petitioners filed a complaint for annulment of mortgage, deeds, injunction, preliminary injunction, temporary restraining order and damages claiming, among others, that: (1) the ₱300,000.00 loan obligation should have been considered paid, because the time deposit with the same amount under Certificate of Time Deposit No. 284051 had already

---

3 *Id.* at 43.
4 *Id.* at 47.
5 *Id* at 44.
6 *Id.* at 45-46.
7 *Id*. at 48.

been assigned to respondent bank; (2) respondent bank still added the ₱300,000.00 loan to the ₱1.7 million loan obligation for purposes of applying the proceeds of the auction sale; and (3) they realized that there were onerous terms and conditions imposed by respondent bank when it tried to unilaterally increase the charges and interest over and above those stipulated. Petitioners asked the court to restrain respondent bank from proceeding with the scheduled foreclosure sale.

Respondent bank filed its Answer with counterclaim arguing that: (1) the interest rates were clearly provided in the promissory notes, which were used in computing for interest charges; (2) as early as January 1986, petitioners' time deposit was made to apply for the payment of interest of their ₱300,000.00 loan; and (3) the statement of account as of April 10, 1992 provided for a computation of interest and penalty charges only from May 26, 1989, since the proceeds of petitioners' time deposit was applied to the payment of interest and penalty charges for the preceding period. Respondent bank also claimed that petitioners were fully apprised of the bank's terms and conditions; and that the extrajudicial foreclosure was sought for the satisfaction of the second loan in the amount of ₱1.7 million covered by PN No. BDS 606-89 and the real estate mortgage, and not the ₱300,000.00 loan covered by another PN No. 84-055.

In an Order[8] dated November 10, 1992, the RTC denied the Application for a Writ of Preliminary Injunction. However, in petitioners' Supplemental Motion for Issuance of a Restraining Order and/or Preliminary Injunction to enjoin respondent bank and the Provincial Sheriff from effecting or conducting the auction sale, the RTC reversed itself and issued the restraining order in its Order[9] dated January 14, 1993.

Respondent bank filed its Motion to Lift Restraining Order, which the RTC granted in its Order[10] dated March 9, 1993. Respondent bank then proceeded with the extrajudicial foreclosure of the mortgaged property. On July 7, 1993, a Certificate of Sale was issued to respondent bank being the highest bidder in the amount of ₱3,500,000.00.

Subsequently, respondent bank filed a Motion to Dismiss Complaint[11] for failure to prosecute action for unreasonable length of time to which petitioners filed their Opposition.[12] On November 19, 1998, the RTC issued its Order[13] denying respondent bank's Motion to Dismiss Complaint.

---

8 Per Presiding Judge Edilberto Aquino; *id.* at 89-93.
9 *Rollo*, pp. 94-96.
10 Per Executive Judge Augusto N. Felix; *id*. at 116-117;
11 *Rollo*, pp. 126-130.
12 *Id*. at 132-133.
13 Per Presiding Judge Edgardo F. Sundiam; *id*. at 134-135;

Trial thereafter ensued. Petitioner Florentino was presented as the lone witness for the plaintiffs. Subsequently, respondent bank filed a Demurrer to Evidence.

On November 15, 1999, the RTC issued its Order[14] granting respondent's demurrer to evidence, the dispositive portion of which reads:

> WHEREFORE, this case is hereby ordered DISMISSED. Considering there is no evidence of bad faith, the Court need not order the plaintiffs to pay damages under the general concept that there should be no premium on the right to litigate.
>
> NO COSTS.
>
> SO ORDERED.[15]

The RTC found that as to the ₱300,000.00 loan, petitioners had assigned petitioner Florentino's time deposit in the amount of ₱300,000.00 in favor of respondent bank, which maturity coincided with petitioners' loan maturity. Thus, if the loan was unpaid, which was later extended to February 17, 1985, respondent bank should had just applied the time deposit to the loan. However, respondent bank did not, and allowed the loan interest to accumulate reaching the amount of ₱594,043.54 as of April 10, 1992, hence, the amount of ₱292,600.00 as penalty charges was unjust and without basis.

As to the ₱1.7 million loan which petitioners obtained from respondent bank after the ₱300,000.00 loan, it had reached the amount of ₱3,171,836.18 per Statement of Account dated April 27, 1993, which was computed based on the 23% interest rate and 12% penalty charge agreed upon by the parties; and that contrary to petitioners' claim, respondent bank did not add the ₱300,000.00 loan to the ₱1.7 million loan obligation for purposes of applying the proceeds of the auction sale.

The RTC found no legal basis for petitioners' claim that since the total obligation was ₱1.7 million and respondent bank's bid price was ₱3.5 million, the latter should return to petitioners the difference of ₱1.8 million. It found that since petitioners' obligation had reached ₱2,991,294.82 as of January 31, 1992, but the certificate of sale was executed by the sheriff only on July 7, 1993, after the restraining order was lifted, the stipulated interest and penalty charges from January 31, 1992 to July 7, 1993 added to the loan already amounted to ₱3.5 million as of the auction sale.

---

14 *Rollo*, pp. 199-204.

15 *Id*. at 204.

The RTC found that the 23% interest rate p.a., which was then the prevailing loan rate of interest could not be considered unconscionable, since banks are not hospitable or equitable institutions but are entities formed primarily for profit. It also found that Article 1229 of the Civil Code invoked by petitioners for the reduction of the interest was not applicable, since petitioners had not paid any single centavo of the ₱1.7 million loan which showed they had not complied with any part of the obligation.

Petitioners appealed the RTC decision to the CA. A Comment was filed by respondent bank and petitioners filed their Reply thereto.

On June 17, 2010, the CA issued its assailed Decision, the dispositive portion of which reads:

> **WHEREFORE**, the instant appeal is hereby **DENIED**. The Order dated November 15, 1999 issued by the Regional Trial Court (RTC), Branch 64, Tarlac City, in Civil Case No. 7550 is hereby **AFFIRMED**.[16]

The CA found that the time deposit of ₱300,000.00 was equivalent only to the principal amount of the loan of ₱300,000.00 and would not be sufficient to cover the interest, penalty, collection charges and attorney's fees agreed upon, thus, in the Statement of Account dated April 10, 1992, the outstanding balance of petitioners' loan was ₱594,043.54. It also found not persuasive petitioners' claim that the ₱300,000.00 loan was added to the ₱1.7 million loan. The CA, likewise, found that the interest rates and penalty charges imposed were not unconscionable and adopted *in toto* the findings of the RTC on the matter.

Petitioners filed their Motion for Reconsideration, which the CA denied in a Resolution dated July 20, 2011.

Hence, petitioners filed this petition for review arguing that:

> THE HON. COURT OF APPEALS ERRED IN AFFIRMING THE ORDER OF THE RTC-BRANCH 64, TARLAC CITY, DATED NOVEMBER 15, 1999, DESPITE THE FACT THAT THE SAME IS CONTRARY TO SETTLED JURISPRUDENCE ON THE MATTER.[17]

The issue for resolution is whether the 23% p.a. interest rate and the 12% p.a. penalty charge on petitioners' ₱1,700,000.00 loan to which they agreed upon is excessive or unconscionable under the circumstances.

---

16 *Id*. at 36. (Emphasis in the original.)

17 *Id.* at 19.

Parties are free to enter into agreements and stipulate as to the terms and conditions of their contract, but such freedom is not absolute. As Article 1306 of the Civil Code provides, "The contracting parties may establish such stipulations, clauses, terms and conditions as they may deem convenient, provided they are not contrary to law, morals, good customs, public order, or public policy." Hence, if the stipulations in the contract are valid, the parties thereto are bound to comply with them, since such contract is the law between the parties. In this case, petitioners and respondent bank agreed upon on a 23% p.a. interest rate on the ₱1.7 million loan. However, petitioners now contend that the interest rate of 23% p.a. imposed by respondent bank is excessive or unconscionable, invoking our ruling in *Medel v. Court of Appeals,*[18] *Toring v. Spouses Ganzon-Olan,*[19] and *Chua v. Timan.*[20]

We are not persuaded.

In *Medel v. Court of Appeals*,[21] we found the stipulated interest rate of *66%* p.a. or a 5.5% per month on a ₱500,000.00 loan excessive, unconscionable and exorbitant, hence, contrary to morals if not against the law and declared such stipulation void. In *Toring v. Spouses Ganzon-Olan*,[22] the stipulated interest rates involved were 3% and 3.81% per month on a ₱10 million loan, which we find under the circumstances excessive and reduced the same to 1% per month. While in *Chua v. Timan*,[23] where the stipulated interest rates were 7% and 5% a month, which are equivalent to 84% and 60% p.a., respectively, we had reduced the same to 1% per month or 12% p.a. We said that we need not unsettle the principle we had affirmed in a plethora of cases that stipulated interest rates of 3% per month and higher are excessive, unconscionable and exorbitant, hence, the stipulation was void for being contrary to morals.[24]

In this case, the interest rate agreed upon by the parties was only *23% p.a.*, or less than 2% per month, which are much lower than those interest rates agreed upon by the parties in the above-mentioned cases. Thus, there is no similarity of factual milieu for the application of those cases.

We do not consider the interest rate of 23% p.a. agreed upon by petitioners and respondent bank to be unconscionable.

---

18 359 Phil. 820 (1998).
19 G.R. No. 168782, October 10, 2008, 568 SCRA 376.
20 G.R. No. 170452, August 13, 2008, 562 SCRA 146.
21 *Supra* note 18.
22 *Supra* note 19.
23 *Supra* note 20.
24 *Id*. at 149-150.

In *Villanueva v. Court of Appeals*,[25] where the issue raised was whether the 24% p.a. stipulated interest rate is unreasonable under the circumstances, we answered in the negative and held:

> In *Spouses Zacarias Bacolor and Catherine Bacolor v. Banco Filipino Savings and Mortgage Bank, Dagupan City Branch*, this Court held that the interest rate of 24% *per annum* on a loan of ₱244,000.00, agreed upon by the parties, may not be considered as unconscionable and excessive. As such, the Court ruled that the borrowers cannot renege on their obligation to comply with what is incumbent upon them under the contract of loan as the said contract is the law between the parties and they are bound by its stipulations.
>
> Also, in *Garcia v. Court of Appeals*, this Court sustained the agreement of the parties to a 24% *per annum* interest on an ₱8,649,250.00 loan finding the same to be reasonable and clearly evidenced by the amended credit line agreement entered into by the parties as well as two promissory notes executed by the borrower in favor of the lender.
>
> Based on the above jurisprudence, the Court finds that the 24% *per annum* interest rate, provided for in the subject mortgage contracts for a loan of ₱225,000.00, may not be considered unconscionable. Moreover, considering that the mortgage agreement was freely entered into by both parties, the same is the law between them and they are bound to comply with the provisions contained therein.[26]

Clearly, jurisprudence establish that the 24% p.a. stipulated interest rate was not considered unconscionable, thus, the 23% p.a. interest rate imposed on petitioners' loan in this case can by no means be considered excessive or unconscionable.

We also do not find the stipulated 12% p.a. penalty charge excessive or unconscionable.

In *Ruiz v. CA*,[27] we held:

> The 1% surcharge on the principal loan for every month of default is valid. This surcharge or penalty stipulated in a loan agreement in case of default partakes of the nature of liquidated damages under Art. 2227 of the New Civil Code, and is separate and distinct from interest payment. Also referred to as a penalty clause, it is expressly recognized by law. It is an accessory undertaking to assume greater liability on the part of an obligor in case of breach of an obligation. The obligor would then be bound to pay the stipulated amount of indemnity without the necessity of proof on the existence and on the measure of damages caused by the breach. x x x[28]

---

25 G.R. No. 163433, August 22, 2011, 655 SCRA 707.

26 *Id*. at 716-717. (Italics in the original)

27 449 Phil. 419 (2003).

28 *Id*. at 435.

And in *Development Bank of the Philippines v. Family Foods Manufacturing Co., Ltd.,*[29] we held that:

> x x x The enforcement of the penalty can be demanded by the creditor only when the non-performance is due to the fault or fraud of the debtor. The non-performance gives rise to the presumption of fault; in order to avoid the payment of the penalty, the debtor has the burden of proving an excuse – the failure of the performance was due to either *force majeure* or the acts of the creditor himself.[30]

Here, petitioners defaulted in the payment of their loan obligation with respondent bank and their contract provided for the payment of 12% p.a. penalty charge, and since there was no showing that petitioners' failure to perform their obligation was due to *force majeure* or to respondent bank's acts, petitioners cannot now back out on their obligation to pay the penalty charge. A contract is the law between the parties and they are bound by the stipulations therein.

WHEREFORE, the petition for review is **DENIED**. The Decision dated June 17, 2010 and the Resolution dated July 20, 2011 of the Court of Appeals are hereby **AFFIRMED**.

SO ORDERED.

DIOSDADO M. PERALTA
Associate Justice

WE CONCUR:

PRESBITERO J. VELASCO, JR.
Associate Justice
Chairperson

ROBERTO A. ABAD
Associate Justice

JOSE CATRAL MENDOZA
Associate Justice

---

29 G.R. No. 180458, July 30, 2009, 594 SCRA 461.

30 *Development Bank of the Philippines v. Family Foods Manufacturing Co., Ltd., supra*, at 473, citing *Development Bank of the Philippines v. Go*, G.R. No. 168779, September 14, 2007, 533 SCRA 460, 470-471.

MARVIC MARIO VICTOR F. LEONEN
Associate Justice

ATTESTATION

I attest that the conclusions in the above Decision had been reached in consultation before the case was assigned to the writer of the opinion of the Court's Division.

PRESBITERO J. VELASCO, JR.
Associate Justice
Chairperson, Third Division

CERTIFICATION

Pursuant to Section 13, Article VIII of the Constitution and the Division Chairperson's Attestation, I certify that the conclusions in the above Decision had been reached in consultation before the case was assigned to the writer of the opinion of the Court's Division.

MARIA LOURDES P. A. SERENO
Chief Justice