Republic of the Philippines
SUPREME COURT
Manila

THIRD DIVISION

SPOUSES TAGUMPAY N. ALBOS and AIDA C. ALBOS, Petitioners,	**G.R. No. 210831**
	Present:
- versus -	VELASCO, JR., *J.*, Chairperson, PERALTA,
SPOUSES NESTOR M. EMBISAN and ILUMINADA A. EMBISAN, DEPUTY SHERIFF MARINO V. CACHERO, and the REGISTER OF DEEDS OF QUEZON CITY, Respondents.	VILLARAMA, JR., REYES, and JARDELEZA, *JJ.*
	Promulgated:
	November 26, 2014

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DECISION

VELASCO, JR., *J.*:

Nature of the Case

Before the Court is a Petition for Review on Certiorari under Rule 45 of the Rules of Court seeking the reversal and the setting aside of the Decision[1] of the Court of Appeals (CA) dated May 29, 2013 and its Resolution dated January 13, 2014 in CA-G.R. CV No. 93667. Said rulings upheld the validity of the extra-judicial foreclosure sale over the property that petitioners, spouses Tagumpay and Aida Albos, mortgaged in favor of private respondents.

The Facts

On October 17, 1984, petitioners entered into an agreement, denominated as "*Loan with Real Estate Mortgage,*"[2] with respondent spouses Nestor and Iluminada Embisan (spouses Embisan) in the amount of ₱84,000.00 payable within 90 days with a monthly interest rate of 5%. To secure the indebtedness, petitioners mortgaged to the spouses Embisan a parcel of land in Project 3, Quezon City, measuring around 207.6 square meters and registered under their name, as evidenced by Transfer Certificate Title No. 257697.[3]

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[1] Penned by Associate Justice Rodil V. Zalameda and concurred in by Presiding Justice Andres B. Reyes, Jr. and Associate Justice Ramon M. Bato, Jr.

[2] *Rollo*, pp. 85-86.

[3] Id. at 100-102.

For failure to settle their account upon maturity, petitioner Aida Albos requested and was given an extension of eleven (11) months, or until December 17, 1985, within which to pay the loan obligation. However, when the said deadline came anew, petitioners once again defaulted and so, on agreement of the parties, another extension of five (5) months, or until May 17, 1986, was set.

May 17, 1986 came and went but the obligation remained unpaid. Thus, when the petitioners requested a third extension, as will later be alleged by the respondent spouses, an additional eight (8) months was granted on the condition that the monthly 5% interest from then on, i.e. June 1986 onwards, will be compounded. This stipulation, however, was not reduced in writing.

On February 9, 1987, respondent spouses addressed a letter[4] to petitioners demanding the payment of ₱234,021.90, representing the unpaid balance and interests from the loan. This was followed, on April 14, 1987, by another letter[5] of the same tenor, but this time demanding from the petitioners the obligation due amounting to ₱258,009.15.

Obviously in a bid to prevent the foreclosure of their mortgaged property, petitioners paid respondent spouses the sum of ₱44,500.00 on October 2, 1987. The respondent spouses accepted the partial payment of the principal loan amount owed to them, which, based on the Statement of Account[6] the respondent spouses prepared, by that time, has already ballooned to ₱296,658.70. As extrapolated from the Statement of Account:

Month	Year	Loan	Interest	Payment	Balance
October	1984	84,000.00			84,000.00
November	1984		4,200.00	8,000.00	80,200.00
December	1984		4,200.00		84,400.00
January	1985		4,200.00	4,000.00	84,600.00
February	1985		4,200.00		88,800.00
March	1985		4,200.00		93,000.00
April	1985		4,200.00		97,200.00
May	1985		4,200.00		101,400.00
June	1985		4,200.00		105,600.00
July	1985		4,200.00		109,800.00
August	1985		4,200.00		114,000.00
September	1985		4,200.00		118,200.00
October	1985		4,200.00		122,400.00
November	1985		4,200.00		126,600.00
December	1985		4,200.00		130,800.00
January	1986		4,200.00		135,000.00
February	1986		4,200.00		139,200.00
March	1986		4,200.00		143,400.00
April	1986		4,200.00		147,600.00
May	1986		4,200.00		151,800.00

[4] Id. at 89.
[5] Id. at 90.
[6] Id. at 95.

June	1986		7,590.00		159,390.00
July	1986		7,969.50		167,359.50
August	1986		8,367.98		175,727.45
September	1986		8,786.37		184,513.82
October	1986		9,225.69		192,739.50
November	1986		9,417.50		202,157.00
December	1986		10,107.75		212,264.75
January	1987		10,613.25		222,878.00
February	1987		11,143.90		234,021.90
March	1987		11,701.10		245,723.00
April	1987		12,286.15		258,009.15
May	1987		12,900.45		270,909.60
June	1987		13,545.48		284,455.10
July	1987		14,222.75		298,677.85
August	1987		14,933.90		313,611.75
September	1987		15,680.60		329,292.35
October	1987			44,500.00	284,792.35
Interest for 15 days			7,119.80		291,912.15
Interest for 10 days			4,746.55		**296,658.70**

Due to petitioners' failure to settle their indebtedness, respondent spouses proceeded to extra-judicially foreclose the mortgaged property on October 12, 1987. At the auction sale conducted by the respondent sheriff, respondent spouses emerged as the highest bidders at □330,000.00 and were later issued a Sheriff's Certificate of Sale.[7]

The property was never redeemed, and so the respondent spouses executed an Affidavit of Consolidation[8] over the property on November 23, 1988. The affidavit was subsequently registered with the Registry of Deeds of Quezon City, consolidating ownership to the spouses Embisan. Petitioners alleged that afterwards, on February 4, 1989, they were pressured by the respondent spouses to execute a Contract of Lease[9] over the property wherein the petitioners, as lessees, are obligated to pay the respondent spouses, as lessors, monthly rent in the amount of □2,500.00.

On August 14, 1989, herein petitioners filed a complaint for the annulment of the Loan with Real Estate Mortgage, Certificate of Sale, Affidavit of Consolidation, Deed of Final Sale, and Contract of Lease before the Regional Trial Court of Quezon City (RTC). In their complaint, docketed as Civil Case No. 89-3246, and later raffled to Branch 99 of the court, petitioners alleged that the foreclosure sale is void because respondents only released □60,000.00 out of the □84,000.00 amount loaned, which has already been paid. As petitioner Aida Albos testified during trial, she was able to pay □50,000 out of the □60,000 principal loan released, and also □4,500.00 monthly interests, as evidenced by receipts dated December 19, 1984 and February 9, 1985.[10]

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[7] Id. at 96.
[8] Id. at 99.
[9] Id. at 107.
[10] Id. at 57.

In their Answer, the spouses Embisan countered that the loan was legally and validly entered at arms length after a series of meetings and negotiations; that petitioners agreed to pay compounded interest in exchange for extending the payment period the third time; that never during the life of the mortgage did petitioners pay □50,000.00; and, that petitioners, having defaulted, left the spouses Embisan with no other option except to extra-judicially foreclose the property security as stipulated in the mortgage.

Ruling of the Trial Court

Following trial, the RTC rendered a Decision[11] on December 15, 2008 dismissing the complaint for lack of merit, the dispositive portion of which reads:

> **WHEREFORE,** in view of the foregoing considerations, the complaint filed by plaintiff is **DISMISSED** for lack of merit.
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> Defendants' counterclaim is denied.
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> SO OREDERED.

In so doing, the trial court did not give credence to petitioners' claim that only □60,000.00 of the loaned amount was released to them. It also found that between October 17, 1984 to October 28, 1987, petitioners only paid the total amount of □56,000.00, which is not sufficient to cover both the principal loan and the accrued interest. In addition, the trial court shrugged aside petitioners' contention that they were forced to affix their signatures in the adverted Contract of Lease, adding that having signed the lease agreement, they were estopped from asserting title over the property.

Petitioners filed a Motion for Reconsideration, but the same was denied by the trial court through a Resolution dated January 13, 2014. Aggrieved, they elevated the case to the CA.

Ruling of the Court of Appeals

On appeal, petitioners argued that the imposition by the respondent spouses of a 5% compounded interest on the loan, without the petitioners' consent or knowledge, is fraudulent and contrary to public morals. Respondents, on the other hand, insisted that the compounding of the interest was agreed upon as a condition for the third and final extension of time given for the petitioners to make good their promise to pay.

On May 29, 2013, the CA promulgated the assailed Decision, affirming *in toto* the ruling of the trial court. The appellate court held that, under the circumstances, inasmuch as the request for the third extension—for another eight months—was made after the expiration of one year and four months from when the payment first became due, the agreement to

[11] Id. at 132-135.

compound the interest was just and reasonable. It added that it was precisely the petitioners' repeated non-compliance which prompted the imposition of a compounded interest rate and, therefore, petitioners could no longer feign ignorance of its imposition.

Through the challenged Resolution dated January 13, 2014, the CA denied petitioners' Motion for Reconsideration.

Hence, the instant petition.

The Issues

Petitioners anchor their plea for the reversal of the assailed Decision on the following grounds:[12]

I.

THERE IS NO DOCUMENTARY PROOF TO SHOW THAT THE PETITIONERS AGREED IN WRITING TO THE IMPOSITION OF THE 5% COMPOUNDED MONTHLY INTEREST, CONTRARY TO ARTICLE 1956 OF THE CIVIL CODE

II.

THE 5% COMPOUNDED MONTHLY INTEREST UNILATERALLY IMPOSED BY RESPONDENT EMBISAN ON THE PETITIONERS IS EXCESSIVE, EXORBITANT, OPPRESSIVE, INIQUITOUS AND UNCONSCIONABLE, THEREFORE, THE SAME IS VOID FOR BEING CONTRARY TO LAW AND MORALS

III.

THE FORECLOSURE PROCEEDINGS INSTITUTED BY THE RESPONDENT SPOUSES EMBISAN SHOULD BE NULLIFIED FOR BEING BASED ON A WRONG COMPUTATION OF THE OUTSTANDING LOAN OF THE PETITIONERS WHICH WAS WRONGLY COMPUTED ON THE BASIS OF A 5% COMPOUNDED MONTHLY INTEREST

Succinctly put, the pivotal issue to be resolved is whether or not the extra-judicial foreclosure proceedings should be nullified for being based on an allegedly erroneous computation of the loan's interest.

Respondent spouses, in their Comment, contend that the issues raised in the petition are questions of fact that cannot be entertained by this Court; that parole evidence can be introduced, as was properly appreciated by the RTC and CA, to ascertain the true intention of the parties on how the interest on the loan will accrue; and that petitioners' cause of action is barred by prescription, counting four (4) years from the original due date of the loan, which was December 17, 1984.

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[12] Id. at 42.

The Court's Ruling

The petition is meritorious.

The compounding of interest should be in writing

For academic purposes, We first determine whether or not the stipulation compounding the interest charged should specifically be indicated in a written agreement.

We rule in the affirmative.

Article 1956 of the New Civil Code, which refers to monetary interest, provides:

> **Article 1956.** No interest shall be due unless it has been expressly stipulated in writing.

As mandated by the foregoing provision, payment of monetary interest shall be due only if: (1) there was an express stipulation for the payment of interest; and (2) the agreement for such payment was reduced in writing. Thus, We have held that collection of interest without any stipulation thereof in writing is prohibited by law.[13]

In the case at bar, it is undisputed that the parties have agreed for the loan to earn 5% monthly interest, the stipulation to that effect put in writing. When the petitioners defaulted, the period for payment was extended, carrying over the terms of the original loan agreement, including the 5% simple interest. However, by the third extension of the loan, respondent spouses decided to alter the agreement by changing the manner of earning interest rate, compounding it beginning June 1986. This is apparent from the Statement of Account prepared by the spouses Embisan themselves.

Given the circumstances, We rule that the first requirement—that there be an express stipulation for the payment of interest—is not sufficiently complied with, for purposes of imposing compounded interest on the loan. The requirement does not only entail reducing in writing the interest rate to be earned but also the manner of earning the same, if it is to be compounded. Failure to specify the manner of earning interest, however, shall not automatically render the stipulation imposing the interest rate void since it is readily apparent from the contract itself that the parties herein agreed for the loan to bear interest. Instead, in default of any stipulation on the manner of earning interest, simple interest shall accrue.

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[13] *Siga-an v. Villanueva*, G.R. No. 173227, January 20, 2009, 576 SCRA 696, 705.

Settled is the rule that ambiguities in a contract are interpreted against the party that caused the ambiguity. Any ambiguity in a contract whose terms are susceptible of different interpretations must be read against the party who drafted it.[14] In the extant case, respondent spouses, having imposed, unilaterally at that, the compounded interest rate, had the correlative duty of clarifying and reducing in writing how the said interest shall be earned. Having failed to do so, the silence of the agreement on the manner of earning interest is a valid argument for prohibiting them from charging interest at a compounded rate.

Further, by analogy, We have had the occasion to hold that, when a final money judgment ordered the payment of "legal interest" without mention of payment of compound interest, a judge who orders payment of compound interest does so in excess of his authority.[15]As held in *Philippine American Accident Insurance v. Flores*:[16]

> The judgment which was sought to be executed ordered the payment of simple "legal interest" only. It said nothing about the payment of compound interest. Accordingly, when the respondent judge ordered the payment of compound interest he went beyond the confines of his own judgment which had been affirmed by the Court of Appeals and which had become final. x x x

Therefore, in default of any unequivocal wording in the contract, the legal interest stipulated by the parties should be understood to be simple, not compounded.

Imposing 5% monthly interest, whether compounded or simple, is unconscionable

Nevertheless, even if there was such an agreement that interest will be compounded, We agree with the petitioners that the 5% monthly rate, be it simple or compounded, written or verbal, is void for being too exorbitant, thus running afoul of Article 1306 of the New Civil Code, which provides:

> **Article 1306.** 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. (emphasis added)

As case law instructs, the imposition of an unconscionable rate of interest on a money debt, even if knowingly and voluntarily assumed, is immoral and unjust. It is tantamount to a repugnant spoliation and an iniquitous deprivation of property, repulsive to the common sense of man. It has no support in law, in principles of justice, or in the human conscience nor

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[14] *Fortune Medicare, Inc. v. Amorin*, G.R. No. 195872, March 12, 2014.

[15] *David v. Court of Appeals,* G.R. No. 115821, October 13, 1999, 316 SCRA 710, 717.

[16] *Philippine American Accident Insurance v. Flores*, No. L-47180, May 19, 1980, 97 SCRA 811, 813-814.

is there any reason whatsoever which may justify such imposition as righteous and as one that may be sustained within the sphere of public or private morals.[17]

Summarizing the jurisprudential trend towards this direction is the recent case of *Castro v. Tan*[18] in which We held:

> While we agree with petitioners that parties to a loan agreement have wide latitude to stipulate on any interest rate in view of the Central Bank Circular No. 905 s. 1982 which suspended the Usury Law ceiling on interest effective January 1, 1983, it is also worth stressing that interest rates whenever unconscionable may still be declared illegal. There is certainly nothing in said circular which grants lenders carte blanche authority to raise interest rates to levels which will either enslave their borrowers or lead to a hemorrhaging of their assets.
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> In several cases, we have ruled that stipulations authorizing iniquitous or unconscionable interests are contrary to morals, if not against the law. In Medel v. Court of Appeals,[19] we annulled a stipulated 5.5% per month or 66% per annum interest on a ₱500,000.00 loan and a 6% per month or 72% per annum interest on a ₱60,000.00 loan, respectively, for being excessive, iniquitous, unconscionable and exorbitant. In Ruiz v. Court of Appeals,[20] we declared a 3% monthly interest imposed on four separate loans to be excessive. In both cases, the interest rates were reduced to 12% per annum.
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> **In this case, the 5% monthly interest rate, or 60% per annum, compounded monthly, stipulated in the Kasulatan is even higher than the 3% monthly interest rate imposed in the Ruiz case. Thus, we similarly hold the 5% monthly interest to be excessive, iniquitous, unconscionable and exorbitant, contrary to morals, and the law. It is therefore void ab initio for being violative of Article 1306 of the Civil Code. With this, and in accord with the Medel and Ruiz cases, we hold that the Court of Appeals correctly imposed the legal interest of 12% per annum in place of the excessive interest stipulated in the Kasulatan.** (emphasis added)

As can be gleaned, jurisprudence on the nullity of excessive interest rates is both clear and consistent. We find no cogent reason to deviate therefrom. As the lender in *Castro*, respondent spouses herein similarly imposed a 5% monthly interest in the loan contracted by petitioners. Following the judicial pronouncement in the said cases, the interest rate so imposed herein is nullified for being unconscionable. In lieu thereof, a simple interest of 12% per annum should be imposed.

The foreclosure sale should be nullified

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[17] *Castro v. Tan*, G.R. No. 168940, November 24, 2009, 605 SCRA 231, 232.
[18] Id. at 237-238.
[19] G.R. No. 146942, April 22, 2003, 401 SCRA 411.
[20] G.R. No. 131622, November 17, 1998, 299 SCRA 481.

In view of the above disquisitions, We are constrained to nullify the foreclosure proceedings with respect to the mortgaged property in this case, following the doctrine in *Heirs of Zoilo and Primitiva Espiritu v. Landrito*.[21]

In *Heirs of Espiritu*, the spouses Maximo and Paz Landrito, sometime in 1986, borrowed from the spouses Zoilo and Primitiva Espiritu the amount of □350,000.00, secured by a real estate mortgage. Because of the Landritos' continued inability to pay the loan, the due date for payment was extended on the condition that the interest that has already accrued shall, from then on, form part of the principal. As such, after the third extension, the principal amounted to □874,125.00 in only two years. Despite the extensions, however, the debt remained unpaid, prompting the spouses Espiritu to foreclose the mortgaged property.

The foreclosure proceeding in *Heirs of Espiritu*, however, was eventually nullified by this Court because the Landritos were deprived of the opportunity to settle the debt, in view of the overstated amount demanded from them. As held:

> Since the Spouses Landrito, the debtors in this case, were not given an opportunity to settle their debt, at the correct amount and without the iniquitous interest imposed, no foreclosure proceedings may be instituted. A judgment ordering a foreclosure sale is conditioned upon a finding on the correct amount of the unpaid obligation and the failure of the debtor to pay the said amount. In this case, it has not yet been shown that the Spouses Landrito had already failed to pay the correct amount of the debt and, therefore, a foreclosure sale cannot be conducted in order to answer for the unpaid debt. x x x
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> As a result, the subsequent registration of the foreclosure sale cannot transfer any rights over the mortgaged property to the Spouses Espiritu. The registration of the foreclosure sale, herein declared invalid, cannot vest title over the mortgaged property. x x x

Applying *Espiritu*, the extra-judicial foreclosure of the mortgaged property dated October 12, 1987 is declared null, void, and of no legal effect.

WHEREFORE, in view of the foregoing, the petition is **GRANTED**. The Decision and Resolution of the Court of Appeals, dated May 29, 2013 and January 13, 2014, respectively, in CA-G.R. CV No. 93667 are hereby **REVERSED** and **SET ASIDE**. Let a new Decision be entered, the dispositive portion of which reads:

1. The stipulation in the Loan with Real Estate Mortgage imposing an interest of 5% monthly is declared void.
2. In view of the nullity of the interest imposed on the loan which affected the total arrearages upon which foreclosure was based, the foreclosure of mortgage, Certificate of Sale, Affidavit of

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[21] G.R. No. 169617, April 3, 2007, 520 SCRA 383, 396-397.

Consolidation, Deed of Final Sale, and Contract of Lease are declared void.

3. The case is remanded to the Regional Trial Court to compute the current arrearages of petitioners taking into account the partial payments made by them and the imposition of the simple interest rate of 12% per annum.

SO ORDERED.

PRESBITERO J. VELASCO, JR.
Associate Justice

WE CONCUR:

DIOSDADO M. PERALTA
Associate Justice

MARTIN S. VILLARAMA, JR.
Associate Justice

BIENVENIDO L. REYES
Associate Justice

FRANCIS H. JARDELEZA
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

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