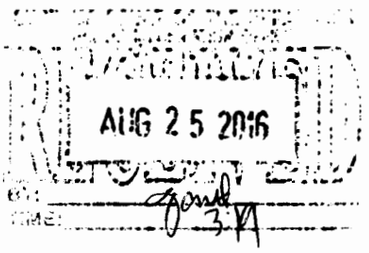
Republic of the Philippines
Supreme Court
Manila

FIRST DIVISION



TERESITA I. BUENAVENTURA,
Petitioner,

- versus -

METROPOLITAN BANK AND TRUST COMPANY,
Respondent.

G.R. No. 167082

Present:

SERENO, *C.J.*,
LEONARDO-DE CASTRO,
BERSAMIN,
PERLAS-BERNABE, and
CAGUIOA, *JJ.*

Promulgated:

AUG 03 2016

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DECISION

BERSAMIN, *J.*:

A duly executed contract is the law between the parties, and, as such, commands them to comply fully and not selectively with its terms. A contract of adhesion, of itself, does not exempt the parties from compliance with what was mutually agreed upon by them.

The Case

In this appeal, the petitioner seeks the reversal of the decision promulgated on April 23, 2004,[1] whereby the Court of Appeals (CA) affirmed with modification the judgment[2] rendered on July 11, 2002 by the Regional Trial Court (RTC), Branch 61, in Makati City. Also being appealed is the resolution[3] promulgated on February 9, 2005, whereby the CA denied her motion for reconsideration.

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1 *Rollo*, pp. 174-182; penned by Associate Justice Edgardo P. Cruz (retired), with the concurrence of Associate Justice Delilah Vidallon-Magtolis (retired) and Associate Justice Noel G. Tijam.
2 CA *rollo*, pp. 62-69; penned by Judge Marissa Macaraig-Guillen
3 *Rollo*, p. 193.

Antecedents

The following factual and procedural antecedents are narrated by the CA in its assailed decision, to wit:

> On January 20, 1997 and April 17, 1997, Teresita Buenaventura (or "appellant") executed Promissory Note (or "PN") Nos. 232663 and 232711, respectively, each in the amount of ₱1,500,000.00 and payable to Metropolitan Bank and Trust Company (or "appellee"). PN No. 232663 was to mature on July 1, 1997, with interest and credit evaluation and supervision fee (or "CESF") at the rate of 17.532% per annum, while PN No. 232711 was to mature on April 7, 1998, with interest and CESF at the rate of 14.239% per annum. Both PNs provide for penalty of 18% per annum on the unpaid principal from date of default until full payment of the obligation.
>
> Despite demands, there remained unpaid on PN Nos. 232663 and 232711 the amounts of ₱2,061,208.08 and ₱1,492,236.37, respectively, as of July 15, 1998, inclusive of interest and penalty. Consequently, appellee filed an action against appellant for recovery of said amounts, interest, penalty and attorney's fees before the Regional Trial Court of Makati City (Branch 61).
>
> In answer, appellant averred that in 1997, she received from her nephew, Rene Imperial (Or "Imperial"), three postdated checks drawn against appellee (Tabaco Branch), i.e., Check No. TA 1270484889PA dated January 5, 1998 in the amount of ₱1,200,000.00, Check No. 1270482455PA dated March 31, 1998 in the amount of ₱1,197,000.00 and Check No. TA1270482451PA dated March 31, 1998 in the amount of ₱500,000.00 (or "subject checks"), as partial payments for the purchase of her properties; that she rediscounted the subject checks with appellee (Timog Branch), for which she was required to execute the PNs to secure payment thereof; and that she is a mere guarantor and cannot be compelled to pay unless and until appellee shall have exhausted all the properties of Imperial.[4]

On July 11, 2002, the RTC rendered its judgment,[5] *viz.*:

> WHEREFORE, in view of the foregoing, the Court finds in favor of plaintiff METROPOLITAN BANK AND TRUST COMPANY and against defendant TERESITA BUENAVENTURA.
>
> As a consequence of this judgment, defendant Buenaventura is directed to pay plaintiff bank the amount of ₱3,553,444.45 plus all interest and penalties due as stipulated in Promissory Notes Nos. 232663 and 232711 beginning July 15, 1998 until the amount is fully paid and 10% of the total amount due as attorney's fees.
>
> SO ORDERED.

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4 *Rollo*, pp. 174-175.

5 CA *rollo*, p. 69.

Dissatisfied, the petitioner appealed, assigning the following as errors, namely:

> I
>
> THE TRIAL COURT ERRED IN HOLDING THAT THE REDISCOUNTING TRANSACTION BETWEEN APPELLANT AND METROBANK RESULTED TO A LOAN OBLIGATION SECURED BY THE SUBJECT CHECKS AND PROMISSORY NOTES.
>
> A. Rediscounting transactions do not create loan obligations between the parties.
>
> B. By the rediscounting, Metrobank subrogated appellant as creditor of Rene Imperial, the issuer of the checks.
>
> C. Legal subrogation was presumed when Metrobank paid the obligation of Mr. Imperial with the latter's knowledge and consent.
>
> II
>
> THE TRIAL COURT ERRED IN GRANTING METROBANK'S CLAIMS ON THE BASIS OF THE PROMISSORY NOTES.
>
> A. The promissory notes are null and void for being simulated and fictitious.
>
> B. Assuming that the promissory notes are valid, these only serve as guaranty to secure the payment of the rediscounted checks.
>
> III
>
> THE TRIAL COURT ERRED IN NOT RULING THAT APPELLANT IS ENTITLED TO HER COUNTERCLAIMS FOR EXEMPLARY DAMAGES, ATTTORNEY'S FEES, LITIGATION EXPENSES AND COSTS OF SUIT.[6]

On April 23, 2004, the CA promulgated the assailed decision affirming the decision of the RTC with modification,[7] as follows:

> **WHEREFORE,** the appealed decision is **AFFIRMED** with **MODIFICATION** of the second paragraph of its dispositive portion, which should now read:
>
> "As a consequence of this judgment, defendant Buenaventura is directed to pay plaintiff bank the amount of ₱3,553,444.45 plus interest and penalty therein at 14.239% per annum and 18% per annum, respectively, from July 15, 1998 until fully paid and 10% of said amount as attorney's fees."
>
> **SO ORDERED.**[8]

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6 Id. at 23-24.
7 Supra note 1.
8 Id. at 181.

On May 21, 2004, the petitioner moved for the reconsideration of the decision, but the CA denied her motion for that purpose on February 9, 2005.[9]

Hence, this appeal by the petitioner.

Issues

The petitioner ascribes the following errors to the CA, to wit:

> I
> THE COURT OF APPEALS ERRED IN HOLDING THAT PETITIONER IS LIABLE UNDER THE PROMISSORY NOTES.
>
> A. The promissory notes executed by petitioner are null and void for being simulated and fictitious.
>
> B. Even assuming that the promissory notes are valid, these are intended as mere guaranty to secure Rene Imperial's payment of the rediscounted checks. Hence, being a mere guarantor, the action against petitioner under the said promissory notes is premature.
>
> C. Metrobank is deemed to have subrogated petitioner as creditor of Mr. Imperial (the issuer of the checks). Hence, Metrobank's recourse as creditor, is against Mr. Imperial.
>
> II
> THE COURT OF APPEALS ERRED IN NOT RULING THAT PETITIONER IS ENTITLED TO HER COUNTER-CLAIM FOR EXEMPLARY DAMAGES, ATTORNEY'S FEES, LITIGATION EXPENSES AND COSTS OF SUIT.[10]

Ruling

The appeal lacks merit.

First of all, the petitioner claims that the promissory notes she executed were contracts of adhesion because her only participation in their execution was affixing her signature;[11] and that the terms of the promissory notes should consequently be strictly construed against the respondent as the party responsible for their preparation.[12] In contrast, the respondent counters that the terms and conditions of the promissory notes were clear and unambiguous; hence, there was no room or need for interpretation thereof.[13]

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9 CA *rollo*, p. 194.
10 *Rollo*, pp. 13-14.
11 Id. at 16.
12 Id. at 17.
13 Id. at 211-212.

The respondent is correct.

The promissory notes were written as follows:

> FOR VALUE RECEIVED, I/we jointly and severally promise to pay Metropolitan Bank and Trust Company, at its office x x x the principal sum of PESOS x x x, Philippine currency, together with interest and credit evaluation and supervision fee (CESF) thereon at the effective rate of x x x per centum x x x per annum, inclusive, from date hereof and until fully paid.[14]

What the petitioner advocates is for the Court to now read into the promissory notes terms and conditions that would contradict their clear and unambiguous terms in the guise of such promissory notes being contracts of adhesion. This cannot be permitted, for, even assuming that the promissory notes were contracts of adhesion, such circumstance alone did not necessarily entitle her to bar their literal enforcement against her if their terms were unequivocal. It is preposterous on her part to disparage the promissory notes for being contracts of adhesion, for she thereby seems to forget that the validity and enforceability of contracts of adhesion were the same as those of other valid contracts. The Court has made this plain in *Avon Cosmetics, Inc. v. Luna*,[15] stating:

> A contract of adhesion is so-called because its terms are prepared by only one party while the other party merely affixes his signature signifying his adhesion thereto. Such contract is just as binding as ordinary contracts.
>
> It is true that we have, on occasion, struck down such contracts as void when the weaker party is imposed upon in dealing with the dominant bargaining party and is reduced to the alternative of taking it or leaving it, completely deprived of the opportunity to bargain on equal footing. Nevertheless, contracts of adhesion are not invalid *per se* and they are not entirely prohibited. The one who adheres to the contract is in reality free to reject it entirely, if he adheres, he gives his consent.
>
> x x x x
>
> Accordingly, a contract duly executed is the law between the parties, and they are obliged to comply fully and not selectively with its terms. A contract of adhesion is no exception.

As a rule, indeed, the contract of adhesion is no different from any other contract. Its interpretation still aligns with the literal meaning of its terms and conditions absent any ambiguity, or with the intention of the

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[14] Id. at 37.

[15] G.R. No. 153674, December 20, 2006, 511 SCRA 376, 396-397.

parties.[16] The terms and conditions of the promissory notes involved herein, being clear and beyond doubt, should then be enforced accordingly. In this regard, we approve of the observation by the CA, citing *Cruz v. Court of Appeals*,[17] that the intention of the parties should be "deciphered not from the unilateral *post facto* assertions of one of the parties, but from the language used in the contract."[18] As fittingly declared in *The Insular Life Assurance Company, Ltd. vs. Court of Appeals and Sun Brothers & Company*,[19] "[w]hen the language of the contract is explicit leaving no doubt as to the intention of the drafters thereof, the courts may not read into it any other intention that would contradict its plain import." Accordingly, no court, even this Court, can "make new contracts for the parties or ignore those already made by them, simply to avoid seeming hardships. Neither abstract justice nor the rule of liberal construction justifies the creation of a contract for the parties which they did not make themselves or the imposition upon one party to a contract of an obligation not assumed."[20]

Secondly, the petitioner submits that the promissory notes were null and void for being simulated and fictitious; hence, the CA erred in enforcing them against her.

The submission contradicts the records and the law pertinent to simulated contracts.

Based on Article 1345[21] of the *Civil Code*, simulation of contracts is of two kinds, namely: (1) absolute; and (2) relative. Simulation is absolute when there is color of contract but without any substance, the parties not intending to be bound thereby.[22] It is relative when the parties come to an agreement that they hide or conceal in the guise of another contract.[23]

The effects of simulated contracts are dealt with in Article 1346 of the *Civil Code*, to wit:

> 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

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16 The *Civil Code* says:

Art. 1370. If the terms of a contract are clear and leave no doubt upon the intention of the contracting parties, the literal meaning of its stipulation shall control.

If the words appear to be contrary to the evident intention of the parties, the latter shall prevail over the former.

17 G.R. No. 126713, July 27, 1998, 293 SCRA 239, 252.

18 *Rollo*, p. 177.

19 G.R. No. 126850, April 28, 2004, 428 SCRA 79, 92.

20 Id.

21 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.

22 IV Tolentino, *Civil Code of the Philippines,* 1991, p. 516.

23 Id.

order or public policy binds the parties to their real agreement.

The burden of showing that a contract is simulated rests on the party impugning the contract. This is because of the presumed validity of the contract that has been duly executed.[24] The proof required to overcome the presumption of validity must be convincing and preponderant. Without such proof, therefore, the petitioner's allegation that she had been made to believe that the promissory notes would be guaranties for the rediscounted checks, not evidence of her primary and direct liability under loan agreements,[25] could not stand.

Moreover, the issue of simulation of contract was not brought up in the RTC. It was raised for the first time only in the CA.[26] Such belatedness forbids the consideration of simulation of contracts as an issue. Indeed, the appellate courts, including this Court, should adhere to the rule that issues not raised below should not be raised for the first time on appeal. Basic considerations of due process and fairness impel this adherence, for it would be violative of the right to be heard as well as unfair to the parties and to the administration of justice if the points of law, theories, issues and arguments not brought to the attention of the lower courts should be considered and passed upon by the reviewing courts for the first time.

Thirdly, the petitioner insists that the promissory notes, even if valid, were meant as guaranties to secure payment of the checks by the issuer, Rene Imperial; hence, her liability was that of a guarantor, and would take effect only upon exhaustion of all properties and after resort to all legal remedies against Imperial.[27]

The insistence of the petitioner is bereft of merit.

The CA rejected this insistence, expounding as follows:

> A guaranty is not presumed; it must be expressed (Art. 2055, New Civil Code). The PNs provide, in clear language, that appellant is primarily liable thereunder. On the other hand, said PNs do not state that Imperial, who is not even privy thereto, is the one primarily liable and that appellant is merely a guarantor. Parenthetically, the disclosure statement (Exh. "D") executed by appellant states that PN No. 232711 is "secured by postdated checks". In other words, it does not appear that the PNs were executed as guaranty for the payment of the subject checks.
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> Nevertheless, appellant insists that she did not obtain a short-term loan from appellee but rediscounted the subject checks, with the PNs as guaranty. The contention is untenable.

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24 *Ramos v. Heirs of Honorio Ramos, Sr.*, G.R. No. 140848, April 25, 2002, 381 SCRA 594, 602.
25 *Rollo*, p. 18.
26 CA *rollo*, pp. 44-55.
27 *Rollo*, pp. 22-24.

In *Great Asian Sales Center Corporation vs. Court of Appeals* (381 SCRA 557), which was cited in support of appellant's claim, the Supreme Court explained the meaning of "discounting line", thus:

> "In the financing industry, the term 'discounting line' means a credit facility with a financing company or bank which allows a business entity to sell, on a continuing basis, its accounts receivable at a discount. The term 'discount' means the sale of a receivable at less than its face value. The purpose of a discounting line is to enable a business entity to generate instant cash out of its receivables which are still to mature at future dates. The financing company or bank which buys the receivables makes its profit out of the difference between the face value of the receivable and the discounted price."

A guarantor may bind himself for less, but not for more than the principal debtor, both as regards the amount and the onerous nature of the conditions (Art. 2054, *id.*). Curiously, the face amounts of the PNs (totaling ₱3,000,000.00) are more than those of the subject checks (totaling ₱2,897,000.00). And unlike the subject checks, the PNs provide for interest, CESF and penalty.

Moreover, the maturity date (July 1, 1997) of PN No. 232663 is ahead of the dates (January 5, 1998 and March 31, 1998) of the subject checks. In other words, appellant, as "guarantor", was supposed to make good her "guaranty", i.e. PNs in question, even *before* the "principal" obligations, i.e. subject checks, became due. It is also noted that the rediscounting of the subject checks (in January 1997) occurred months *ahead* of the execution of PN No. 232711 (on April 17, 1997) even as the PNs were supposedly a precondition to said rediscounting.

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Stated differently, appellant is primarily liable under the subject checks. She is a principal debtor and not a guarantor. Consequently, the benefit of excussion may not be interposed as a defense in an action to enforce appellant's warranty as indorser of the subject checks.

Moreover, it is absurd that appellant (as maker of the PNs) may act as guarantor of her own obligations (as indorser of the subject checks). Thus, Art. 2047 of the New Civil Code provides that "(b)y guaranty, a person called the **guarantor**, binds himself to the creditor to fulfill the obligation of the **principal debtor** in case the latter should fail to do so."[28] (Emphasis supplied)

The CA was correct. A contract of guaranty is one where a person, the guarantor, binds himself or herself to another, the creditor, to fulfill the

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[28] *Rollo*, pp. 177-180.

obligation of the principal debtor in case of failure of the latter to do so.[29] It cannot be presumed, but must be express and in writing to be enforceable,[30] especially as it is considered a special promise to answer for the debt, default or miscarriage of another.[31] It being clear that the promissory notes were entirely silent about the supposed guaranty in favor of Imperial, we must read the promissory notes literally due to the absence of any ambiguities about their language and meaning. In other words, the petitioner could not validly insist on the guaranty. In addition, the disclosure statements[32] and the statements of loan release[33] undeniably identified her, and no other, as the borrower in the transactions. Under such established circumstances, she was directly and personally liable for the obligations under the promissory notes.

Fourth, the petitioner argues that the respondent was immediately subrogated as the creditor of the accounts by its purchase of the checks from her through its rediscounting facility;[34] and that legal subrogation should be presumed because the petitioner, a third person not interested in the obligation, paid the debt with the express or tacit approval of the debtor.[35]

The argument is barren of factual and legal support.

Legal subrogration finds no application because there is no evidence showing that Imperial, the issuer of the checks, had consented to the subrogation, expressly or impliedly.[36] This circumstance was pointed out by the RTC itself.[37] Also, as the CA emphatically observed,[38] the argument was off-tangent because the suit was not for the recovery of money by virtue of the checks of Imperial but for the enforcement of her obligation as the maker of the promissory notes.

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[29] Art. 2047, *Civil Code*, provides:

Art. 2047. By guaranty a person, called the guarantor, binds himself to the creditor to fulfill the obligation of the principal debtor in case the latter should fail to do so.

If a person binds himself solidarily with the principal debtor, the provisions of Section 4, Chapter 3, Title I of this Book shall be observed. In such case the contract is called a suretyship. (1822a)

[30] Art. 2055, *Civil Code*, declares that: "A guaranty is not presumed; it must be express and cannot extend to more than what is stipulated therein."

[31] Art. 1403, *Civil Code*, requires that **a special promise to answer for the debt, default or miscarriage of another**, among others, must be in writing to be enforceable unless ratified; see also *Aglibot v. Santia*, G.R. No. 185945, December 5, 2012, 687 SCRA 283, 294-295.

[32] *Rollo*, pp. 38, 40.

[33] *Records*, pp. 126-127.

[34] *Rollo*, p. 26.

[35] Id. at 27.

[36] According to Art. 1302, *Civil Code*, there is legal subrogation when: (1) a creditor pays another creditor who is preferred, even without the debtor's knowledge; (2) **a third person, not interested in the obligation, pays with the express or tacit approval of the debtor**; or (3) even without the knowledge of the debtor, a person interested in the fulfillment of the obligation pays, without prejudice to the effects of confusion as to the latter's share.

[37] *Rollo*, p. 65.

[38] Id. at 180.

Fifth, the petitioner posits that she was made to believe by the manager of the respondent's Timog Avenue, Quezon City Branch that the promissory notes would be mere guaranties for the rediscounted checks;[39] that despite the finding of the RTC and the CA that she was a seasoned businesswoman presumed to have read and understood all the documents given to her for signature, she remained a layman faced with and puzzled by complex banking terms; and that her acceding to signing the promissory notes should not be taken against her as to conclude her.[40]

The petitioner's position is unworthy of serious consideration.

After having determined that the terms and conditions of the promissory notes were clear and unambiguous, and thus should be given their literal meaning and not be interpreted differently, we insist and hold that she should be bound by such terms and conditions. Verily, the promissory notes as contracts should bind both contracting parties; hence, the validity or compliance therewith should not be left to the will of the petitioner.[41] Otherwise, she would contravene and violate the principles of mutuality and of the obligatory force of contracts. A respected commentator on civil law has written in this respect:

> The binding effect of the contract on both parties is based on the principles (1) that obligations arising from contracts have the force of law between the contracting parties; and (2) that there must be mutuality between the parties based on their essential equality, to which is repugnant to have one party bound by the contract leaving the other free therefrom.
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> x x x x
>
> Just as nobody can be forced to enter into a contract, in the same manner once a contract is entered into, no party can renounce it unilaterally or without the consent of the other. It is a general principle of law that no one may be permitted to change his mind or disavow and go back upon his own acts, or to proceed contrary thereto, to the prejudice of the other party.
>
> If, after a perfect and binding contract has been executed between the parties, it occurs to one of them to allege some defect therein as a reason for annulling it, the alleged defect must be conclusively proven, since the validity and fulfillment of contracts cannot be left to the will of one of the contracting parties. The fact that a party may not have fully understood the legal effect of the contract is no ground for setting it aside.[42]

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39 Id. at 18.
40 Id. at 20.
41 Art. 1308, *Civil Code*.
42 IV Tolentino, *op. cit.*, at 424-425.

And, lastly, there is need to revise the monetary awards by the CA. Although no issue is raised by the petitioner concerning the monetary awards, the Court feels bound to make this revision as a matter of law in order to arrive at a just resolution of the controversy.

Involved here are two loans of the petitioner from the respondent, specifically: (1) the principal amount of ₱1,500,000.00 covered by Promissory Note No. 232663 to be paid on or before July 1, 1997 with interest and credit evaluation and supervision fee (CESF) at the rate of 17.532% *per annum* and penalty charge of 18% *per annum* based on the unpaid principal to be computed from the date of default until full payment of the obligation; and (2) the principal amount of ₱1,500,000.00 covered by Promissory Note No. 232711 to be paid on or before April 7, 1998 with interest and CESF at the rate of 14.239% *per annum* and penalty charge of 18% *per annum* based on the unpaid principal to be computed from the date of default until full payment of the obligation.

The RTC adjudged the petitioner liable to pay to the respondent the total of ₱3,553,444.45 representing her outstanding obligation, including accrued interests and penalty charges under the promissory notes, plus attorney's fees.[43] On appeal, the CA ruled that she was liable to the respondent for the sum of ₱3,553,444.45 with interest and penalties at 14.239% *per annum* and 18% *per annum*, respectively, from July 15, 1998 until fully paid.[44]

The bases of the amounts being claimed from the petitioner were apparently the two *statements of past due interest and penalty charges as of July 15, 1998*, one corresponding to Promissory Note No. 232711,[45] and the other to Promissory Note No. 232663.[46] Respondent's witness Patrick N. Miranda, testifying on the obligation and the computation thereof,[47] attested as follows:

> *1. What is the amount of her loan obligation?*
>
> -Under Promissory Note No. 232663, her loan obligation is ₱1,492,236.37 inclusive of interest and penalty charges as of July 15, 1998. Under Promissory Note No. 232711, her loan obligation is ₱2,061,208.08, inclusive of interest and penalty charges as of July 15, 1998. Thus, the total is ₱3,553,444.45 as of July 15, 1998. Two (2) Statements of Account were prepared to show the computation and penalty charges.
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> *2. Do you have these Statements of Account?*

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43 *Rollo*, p. 67.
44 Id. at 181.
45 *Record*, p. 104.
46 Id. at 105.
47 Id. at 95.

-Yes, sir. (Copies are hereto attached as *Exhibits "H"* and *"I."*)[48]

The two *statements of past due interest and penalty charges as of July 15, 1998* explained how the respondent had arrived at the petitioner's outstanding liabilities as of July 15, 1998, thusly:

Promissory Note No. 232711[49]

PRINCIPAL AMOUNT	₱ 1,500,000.00
PAST DUE INTEREST – 334 days @34.991% fr. Aug. 15, 1997 to July 15, 1998	₱ 486,958.08
PENALTY CHARGES – 99 days @18.0% fr. April 07, 1998 to July 15, 1998	₱ 74,250.00
TOTAL OUTSTANDING LOAN AS OF JULY 15, 1998	**₱ 2,061,208.08**

Promissory Note No. 232663[50]

PRINCIPAL AMOUNT	₱ 1,200,000.00
PAST DUE INTEREST – 191 days @27.901% fr. [J]an. 05, 1998 to [J]uly 15, 1998	₱ 177,636.37
PENALTY CHARGES – 191 days @18.0% fr. [J]an. 05, 1998 to [J]uly 15, 1998	₱ 114,600.00
TOTAL OUTSTANDING LOAN AS OF JULY 15, 1998	**₱ 1,492,236.37**

The total of ₱3,553,444.45 was the final sum of the computations contained in the *statements of past due interest and penalty charges as of July 15, 1998*, and was inclusive of interest at the rate of 34.991% (on the principal of ₱1,500,000.00) and 27.901% (on the principal of ₱1,200,000.00). Yet, such interest rates were different from the interest rates stipulated in the promissory notes, namely: 14.239% for Promissory Note No. 232711 and 17.532% for Promissory Note No. 232663. As a result, the ₱3,553,444.45 claimed by the respondent as the petitioner's aggregate outstanding loan obligation included interests of almost double the rates stipulated by the parties.

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48 Id. at 96.
49 Supra note 44.
50 Id. at 105.

We hold that the respondent had no legal basis for imposing rates far higher than those agreed upon and stipulated in the promissory notes. It did not suitably justify the imposition of the increased rates of 34.991% and 27.901%, as borne out by the *statements of past due interest and penalty charges as of July 15, 1998*, although it certainly was its burden to show the legal and factual support for the imposition. We need not remind that the burden of proof is the duty of any party to present evidence to establish its claim or defense by the amount of evidence required by law, which in civil cases is preponderance of evidence.[51] Consequently, we have to strike down the imposition.

Parenthetically, we observe that the stipulation in the promissory notes on the automatic increase of the interest rate to the prevailing rate[52] did not justify the increase of the interest rates because the respondent did not adduce evidence about the prevailing rates at the time material to this case.

On May 16, 2013, the Monetary Board of the Bangko Sentral ng Pilipinas, in the exercise of its statutory authority to review and fix interest rates, issued Circular No. 799, Series of 2013 to lower to 6% *per annum* the rate of interest for loan or forbearance of any money, goods or credits, and the rate allowed in judgment.[53] The revised rate applies only in the absence of stipulation in loan contracts. Hence, the contractual stipulations on the rates of interest contained in the promissory notes remained applicable.

Considering that, as mentioned, the ₱3,553,444.45 was an aggregate inclusive of the interest (*i.e.*, at the rates of 34.991% and 27.901% *per annum*); and that the penalty charges contravened the express provisions of the promissory notes, the RTC and the CA both erred on a matter of law, and we should correct their error as a matter of law in the interest of justice.

It is further held that the CA could not validly apply the lower interest rate of 14.239% *per annum* to the whole amount of ₱3,553,444.45 in contravention of the stipulation of the parties. In *Mallari v. Prudential Bank*,[54] the Court declared that the interest rate of "3% per month and higher are excessive, unconscionable and exorbitant, hence, the stipulation was void for being contrary to morals." Even so, the Court did not consider as

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[51] *United Merchants Corporation v. Country Bankers Insurance Corporation*, G.R. No. 198588, July 11, 2012, 676 SCRA 382, 395.

[52] Paragraph 5 of the Promissory Note, last sentence, reads:

> In case of default, I/we agree that as additional compensation, the interest rate shall automatically be raised to the prevailing rate, the increased rate to be applied from the date of default. (Records, pp. 5, 7).

[53] Section 1. The rate of interest for the loan or forbearance of any money, goods or credits and the rate allowed in judgments, in the absence of an express contract as to such rate of interest, shall be six percent (6%) *per annum*.

[54] G.R. No. 197861, June 5, 2013, 697 SCRA 555, 564.

unconscionable the interest rate of 23% *per annum* agreed upon by the parties. Upholding the 23% *per annum* interest rate agreed upon, the Court instead opined 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."[55] Consequently, the respondent could not impose the flat interest rate of 14.239% *per annum* on the petitioner's loan obligation. Verily, the obligatory force of the stipulations between the parties called for the imposition of the interest rates stipulated in the promissory notes.

To accord with the prevailing jurisprudence, the Court pronounces that the respondent was entitled to recover the principal amount of ₱1,500,000.00 subject to the stipulated interest of 14.239% *per annum* from date of default until full payment;[56] and the principal amount of ₱1,200,000.00 subject to the stipulated interest of 17.532% *per annum* from date of default until full payment.[57]

The next matter to be considered and determined is the date of default.

According to Article 1169 of the *Civil Code*, there is delay or default from the time the obligee judicially or extrajudicially demands from the obligor the fulfillment of his or her obligation. The records reveal that the respondent did not establish *when* the petitioner defaulted in her obligation to pay based on the two promissory notes. As such, its claim for payment computed from July 15, 1998 until full payment of the obligation had no moorings other than July 15, 1998 being the date reflected in the *statements of past due interest and penalty charges as of July 15, 1998*. Nonetheless, its counsel, through the letter dated July 7, 1998,[58] made a *final demand* in writing for the petitioner to settle her total obligation within five days from receipt. As the registry return receipt indicated,[59] the final demand letter was received for the petitioner by one Elisa dela Cruz on July 28, 1998. Hence, the petitioner had five days from such receipt, or until August 2, 1998, within which to comply. The reckoning date of default is, therefore, August 3, 1998.

As to the penalty charge, the same was warranted for being expressly stipulated in the promissory notes, to wit:

> I/we further agree to pay the Bank, in addition to the agreed interest rate, a penalty charge of <u>eighteen</u> per centum (<u>18%</u>) per annum based on any unpaid principal to be computed from date of default until

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55 Id., citing *Villanueva v. Court of Appeals*, G.R. No. 163433, August 22, 2011, 655 SCRA 707, 716-717.
56 Records, p. 98.
57 Id. at 99.
58 Id. at 108.
59 Id. at 109.

full payment of the obligation.[60]

Verily, a penal clause is an accessory undertaking attached to a principal obligation. It has for its purposes, *firstly*, to provide for liquidated damages; and, *secondly*, to strengthen the coercive force of the obligation by the threat of greater responsibility in the event of breach of obligation.[61] Under Article 1226 of the *Civil Code*,[62] a penal clause is a substitute indemnity for damages and the payment of interests in case of noncompliance, *unless there is a stipulation to the contrary.* In *Tan v. Court of Appeals,*[63] the Court has elaborated on the nature of a penalty clause in the following:

> Penalty on delinquent loans may take different forms. In *Government Service Insurance System v. Court of Appeals*, this Court has ruled that the New Civil Code permits an agreement upon a penalty apart from the monetary interest. If the parties stipulate this kind of agreement, the penalty does not include the monetary interest, and as such the two are different and distinct from each other and may be demanded separately. Quoting *Equitable Banking Corp. v. Liwanag,* the GSIS case went on to state that such a stipulation about payment of an additional interest rate partakes of the nature of a penalty clause which is sanctioned by law, more particularly under Article 2229 of the New Civil Code which provides that:
>
> > If the obligation consists in the payment of a sum of money, and the debtor incurs in delay, the indemnity for damages, there being no stipulation to the contrary, shall be the payment of the interest agreed upon, and the absence of stipulation, the legal interest, which is six per cent per annum.
>
> The penalty charge of two percent (2%) per month in the case at bar began to accrue from the time of default by the petitioner. There is no doubt that the petitioner is liable for both the stipulated monetary interest and the stipulated penalty charge. The penalty charge is also called penalty or compensatory interest.

The Court has explained the rate of compensatory interest on monetary awards adjudged in decisions of the Court in *Planters Development Bank v. Lopez*,[64] citing *Nacar v. Gallery Frames*,[65] to wit:

> With respect to the computation of compensatory interest, Section 1 of Bangko Sentral ng Pilipinas (BSP) Circular No. 799, Series of 2013, which took effect on July 1, 2013, provides:

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60 *Rollo*, pp. 37 and 39.

61 IV Tolentino, *op. cit.*, at 259.

62 Art. 1226. In obligations with a penal clause, the penalty shall substitute the indemnity for damages and the payment of interests in case of noncompliance, if there is no stipulation to the contrary. Nevertheless, damages shall be paid if the obligor refuses to pay the penalty or is guilty of fraud in the fulfillment of the obligation.

The penalty may be enforced only when it is demandable in accordance with the provisions of this code.

63 G.R. No. 116285, October 19, 2001, 367 SCRA 571, 579-580.

64 G.R. No. 186332, October 23, 2013, 708 SCRA 481, 501-503.

65 G.R. No. 189871, August 13, 2013, 703 SCRA 439, 455-457.

> Section 1. The rate of interest for the loan or forbearance of any money, goods or credits and the rate allowed in judgments, in the absence of an express contract as to such rate of interest, shall be six percent (6%) per annum.

This provision amends Section 2 of Central Bank (CB) Circular No. 905-82, Series of 1982, which took effect on January 1, 1983. Notably, we recently upheld the constitutionality of CB Circular No. 905-82 in *Advocates for Truth in Lending, Inc., et al. v. Bangko Sentral ng Pilipinas Monetary Board, etc.* Section 2 of CB Circular No. 905-82 provides:

> Section 2. The rate of interest for the loan or forbearance of any money, goods or credits and the rate allowed in judgments, in the absence of express contract as to such rate of interest, shall continue to be twelve percent (12%) per annum.

Pursuant to these changes, this Court modified the guidelines in *Eastern Shipping Lines, Inc. v. Court of Appeals* in the case of *Dario Nacar v. Gallery Frames, et al.(Nacar).* In Nacar, we established the following guidelines:

> I. When an obligation, regardless of its source, i.e., law, contracts, quasi-contracts, delicts or quasi-delicts is breached, the contravenor can be held liable for damages. The provisions under Title XVIII on "Damages" of the Civil Code govern in determining the measure of recoverable damages.
>
> II. **With regard particularly to an award of interest in the concept of actual and compensatory damages, the rate of interest, as well as the accrual thereof, is imposed, as follows:**
>
> > **1. When the obligation is breached, and it consists in the payment of a sum of money, i.e., a loan or forbearance of money, the interest due should be that which may have been stipulated in writing. Furthermore, the interest due shall itself earn legal interest from the time it is judicially demanded. In the absence of stipulation, the rate of interest shall be 6% per annum to be computed from default, i.e., from judicial or extrajudicial demand under and subject to the provisions of Article 1169 of the Civil Code.** (emphasis and underscore supplied)
> >
> > 2. When an obligation, not constituting a loan or forbearance of money, is breached, an interest on the amount of damages awarded may be imposed at the discretion of the court at the rate of 6% per annum. No interest, however, shall be adjudged on unliquidated claims or damages, except when or until the demand can be established with reasonable certainty. Accordingly, where the demand is

> established with reasonable certainty, the interest shall begin to run from the time the claim is made judicially or extrajudicially (Art. 1169, Civil Code), but when such certainty cannot be so reasonably established at the time the demand is made, the interest shall begin to run only from the date the judgment of the court is made (at which time the quantification of damages may be deemed to have been reasonably ascertained). The actual base for the computation of legal interest shall, in any case, be on the amount finally adjudged.
>
> 3. When the judgment of the court awarding a sum of money becomes final and executory, the rate of legal interest, whether the case falls under paragraph 1 or paragraph 2, above, shall be 6% per annum from such finality until its satisfaction, this interim period being deemed to be by then an equivalent to a forbearance of credit.
>
> And, in addition to the above, judgments that have become final and executory prior to July 1, 2013, shall not be disturbed and shall continue to be implemented applying the rate of interest fixed therein.

To accord with the foregoing rulings, the 17.532% and 14.239% annual interest rates shall also respectively earn a penalty charge of 18% *per annum* reckoned on the unpaid principals computed from the date of default (August 3, 1998) until fully paid. This is in line with the express agreement between the parties to impose such penalty charge.

Article 2212 of the *Civil Code* requires that interest due shall earn legal interest from the time it is judicially demanded, although the obligation may be silent upon this point. Accordingly, the interest due shall itself earn legal interest of 6% *per annum* from the date of finality of the judgment until its full satisfaction, the interim period being deemed to be an equivalent to a forbearance of credit.[66]

WHEREFORE, the Court **AFFIRMS** the decision promulgated on April 23, 2004 with the **MODIFICATION** that the petitioner shall pay to the respondent: (1) the principal sum of ₱1,500,000.00 under Promissory Note No. 232711, plus interest at the rate of 14.239% *per annum* commencing on August 3, 1998 until fully paid; (2) the principal sum of ₱1,200,000.00 under Promissory Note No. 232663, plus interest at the rate of 17.532% *per annum* commencing on August 3, 1998 until fully paid; (3) penalty interest on the unpaid principal amounts at the rate of 18% *per annum* commencing on August 3, 1998 until fully paid; (4) legal interest of

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[66] *Planters Development Bank v. Lopez*, supra note 64.

6% *per annum* on the interests commencing from the finality of this judgment until fully paid; (5) attorney's fees equivalent to 10% of the total amount due to the respondent; and (6) costs of suit.

SO ORDERED.

LUCAS P. BERSAMIN
Associate Justice

WE CONCUR:

MARIA LOURDES P. A. SERENO
Chief Justice

TERESITA J. LEONARDO-DE CASTRO
Associate Justice

ESTELA M. PERLAS-BERNABE
Associate Justice

ALFREDO BENJAMIN S. CAGUIOA
Associate Justice

CERTIFICATION

Pursuant to Section 13, Article VIII of the Constitution, 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