Republic of the Philippines
Supreme Court
Manila

FIRST DIVISION

SECURITY BANK CORPORATION,
Petitioner,

-versus-

SPOUSES RODRIGO and ERLINDA MERCADO,
Respondents.

G.R. No. 192934

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SPOUSES RODRIGO and ERLINDA MERCADO,
Petitioners,

-versus-

SECURITY BANK and TRUST COMPANY,
Respondent.

G.R. No. 197010

Present:

LEONARDO-DE CASTRO,*
DEL CASTILLO, *Acting Chairperson***
JARDELEZA,
TIJAM, and
GESMUNDO,*** *JJ.*

Promulgated:

JUN 27 2018

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DECISION

JARDELEZA, *J.*:

These are consolidated petitions[1] seeking to nullify the Court of Appeals' (CA) July 19, 2010 Decision[2] and May 2, 2011 Resolution[3] in CA-

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* On official leave.

** Designated as Acting Chairperson of the First Division per Special Order No. 2562 dated June 20, 2018.

*** Designated as Acting Member of the First Division per Special Order No. 2560 dated May 11, 2018.

[1] Petition for review on *certiorari* filed by Security Bank Corporation (formerly known as Security Bank and Trust Company, *rollo* (G.R. No. 192934), pp. 24-46; and petition for review on *certiorari* filed by the spouses Rodrigo and Erlinda Mercado, *rollo* (G.R. No. 197010), pp. 9-22. We resolved to consolidate these petitions in our Resolution dated January 18, 2012, see *rollo* (G.R. No. 192934), p. 183.

[2] *Rollo* (G.R. No. 192934), pp. 9-22; penned by Associate Justice Isaias Dicdican, with Associate Justices Stephen C. Cruz and Danton Q. Bueser concurring.

[3] *Rollo* (G.R. No. 197010), pp. 49-50.

G.R. CV No. 90031. The CA modified the February 26, 2007 Decision,[4] as amended by the June 19, 2007 Amendatory Order[5] (Amended Decision), of Branch 84, Regional Trial Court (RTC), Batangas City in the consolidated cases of Civil Case No. 5808 and LRC Case No. N-1685. The RTC nullified the extrajudicial foreclosure sales over petitioners-spouses Rodrigo and Erlinda Mercado's (spouses Mercado) properties, and the interest rates imposed by petitioner Security Bank Corporation (Security Bank).

On September 13, 1996, Security Bank granted spouses Mercado a revolving credit line in the amount of ₱1,000,000.00.[6] The terms and conditions of the revolving credit line agreement included the following stipulations:

> 7. Interest on Availments – I hereby agree to pay Security Bank interest on outstanding Availments at a per annum rate determined from time to time, by Security Bank and advised through my Statement of Account every month. I hereby agree that the basis for the determination of the interest rate by Security Bank on my outstanding Availments will be Security Bank's prevailing lending rate at the date of availment. I understand that the interest on each availment will be computed daily from date of availment until paid.
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> x x x x
>
> 17. Late Payment Charges – If my account is delinquent, I agree to pay Security Bank the payment penalty of 2% per month computed on the amount due and unpaid or in excess of my Credit Limit.[7]

On the other hand, the addendum to the revolving credit line agreement further provided that:

> I hereby agree to pay Security Bank Corporation (SBC) interest on outstanding availments based on annual rate computed and billed monthly by SBC on the basis of its prevailing monthly rate. It is understood that the annual rate shall in no case exceed the total monthly prevailing rate as computed by SBC. I hereby give my continuing consent without need of additional confirmation to the interests stipulated as computed by SBC. The interests shall be due on the first day of every month after date of availment. x x x[8]

To secure the credit line, the spouses Mercado executed a Real Estate Mortgage[9] in favor of Security Bank on July 3, 1996 over their properties covered by Transfer Certificate of Title (TCT) No. T-103519 (located in Lipa

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4 *Rollo* (G.R. No. 192934), pp. 64-78; penned by Presiding Judge Paterno V. Tac-an.
5 *Id.* at 79-82.
6 *Id.* at 51, 94.
7 *Id.* at 94.
8 *Id.* at 52; Records (Civil Case No. 5808), Vol. I, p. 26.
9 *Rollo* (G.R. No. 192934), pp. 95-98.

City, Batangas), and TCT No. T-89822 (located in San Jose, Batangas).[10] On September 13, 1996, the spouses Mercado executed another Real Estate Mortgage[11] in favor of Security Bank this time over their properties located in Batangas City, Batangas covered by TCT Nos. T-33150, T-34288, and T-34289 to secure an additional amount of ₱7,000,000.00 under the same revolving credit agreement.

Subsequently, the spouses Mercado defaulted in their payment under the revolving credit line agreement. Security Bank requested the spouses Mercado to update their account, and sent a final demand letter on March 31, 1999.[12] Thereafter, it filed a petition for extrajudicial foreclosure pursuant to Act No. 3135,[13] as amended, with the Office of the Clerk of Court and *Ex-Officio* Sheriff of the RTC of Lipa City with respect to the parcel of land situated in Lipa City. Security Bank likewise filed a similar petition with the Office of the Clerk of Court and *Ex-Officio* Sheriff of the RTC of Batangas City with respect to the parcels of land located in San Jose, Batangas and Batangas City.[14]

The respective notices of the foreclosure sales of the properties were published in newspapers of general circulation once a week for three consecutive weeks as required by Act No. 3135, as amended. However, the publication of the notices of the foreclosure of the properties in Batangas City and San Jose, Batangas contained errors with respect to their technical description. Security Bank caused the publication of an erratum in a newspaper to correct these errors. The corrections consist of the following: (1) TCT No. 33150 – "Lot 952-C-1" to "Lot 952-C-1-**B**;" and (2) TCT No. 89822 – "Lot 1931 Cadm- 164-D" to "Lot 1931 Cadm **4**64-D." The erratum was published only once, and did not correct the lack of indication of location in both cases.[15]

On October 19, 1999, the foreclosure sale of the parcel of land in Lipa City, Batangas was held wherein Security Bank was adjudged as the winning bidder. The Certificate of Sale[16] over it was issued on November 3, 1999. A similar foreclosure sale was conducted over the parcels of land in Batangas City and San Jose, Batangas where Security Bank was likewise adjudged as the winning bidder. The Certificate of Sale[17] over these properties was issued on October 29, 1999. Both Certificates of Sale were registered, respectively, with the Registry of Deeds of Lipa City on November 11, 1999 and the Registry of Deeds of Batangas City on November 17, 1999.[18]

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10 *Id.* at 51, 99-101.
11 *Id.* at 102-105.
12 *Id.* at 66; Records (Civil Case No. 5808), Vol. 1, p. 38.
13 An Act to Regulate the Sale of Property Under Special Powers Inserted in or Annexed to Real-Estate Mortgages (1924).
14 *Rollo* (G.R. No. 192934), p. 52.
15 *Id.* at 53, 73.
16 *Id.* at 114-115.
17 *Id.* at 112-113.
18 *Id.* at 53.

On September 18, 2000, the spouses Mercado offered to redeem the foreclosed properties for ₱10,000,000.00. However, Security Bank allegedly refused the offer and made a counter-offer in the amount of ₱15,000,000.00.[19]

On November 8, 2000, the spouses Mercado filed a complaint for annulment of foreclosure sale, damages, injunction, specific performance, and accounting with application for temporary restraining order and/or preliminary injunction[20] with the RTC of Batangas City, docketed as Civil Case No. 5808 and eventually assigned to Branch 84.[21] In the complaint, the spouses Mercado averred that: (1) the parcel of land in San Jose, Batangas should not have been foreclosed together with the properties in Batangas City because they are covered by separate real estate mortgages; (2) the requirements of posting and publication of the notice under Act No. 3135, as amended, were not complied with; (3) Security Bank acted arbitrarily in disallowing the redemption of the foreclosed properties for ₱10,000,000.00; (4) the total price for all of the parcels of land only amounted to ₱4,723,620.00; and (5) the interests and the penalties imposed by Security Bank on their obligations were iniquitous and unconscionable.[22]

Meanwhile, Security Bank, after having consolidated its titles to the foreclosed parcels of land, filed an *ex-parte* petition for issuance of a writ of possession[23] over the parcels of land located in Batangas City and San Jose, Batangas with the RTC of Batangas City on June 9, 2005. The case was docketed as LRC Case No. N-1685 and subsequently raffled to Branch 84 where Civil Case No. 5808 was pending.[24]

Thereafter, the two cases were consolidated before Branch 84 of the RTC of Batangas City.

In its February 26, 2007 Decision,[25] the RTC declared that: (1) the foreclosure sales of the five parcels of land void; (2) the interest rates contained in the revolving credit line agreement void for being potestative or solely based on the will of Security Bank; and (3) the sum of ₱8,000,000.00 as the true and correct obligation of the spouses Mercado to Security Bank.[26]

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19 *Id.*

20 Records (Civil Case No. 5808), Vol. I, pp. 1-11.

21 *Rollo* (G.R. No. 192934), pp. 28-29.

22 Records (Civil Case No. 5808), Vol. I, pp. 6-8.

23 Records (LRC Case No. N-1685), pp. 1-5.

24 *Rollo* (G.R. No. 192934), p. 54.

25 *Supra* note 4.

26 *Rollo* (G.R. No. 192934), pp. 77-78. The full dispositive portion of which states:

WHEREFORE, Judgment is hereby rendered in favor of [spouses Mercado] and against [Security Bank]:

1. Declaring as void the Foreclosure Sales concerning the following real properties:
   1. TCT No. T-103519 - Lipa City
   2. TCT No. T-89822 - San Jose, Batangas
   3. TCT No. 33150 - Batangas City
   4. TCT No. T-34289 - Batangas City
   5. TCT No. 34288 - Batangas City
2. [D]eclaring the interest rates contained in the addendum of the real property mortgagors/promissory notes as void as well as the interest and penalties computed and charged against [spouses Mercado] and declaring the sum of eight million (₱8,000,000.00) pesos as the true and correct obligation of [spouses

The RTC declared the foreclosure sales void because "[t]he act of making only one corrective publication x x x is a fatal omission committed by the mortgagee bank."[27] It also found merit in the spouses Mercado's contention that the parcel of land in San Jose, Batangas and the three parcels of land in Batangas City should not be lumped together in a single foreclosure sale. Not only does it make the redemption onerous, it further violates Sections 1 and 5 of Act No. 3135 which do not envision and permit a single sale of more than one real estate mortgage separately constituted. The notice of sale itself is also defective because the act of making only one corrective publication is fatal.[28]

The RTC also ruled that the stipulation as to the interest rate on the availments under the revolving credit line agreement "where the fixing of the interest rate is the sole prerogative of the creditor/mortgagee, belongs to the class of potestative condition which is null and void under [Article] 1308 of the New Civil [C]ode."[29] It also violates Central Bank Circular No. 1191 which requires the interest rate for each re-pricing period to be subject to a mutual agreement between the borrower and bank. As such, no interest has been expressly stipulated in writing as required under Article 1956 of the New Civil Code.[30] The RTC ruled that since the spouses Mercado offered to pay the higher amount of ₱10,000,000.00 and the bank unjustifiably refused to accept it, no interest shall be due and demandable after the offer.[31]

Security Bank moved for reconsideration of the RTC's Decision, claiming that the trial court: (1) does not have jurisdiction over the parcels of land in Lipa City, Batangas; and (2) erred in limiting the obligation to only ₱8,000,000.00.[32]

The RTC modified its Decision in an Amendatory Order[33] dated June 19, 2007 where it declared that: (1) only the foreclosure sales of the parcels of land in Batangas City and San Jose, Batangas are void as it has no jurisdiction over the properties in Lipa City, Batangas; (2) the obligation of the spouses Mercado is ₱7,500,000.00, after deducting ₱500,000.00 from the principal loan of ₱1,000,000.00; and (3) as "cost of money," the obligation shall bear the interest at the rate of 6% from the time of date of the Amendatory Order until fully paid.[34]

Mercado] to [Security Bank] which shall be the basis of payment to the bank and which amount may be deposited by way of consignation should the bank refuse to accept it.

Such consignation with prior and subsequent notice to the Bank shall automatically extinguish the P8,000,000.00 loan if seasonably made.

3. [O]rdering the payment of attorney's fees of P50,000.00.
4. [M]aking the injunction permanent against the enforcement of the real estate mortgages and the foreclosure sales x x x[.]
5. Cost of suit.

27 *Id.* at 74.
28 *Id.* at 74-76.
29 *Id.* at 74.
30 *Id.* at 75.
31 *Id.* at 77.
32 Records (Civil Case No. 5808), Vol. II, pp. 83-101.
33 *Supra* note 5.
34 *Rollo* (G.R. No. 192934), pp. 81-82. The dispositive portion of which provides:

The CA, on appeal, affirmed with modifications the RTC Amended Decision. It agreed that the error in the technical description of the property rendered the notice of foreclosure sale defective. Security Bank's subsequent single publication of an erratum will not cure the defective notice; it is as if no valid publication of the notice of the foreclosure sale was made.[35] The CA also concluded that the provisos giving Security Bank the sole discretion to determine the annual interest rate is violative of the principle of mutuality of contracts because there is no reference rate from which to peg the annual interest rate to be imposed.[36]

The CA, however, disagreed with the trial court's findings as to the amount of the outstanding obligation, the imposition of interest, and the penalty. As to the principal amount of the obligation and the legal interest, it noted that the liability of the spouses Mercado from Security Bank is ₱7,516,880.00 or the principal obligation of ₱8,000,000.00 less the amount of ₱483,120.00 for which the Lipa City property has been sold.[37] It also modified the legal interest rate imposed from 6% to 12% from the date of extrajudicial demand, *i.e.*, March 31, 1999.[38] Lastly, it imposed the stipulated 2% monthly penalty under the revolving credit line agreement.[39] Thus:

> **WHEREFORE**, in view of the foregoing premises, the instant appeal is hereby **PARTIALLY GRANTED**. Accordingly, the assailed Decision dated February 26, 2007 and the Amendatory Order dated June 19, 2007 are hereby **MODIFIED**. [Spouses Mercado] are hereby ordered to pay [Security Bank] the sum of Seven Million Five Hundred Sixteen Thousand Eight Hundred Eighty Pesos (P7,516,880.00) with interest at the rate of twelve percent (12%) *per annum* from March 30, 1999, the date of extrajudicial demand, until fully paid. [Spouses Mercado] are further ordered to pay the stipulated penalty of two percent (2%) per month on the amount due in favor of Security Bank. The award of attorney's fees in favor of [spouses Mercado] is hereby deleted for lack of merit. All

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WHEREFORE, judgment is rendered in favor of [spouses Mercado] and against [Security Bank]:

1. Declaring as void the foreclosure sale concerning the following real properties: []1.) TCT No. T-89822 - San Jose, Batangas; 2.) TCT No. 33150 - Batangas City; 3.) TCT No. T-34289 - Batangas City; 4.) TCT No. 34288 - Batangas City[];

x x x x

3. [D]eclaring the sum of Php 7,500,000.00 as the principal obligation of the said [spouses Mercado] instead of Php 15,000,000.00 as demanded [by Security Bank] to which is being added from the date of this Amended Decision the rate of cost of money of 6% per annum or ½ percent per month until fully paid;
4. [D]enying the petition for issuance of writ of possession;

x x x x

6. [M]aking the injunction permanent against the enforcement of the real estate mortgages and against the foreclosure sales in respect to the above-named properties[.]

[35] *Id.* at 58-59.
[36] *Id.* at 60-61.
[37] *Id.* at 61.
[38] *Id.*; Records (Civil Case No. 5808), Vol. I, p. 38.
[39] *Rollo* (G.R. No. 192934), p. 62.

other dispositions of the trial court are hereby **AFFIRMED**.[40]

Hence, these consolidated petitions.

Security Bank argues that the CA erred in declaring: (1) the foreclosure sale invalid; and (2) the provisions on interest rate violative of the principle of mutuality of contracts. *First*, the foreclosure sale is valid because Security Bank complied with the publication requirements of Act No. 3135, as amended. The mistake in the original notice is inconsequential or minor since it only pertains to a letter and number in the technical description without actually affecting the actual size, location, and/or description or title number of the property.[41] It invokes Office of the Court Administrator (OCA) Circular No. 14[42] issued on May 29, 1984 governing the format of sale which allegedly does not require that the complete technical description of the property be published.[43] *Second*, Security Bank insists that the provision on the interest rate observed the principle of mutuality of contracts. Absolute discretion on its part is wanting because a ceiling on the maximum applicable rate is found in the addendum. It is the market forces that dictate and establish the rate of interest to be applied and takes into account various factors such as, but not limited to, Singapore Rate, London Rate, Inter-Bank Rate which serve as reference rates. This is acceptable, as held in *Polotan, Sr. v. Court of Appeals (Eleventh Division)*.[44] Further, the spouses Mercado are bound by the rate because they were aware of, and had freely and voluntarily assented to it.[45]

The spouses Mercado on the other hand, claim that the CA erred in imposing interest and penalty from the date of extrajudicial demand until finality of the Decision. Under the doctrine of operative facts laid down in *Spouses Caraig v. Alday*[46] and *Andal v. Philippine National Bank*,[47] the interest and penalty were considered paid by the auction sale.[48] As such, interest should only run from the finality of this Decision. They also assert that they should be excused from paying the penalty because of economic crises, and their lack of bad faith in this case.[49]

Initially, we denied the spouses Mercado's petition (G.R. No. 197010) in our Resolution[50] dated July 27, 2011. Upon the spouses Mercado's motion for reconsideration,[51] we reinstated the petition on April 18, 2012.[52]

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40 *Id.* at 62-63.
41 *Id.* at 35.
42 Revision and/or Modification of the Notice of Sale of Extra-Judicial Foreclosure.
43 *Rollo* (G.R. No. 192934), p. 37.
44 G.R. No. 119379, September 25, 1998, 296 SCRA 247.
45 *Rollo* (G.R. No. 192934), pp. 40-43.
46 CA-G.R. CV No. 76029, May 31, 2007.
47 G.R. No. 194201, November 27, 2013, 711 SCRA 15.
48 *Rollo* (G.R. No. 197010), pp. 59-60.
49 *Id.* at 17-19.
50 *Id.* at 52.
51 *Id.* at 59-63.
52 *Id.* at 68.

The following issues are presented for this Court's resolution:

I. Whether the foreclosure sales of the parcels of land in Batangas City and San Jose, Batangas are valid.

II. Whether the provisions on interest rate in the revolving credit line agreement and its addendum are void for being violative of the principle of mutuality of contracts.

III. Whether interest and penalty are due and demandable from date of auction sale until finality of the judgment declaring the foreclosure void under the doctrine of operative facts.

We deny the petitions.

I

The foreclosure sales of the properties in Batangas City and San Jose, Batangas are void for non-compliance with the publication requirement of the notice of sale.

Act No. 3135, as amended, provides for the statutory requirements for a valid extrajudicial foreclosure sale. Among the requisites is a valid notice of sale. Section 3, as amended, requires that when the value of the property reaches a threshold, the notice of sale must be published once a week for at least three consecutive weeks in a newspaper of general circulation:

> Sec. 3. Notice shall be given by posting notices of the sale for not less than twenty days in at least three public places of the municipality or city where the property is situated, and **if such property is worth more than four hundred pesos, such notice shall also be published once a week for at least three consecutive weeks in a newspaper of general circulation in the municipality or city.** (Emphasis supplied.)

We have time and again underscored the importance of the notice of sale and its publication. Publication of the notice is required "to give the x x x foreclosure sale a reasonably wide publicity such that those interested might attend the public sale."[53] It gives as much advertising to the sale as possible in order to secure bidders and prevent a sacrifice of the property. We reiterated this in *Caubang v. Crisologo*[54] where we said:

> The principal object of a notice of sale in a foreclosure of mortgage is not so much to notify the mortgagor as to inform the public generally of the nature and condition of the property to be sold, and of the time, place, and terms of the

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53 *Philippine National Bank v. Maraya, Jr.*, G.R. No. 164104, September 11, 2009, 599 SCRA 394, 400.
54 G.R. No. 174581, February 4, 2015, 749 SCRA 563.

> sale. Notices are given to secure bidders and prevent a sacrifice of the property. Therefore, statutory provisions governing publication of notice of mortgage foreclosure sales must be strictly complied with and slight deviations therefrom will invalidate the notice and render the sale, at the very least, voidable. Certainly, the statutory requirements of posting and publication are mandated and imbued with public policy considerations. Failure to advertise a mortgage foreclosure sale in compliance with the statutory requirements constitutes a jurisdictional defect, and any substantial error in a notice of sale will render the notice insufficient and will consequently vitiate the sale.[55] (Citation omitted.)

Failure to advertise a mortgage foreclosure sale in compliance with statutory requirements constitutes a jurisdictional defect which invalidates the sale.[56] This jurisdictional requirement may not be waived by the parties; to allow them to do so would convert the required public sale into a private sale.[57] Thus, the statutory provisions governing publication of notice of mortgage foreclosure sales must be strictly complied with, and that even slight deviations therefrom will invalidate the notice and render the sale at least voidable.[58]

To demonstrate the strictness of the rule, we have invalidated foreclosure sales for lighter reasons. In one case,[59] we declared a foreclosure sale void for failing to comply with the requirement that the notice shall be published once a week for at least three consecutive weeks. There, although the notice was published three times, the second publication of the notice was done on the first day of the third week, and not within the period for the second week.[60]

Nevertheless, the validity of a notice of sale is not affected by immaterial errors.[61] Only a substantial error or omission in a notice of sale will render the notice insufficient and vitiate the sale.[62] An error is substantial if it will deter or mislead bidders, depreciate the value of the property or prevent it from bringing a fair price.[63]

In this case, the errors in the notice consist of: (1) TCT No. T-33150 – "Lot 952-C-1" which should be "Lot 952-C-1-**B;**" (2) TCT No. T-89822 – "Lot 1931, Cadm- 164-D" which should be "Lot 1931 Cadm **4**64-D;"[64] and

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55 *Id.* at 568.
56 *Tambunting v. Court of Appeals*, G.R. No. L-48278, November 8, 1988, 167 SCRA 16, 23-24.
57 *Philippine National Bank v. Maraya, Jr.*, *supra* note 53.
58 *Tambunting v. Court of Appeals*, *supra* at 25. Citation omitted.
59 *Philippine National Bank v. Court of Appeals*, G.R. No. 98382, May 17, 1993, 222 SCRA 134.
60 *Id.* at 140-143.
61 *K-Phil., Inc. v. Metropolitan Bank & Trust Company*, G.R. No. 167500, October 17, 2008, 569 SCRA 459, 466.
62 *Tambunting v. Court of Appeals*, *supra* note 56.
63 *K-Phil., Inc. v. Metropolitan Bank and Trust Company*, *supra* note 61 at 465-466.
64 See TCT No. T-33150, *rollo* (G.R. No. 192934), p. 106; see also TCT No. T-89822, *id.* at 100.

(3) the omission of the location.[65] While the errors seem inconsequential, they in fact constitute data important to prospective bidders when they decide whether to acquire any of the lots announced to be auctioned. First, the published notice misidentified the identity of the properties. Since the lot numbers are misstated, the notice effectively identified lots other than the ones sought to be sold. Second, the published notice omitted the exact locations of the properties. As a result, prospective buyers are left completely unaware of the type of neighborhood and conforming areas they may consider buying into. With the properties misidentified and their locations omitted, the properties' sizes and ultimately, the determination of their probable market prices, are consequently compromised. The errors are of such nature that they will significantly affect the public's decision on whether to participate in the public auction. We find that the errors can deter or mislead bidders, depreciate the value of the properties or prevent the process from fetching a fair price.

Our ruling finds support in *San Jose v. Court of Appeals*[66] where we nullified a foreclosure sale on the ground that the notice did not contain the correct number of the TCT of the property to be sold. We rejected the contention of the mortgagee-creditor that prospective bidders may still rely on the technical description because it was accurate. We held that the notice must contain the correct title number and technical description of the property to be sold:

> The Notice of Sheriff[']s Sale, in this case, did not state the correct number of the transfer certificate of title of the property to be sold. This is a substantial and fatal error which resulted in invalidating the *entire* Notice. That the correct technical description appeared on the Notice does not constitute substantial compliance with the statutory requirements. The purpose of the publication of the Notice of Sheriff[']s Sale is to inform all interested parties of the date, time and place of the foreclosure sale of the real property subject thereof. Logically, this not only requires that the correct date, time and place of the foreclosure sale appear in the notice but also that any and all interested parties be able to determine that what is about to be sold at the foreclosure sale is the real property in which they have an interest.
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> The Court is not unaware of the fact that the majority of the population do not have the necessary knowledge to be able to understand the technical descriptions in certificates of title. It is to be noted and stressed that the Notice is not meant only for individuals with the training to understand technical descriptions of property but also for the layman with an interest in the property to be sold, who normally relies on the number of the certificate of title. To hold that the publication of the correct technical description, with an incorrect title number, of the property to be sold constitutes

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[65] *Id.* at 73.

[66] G.R. No. 106953, August 19, 1993, 225 SCRA 450.

> substantial compliance would certainly defeat the purpose of the Notice. This is not to say that a correct statement of the title number but with an incorrect technical description in the notice of sale constitutes a valid notice of sale. **The Notice of Sheriff[']s Sale, to be valid, must contain the *correct* title number and the *correct* technical description of the property to be sold.**[67] (Emphasis supplied.)

We do not agree with Security Bank's reliance on OCA Circular No. 14 (s. 1984). While it is true that the circular does not require the full technical description of the properties, it still requires the inclusion of the salient portions such as the lot number of the property and its boundaries.[68] In any case, what is apparent is that Security Bank published incorrect data in the notice that could bring about confusion to prospective bidders. In fact, their subsequent publication of an erratum is recognition that the error is significant enough to bring about confusion as to the identity, location, and size of the properties.

The publication of a single erratum, however, does not cure the defect. As correctly pointed out by the RTC, "[t]he act of making only one corrective publication in the publication requirement, instead of three (3) corrections is a fatal omission committed by the mortgagee bank."[69] To reiterate, the published notices that contain fatal errors are nullities. Thus, the erratum is considered as a new notice that is subject to the publication requirement for once a week for at least three consecutive weeks in a newspaper of general circulation in the municipality or city where the property is located. Here, however, it was published only once.

While there are cases where we upheld foreclosure sales on the ground that the mortgagor-debtor's act of redeeming the property amounts to estoppel, we cannot apply this equitable principle here. For one, Security Bank never raised the issue in its pleadings. Defenses and objections that are not pleaded in the answer or motion to dismiss are deemed waived.[70] Second, estoppel is a mere principle in equity. We cannot grant estoppel for the reason that Security Bank itself denies that the spouses Mercado offered to redeem the Batangas properties.[71] Thus, the element of reliance is absent.

II

The interest rate provisions in the parties' agreement violate the principle of mutuality of contracts.

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67 *Id.* at 454.

68 The relevant portion of OCA Circular No. 14 provides:
NOTICE OF EXTRA-JUDICIAL SALE
x x x x
TRANSFER CERTIFICATE OF TITLE NO. _____
A parcel of land _____ situated in ____ containing an area _____, more or less ,____ x x x.

69 *Rollo* (G.R. No. 192934), p. 74.

70 RULES OF COURT, Rule 9, Sec. 1.

71 *Rollo* (G.R. No. 192934), p. 71.

a.

The principle of mutuality of contracts is found in Article 1308 of the New Civil Code, which states that contracts must bind both contracting parties, and its validity or compliance cannot be left to the will of one of them. The binding effect of any agreement between parties to a contract is premised on two settled principles: (1) that any obligation arising from contract has the force of law between the parties; and (2) that there must be mutuality between the parties based on their essential equality.[72] As such, any contract which appears to be heavily weighed in favor of one of the parties so as to lead to an unconscionable result is void. Likewise, any stipulation regarding the validity or compliance of the contract that is potestative or is left solely to the will of one of the parties is invalid.[73] This holds true not only as to the original terms of the contract but also to its modifications. Consequently, any change in a contract must be made with the consent of the contracting parties, and must be mutually agreed upon. Otherwise, it has no binding effect.[74]

Stipulations as to the payment of interest are subject to the principle of mutuality of contracts. As a principal condition and an important component in contracts of loan,[75] interest rates are only allowed if agreed upon by express stipulation of the parties, and only when reduced into writing.[76] Any change to it must be mutually agreed upon, or it produces no binding effect:

> Basic is the rule that there can be no contract in its true sense without the mutual assent of the parties. If this consent is absent on the part of one who contracts, the act has no more efficacy than if it had been done under duress or by a person of unsound mind. Similarly, contract changes must be made with the consent of the contracting parties. The minds of all the parties must meet as to the proposed modification, especially when it affects an important aspect of the agreement. In the case of loan contracts, the interest rate is undeniably always a vital component, for it can make or break a capital venture. Thus, any change must be mutually agreed upon, otherwise, it produces no binding effect.[77] (Citation omitted.)

Thus, in several cases, we declared void stipulations that allowed for the unilateral modification of interest rates. In *Philippine National Bank v. Court of Appeals*,[78] we disallowed the creditor-bank from increasing the

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[72] *Almeda v. Court of Appeals,* G.R. No. 113412, April 17, 1996, 256 SCRA 292, 299-300.

[73] *Id.*

[74] *Silos v. Philippine National Bank,* G.R. No. 181045, July 2, 2014, 728 SCRA 617, 646.

[75] *Id.* at 660.

[76] Article 1956 of the New Civil Code provides that: "[n]o interest shall be due unless it has been expressly stipulated in writing."

See also *Prisma Construction & Development Corporation v. Menchavez*, G.R. No. 160545, March 9, 2010, 614 SCRA 590, 598.

[77] *Philippine Savings Bank v. Castillo*, G.R. No. 193178, May 30, 2011, 649 SCRA 527, 537.

[78] G.R. No. 88880, April 30, 1991, 196 SCRA 536.

stipulated interest rate at will for being violative of the principle of mutuality of contracts. We said:

> Besides violating P.D. 116, the unilateral action of the PNB in increasing the interest rate on the private respondent's loan, violated the mutuality of contracts ordained in Article 1308 of the Civil Code:
>
> "ART. 1308. The contract must bind both contracting parties; its validity or compliance cannot be left to the will of one of them."
>
> In order that obligations arising from contracts may have the force of law between the parties, there must be *mutuality* between the parties based on their essential equality. A contract containing a condition which makes its fulfillment dependent exclusively upon the uncontrolled will of one of the contracting parties, is void (Garcia vs. Rita Legarda, Inc., 21 SCRA 555). Hence, even assuming that the P1.8 million loan agreement between the PNB and the private respondent gave the PNB a license (although in fact there was none) to increase the interest rate at will during the term of the loan, that license would have been null and void for being violative of the principle of mutuality essential in contracts. It would have invested the loan agreement with the character of a contract of adhesion, where the parties do not bargain on equal footing, the weaker party's (the debtor) participation being reduced to the alternative "to take it or leave it" (Qua vs. Law Union & Rock Insurance Co., 95 Phil. 85). Such a contract is a veritable trap for the weaker party whom the courts of justice must protect against abuse and imposition.[79] (Italics in the original.)

The same treatment is given to stipulations that give one party the unbridled discretion, without the conformity of the other, to increase the rate of interest notwithstanding the inclusion of a similar discretion to decrease it. In *Philippine Savings Bank v. Castillo*[80] we declared void a stipulation[81] that allows for both an increase or decrease of the interest rate, without subjecting the modification to the mutual agreement of the parties:

> Escalation clauses are generally valid and do not contravene public policy. They are common in credit agreements as means of maintaining fiscal stability and retaining the value of money on long-term contracts. To prevent any one-sidedness that these clauses may cause, we have held in *Banco Filipino Savings and Mortgage Bank v. Judge Navarro* that there should be a corresponding de-

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79 *Id.* at 544-545.

80 *Supra.*

81 *Id.* at 529. The clause therein provided:

The rate of interest and/or bank charges herein stipulated, during the terms of this promissory note, its extensions, renewals or other modifications, may be increased, decreased or otherwise changed from time to time within the rate of interest and charges allowed under present or future law(s) and/or government regulation(s) as the PHILIPPINE SAVINGS BANK may prescribe for its debtors.

> escalation clause that would authorize a reduction in the interest rates corresponding to downward changes made by law or by the Monetary Board. As can be gleaned from the parties' loan agreement, a de-escalation clause is provided, by virtue of which, petitioner had lowered its interest rates.
>
> Nevertheless, the validity of the escalation clause did not give petitioner the unbridled right to unilaterally adjust interest rates. The adjustment should have still been subjected to the mutual agreement of the contracting parties. In light of the absence of consent on the part of respondents to the modifications in the interest rates, the adjusted rates cannot bind them notwithstanding the inclusion of a de-escalation clause in the loan agreement.[82] (Underscoring supplied; citation omitted.)

We reiterated this in *Juico v. China Banking Corporation*,[83] where we held that the lack of written notice and written consent of the borrowers made the interest proviso a one-sided imposition that does not have the force of law between the parties:

> This notwithstanding, we hold that the escalation clause is still void because it grants respondent the power to impose an increased rate of interest without a written notice to petitioners and their written consent. Respondent's monthly telephone calls to petitioners advising them of the prevailing interest rates would not suffice. A detailed billing statement based on the new imposed interest with corresponding computation of the total debt should have been provided by the respondent to enable petitioners to make an informed decision. An appropriate form must also be signed by the petitioners to indicate their conformity to the new rates. Compliance with these requisites is essential to preserve the mutuality of contracts. For indeed, one-sided impositions do not have the force of law between the parties, because such impositions are not based on the parties' essential equality.[84] (Citation omitted.)

In the case of *Silos v. Philippine National Bank*,[85] we invalidated the following provisions:

> 1.03. Interest. (a) The Loan shall be subject to interest at the rate of 19.5% *per annum*. Interest shall be payable in advance every one hundred twenty days at the rate prevailing at the time of the renewal.
>
> (b) The Borrower agrees that the Bank may modify the interest rate in the Loan depending on whatever policy the Bank may adopt in the future, including without limitation,

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82 *Id.* at 537.
83 G.R. No. 187678, April 10, 2013, 695 SCRA 520.
84 *Id.* at 539.
85 *Supra* note 74.

> the shifting from the floating interest rate system to the fixed interest rate system, or vice versa. Where the Bank has imposed on the Loan interest at a rate *per annum*, which is equal to the Bank's spread over the current floating interest rate, the Borrower hereby agrees that the Bank may, without need of notice to the Borrower, increase or decrease its spread over the floating interest rate at any time depending on whatever policy it may adopt in the future.[86] (Emphasis and citation omitted, italics supplied.)

In *Silos*, an amendment to the above credit agreement was made:

> 1.03. Interest on Line Availments. (a) The Borrowers agree to pay interest on each Availment from date of each Availment up to but not including the date of full payment thereof at the rate *per annum* which is determined by the Bank to be prime rate plus applicable spread in effect as of the date of each Availment.[87] (Emphasis and citation omitted.)

In that case, we found that the method of fixing interest rates is based solely on the will of the bank. The method is "one-sided, indeterminate, and [based on] subjective criteria such as profitability, cost of money, bank costs, etc. x x x."[88] It is "arbitrary for there is no fixed standard or margin above or below these considerations."[89] More, it is worded in such a way that the borrower shall agree to whatever interest rate the bank fixes. Hence, the element of consent from or agreement by the borrower is completely lacking.

Here, the spouses Mercado supposedly: (1) agreed to pay an annual interest based on a "floating rate of interest;" (2) to be determined solely by Security Bank; (3) on the basis of Security Bank's own prevailing lending rate; (4) which shall not exceed the total monthly prevailing rate as computed by Security Bank; and (5) without need of additional confirmation to the interests stipulated as computed by Security Bank.

Notably, stipulations on floating rate of interest differ from escalation clauses. Escalation clauses are stipulations which allow for the increase (as well as the mandatory decrease) of the original fixed interest rate.[90] Meanwhile, floating rates of interest refer to the variable interest rate stated on a market-based reference rate agreed upon by the parties.[91] The former refers to the method by which fixed rates may be increased, while the latter pertains to the interest rate itself that is not fixed. Nevertheless, both are contractual provisions that entail adjustment of interest rates subject to the principle of mutuality of contracts. Thus, while the cited cases involve

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86 *Id.* at 623.
87 *Id.* at 624.
88 *Id.* at 659.
89 *Id.*
90 Manual of Regulations for Banks, Vol. 1, § X305.2.
91 Manual of Regulations for Banks, Vol. 1, § X305.3.

escalation clauses, the principles they lay down on mutuality equally apply to floating interest rate clauses.

The *Banko Sentral ng Pilipinas* (BSP) Manual of Regulations for Banks (MORB) allows banks and borrowers to agree on a floating rate of interest, provided that it must be based on market-based reference rates:

> § X305.3 Floating rates of interest. **The rate of interest on a floating rate loan during each interest period shall be stated on the basis of Manila Reference Rates (MRRs), T-Bill Rates or other market based reference rates plus a margin as may be agreed upon by the parties.**
>
> The MRRs for various interest periods shall be determined and announced by the Bangko Sentral every week and shall be based on the weighted average of the interest rates paid during the immediately preceding week by the ten (10) KBs with the highest combined levels of outstanding deposit substitutes and time deposits, on promissory notes issued and time deposits received by such banks, of P100,000 and over per transaction account, with maturities corresponding to the interest periods for which such MRRs are being determined. Such rates and the composition of the sample KBs shall be reviewed and determined at the beginning of every calendar semester on the basis of the banks' combined levels of outstanding deposit substitutes and time deposits as of 31 May or 30 November, as the case may be.
>
> The rate of interest on floating rate loans existing and outstanding as of 23 December 1995 shall continue to be determined on the basis of the MRRs obtained in accordance with the provisions of the rules existing as of 01 January 1989: *Provided, however*, That the parties to such existing floating rate loan agreements are not precluded from amending or modifying their loan agreements by adopting a floating rate of interest determined on the basis of the TBR or other market based reference rates.
>
> Where the loan agreement provides for a floating interest rate, the interest period, which shall be such period of time for which the rate of interest is fixed, shall be such period as may be agreed upon by the parties.
>
> For the purpose of computing the MRRs, banks shall accomplish the report forms, RS Form 2D and Form 2E (BSP 5-17-34A).[92] (Emphasis and underscoring supplied.)

This BSP requirement is consistent with the principle that the determination of interest rates cannot be left solely to the will of one party. It further emphasizes that the reference rate must be stated in writing, and must be agreed upon by the parties.

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[92] Manual of Regulation for Banks, Vol. 1, § X305.3; See also BSP Circular No. 99, December 23, 1995.

b.

Security Bank argues that the subject provisions on the interest rate observed the principle of mutuality of contracts. It claims that there is a ceiling on the maximum applicable rate, and it is the market forces that dictate and establish the rate of interest.

We disagree.

The RTC and CA were correct in holding that the interest provisions in the revolving credit line agreement and its addendum violate the principle of mutuality of contracts.

First, the authority to change the interest rate was given to Security Bank alone as the lender, without need of the written assent of the spouses Mercado. This unbridled discretion given to Security Bank is evidenced by the clause "I hereby give my continuing consent without need of additional confirmation to the interests stipulated as computed by [Security Bank]."[93] The lopsidedness of the imposition of interest rates is further highlighted by the lack of a breakdown of the interest rates imposed by Security Bank in its statement of account[94] accompanying its demand letter.

Second, the interest rate to be imposed is determined solely by Security Bank for lack of a stated, valid reference rate. The reference rate of "Security Bank's prevailing lending rate" is not pegged on a market-based reference rate as required by the BSP. In this regard, we do not agree with the CA that this case is similar with *Polotan, Sr. v. Court of Appeals (Eleventh Division)*.[95] There, we declared that escalation clauses are not basically wrong or legally objectionable *as long as they are not solely potestative but based on reasonable and valid grounds*. We held that the interest rate based on the "prevailing market rate" is valid because it cannot be said to be dependent solely on the will of the bank as it is also dependent on the prevailing market rates. The fluctuation in the market rates is beyond the control of the bank.[96] Here, however, the stipulated interest rate based on "Security Bank's prevailing lending rate" is not synonymous with "prevailing market rate." For one, Security Bank is still the one who determines its own prevailing lending rate. More, the argument that Security Bank is guided by other facts (or external factors such as Singapore Rate, London Rate, Inter-Bank Rate) in determining its prevailing monthly rate fails because these reference rates are not contained in writing as required by law and the BSP. Thus, we find that the interest stipulations here are akin to the ones invalidated in *Silos* and in *Philippine Savings Bank* for being potestative.

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93 Records (Civil Case No. 5808), Vol. I, p. 26.
94 *Id.* at 40.
95 *Supra* note 44.
96 *Id.* at 258.

In striking out these provisions, both in the original and the addendum, we note that there are no other stipulations in writing from which we can base an imposition of interest. Unlike in cases involving escalation clauses that allowed us to impose the original rate of interest, we cannot do the same here as there is none. Nevertheless, while we find that no stipulated interest rate may be imposed on the obligation, legal interest may still be imposed on the outstanding loan. *Eastern Shipping Lines, Inc. v. Court of Appeals*[97] and *Nacar v. Gallery Frames*[98] provide that in the absence of a stipulated interest, a loan obligation shall earn legal interest from the time of default, *i.e.*, from judicial or extrajudicial demand.[99]

III

In *Andal v. Philippine National Bank*,[100] the case cited by the spouses Mercado, we declared the mortgagor-debtors therein liable to pay interest at the rate equal to the legal interest rate from the time they defaulted in payment until their loan is fully paid. We also said that default, for purposes of determining when interest shall run, is to be counted from the time of the finality of decision determining the rate of interest. Spouses Mercado claim that following *Andal*, they, too, could not be deemed to have been in default from the time of the extrajudicial demand on March 31, 1991. They claim anew that since the validity of the interest rates is still being determined in this petition, interest should be imposed only after finality of this Decision.

They err. *Andal* is not squarely applicable to this case. In that case, there was a finding by both the trial court and the CA that no default can be declared because of the arbitrary, illegal, and unconscionable interest rates and penalty charges unilaterally imposed by the bank. There, the debtors questioned *the period of default in relation to the interest imposed* as it was an issue necessary for the determination of the validity of the foreclosure sales therein. In contrast, here, the spouses Mercado never denied that they defaulted in the payment of the principal obligation. They did not assert, from their complaint or up to their petition before this Court, that they would not have been in default were it not for the bank's imposition of the interest rates. Theories raised for the first time cannot be entertained in appeal.

Moreover, for purposes of computing when legal interest shall run, it is enough that the debtor be in default on the principal obligation. To be considered in default under the revolving credit line agreement, the borrower need not be in default for the whole amount, but for any amount due.[101] The

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97 G.R. No. 97412, July 12, 1994, 234 SCRA 78.

98 G.R. No. 189871, August 13, 2013, 703 SCRA 439.

99 *Id.* at 457-458.

100 *Supra* note 47.

101 See *Rollo* (G.R. No. 192934), p. 94. The revolving credit line enumerates the following as events of default:

14. Default – I shall be considered in default in the event that:

a) I am in default in any of these terms and conditions and/or I or the mortgagor am/is in default under the terms and conditions of the Mortgage,

b) my outstanding Availments exceed my Credit Limit,

spouses Mercado never challenged Security Bank's claim that they defaulted as to the payment of the principal obligation of ₱8,000,000.00. Thus, we find they have defaulted to this amount at the time Security Bank made an extrajudicial demand on March 31, 1999.

We also find no merit in their argument that penalty charges should not be imposed. While we see no legal basis to strike down the penalty stipulation, however, we reduce the penalty of 2% per month or 24% *per annum* for being iniquitous and unconscionable as allowed under Article 1229[102] of the Civil Code.

In *MCMP Construction Corp. v. Monark Equipment Corp.*,[103] we declared the rate of 36% *per annum* unconscionable and reduced it to 6% *per annum*. We thus similarly reduce the penalty here from 24% *per annum* to 6% *per annum* from the time of default, *i.e.*, extrajudicial demand.

We also modify the amount of the outstanding obligation of the spouses Mercado to Security Bank. To recall, the foreclosure sale over the parcel of land in Lipa City is not affected by the annulment proceedings. We thus find that the proceeds of the foreclosure sale over the parcel of land in Lipa City in the amount of ₱483,120.00 should be applied to the principal obligation of ₱8,000,000.00 plus interest and penalty from extrajudicial demand (March 31, 1999) until date of foreclosure sale (October 19, 1999).[104] The resulting deficiency shall earn legal interest at the rate of 12% from the filing of Security Bank's answer with counterclaim[105] on January 5, 2001 until June 30, 2013, and shall earn legal interest at the present rate of 6% from July 1, 2013 until finality of judgment.[106] Thus, the outstanding obligation of the spouses Mercado should be computed as follows:

Principal	₱8,000,000.00
Interest at 12% *per annum*	533.917.81

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c) I default in payment of any amount due hereunder,

d) I am in default in any of the terms and conditions of any contracts/evidence of indebtedness and related documents with Security Bank, or I am or the mortgagor is in default under the terms and conditions of any Mortgage which may now be existing or may subsequently be granted to me by Security Bank,

e) I violate terms and conditions of any contract with any bank or other persons, corporations, entities, for the payment of borrowed money, or any other events of defaults in such contracts,

f) Any creditor tries by legal process to attach or levy on my money or any property with Security Bank,

g) I apply for voluntary or involuntary relief under the bankruptcy or insolvency laws,

h) Security Bank believes on reasonable ground that it was induced by fraudulent misrepresentation on my part to grant me the MML. (Emphasis supplied.)

[102] Art. 1229. The judge shall equitably reduce the penalty when the principal obligation has been partly or irregularly complied with by the debtor. Even if there has been no performance, the penalty may also be reduced by the courts if it is iniquitous or unconscionable.

[103] G.R. No. 201001, November 10, 2014, 739 SCRA 432, 443.

[104] See *Juico v. China Banking Corporation, supra* note 83 at 541.

[105] Records (Civil Case No. 5808), Vol. I, pp. 89-106.

[106] *Nacar v. Gallery Frames, supra* note 98.

₱8,000,000.00 x 0.12 x (203 days/365 days)[107]	
Penalty at 6% *per annum*	266,958.90
₱8,000,000.00 x 0.06 x (203 days/365 days)	
	₱8,800,876.71
Less: Bid price for Lipa City property	483,120.00
TOTAL DEFICIENCY	₱8,317,756.71

WHEREFORE, the petitions are **DENIED**. Accordingly, the Court of Appeals' Decision dated July 19, 2010 and the Amendatory Order dated June 19, 2007 are hereby **MODIFIED**. Spouses Rodrigo and Erlinda Mercado are hereby ordered to pay Security Bank Corporation the sum of ₱8,317,756.71 representing the amount of deficiency, inclusive of interest and penalty. Said amount shall earn legal interest of 12% *per annum* from January 5, 2001 until June 30, 2013, and shall earn the legal interest of 6% *per annum* from July 1, 2013 until finality of this Decision. The total amount shall thereafter earn interest at the rate of 6% *per annum* from the finality of judgment until its full satisfaction.

No costs.

SO ORDERED.

FRANCIS H. JARDELEZA
Associate Justice

WE CONCUR:

(On Official Leave)
TERESITA J. LEONARDO-DE CASTRO
Associate Justice

MARIANO C. DEL CASTILLO
Associate Justice
Acting Chairperson

NOEL GIMENEZ TIJAM
Associate Justice

[107] This is the computed number of days from March 31, 1999, the date of extrajudicial demand, until October 19, 1999, the date of the foreclosure sale.

ALEXANDER G. GESMUNDO
Associate Justice

ATTESTATION

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

MARIANO C. DEL CASTILLO
Acting Chairperson, First Division
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 cases were assigned to the writer of the opinion of the Court's Division.

ANTONIO T. CARPIO
Senior Associate Justice[****]

[****] Per Sec. 12 of Republic Act No. 296, The Judiciary Act of 1948, as amended.