REYNALDO P. FLOIRENDO, JR., PETITIONER, VS. METROPOLITAN BANK AND TRUST COMPANY, RESPONDENT.

G.R. No. 148325. September 03, 2007

Ponente: SANDOVAL-GUTIERREZ, J.

Read online (full-text search, related cases, audio case brief): https://batas.org/library/g-r-no-148325/

SANDOVAL-GUTIERREZ, J.:

For our resolution is the instant Petition for Review on Certiorari under Rule 45 of the 1997 Rules of Civil Procedure, as amended, assailing the Decision[1] dated February 22, 2001 and Order[2] dated May 2, 2001 rendered by the Regional Trial Court (RTC), Branch 39, Cagayan de Oro City in Civil Case No. 98-476, entitled, "REYNALDO P. FLOIRENDO, JR., plaintiff, v. METROPOLITAN BANK AND TRUST COMPANY, ET AL., defendants."

Reynaldo P. Floirendo, Jr., petitioner, is the president and chairman of the Board of Directors of Reymill Realty Corporation, a domestic corporation engaged in real estate business. On March 20, 1996, he obtained a loan of P1,000,000.00 from the Metropolitan Bank and Trust Company, Cagayan de Oro City Branch, respondent, to infuse additional working capital for his company. As security for the loan, petitioner executed a real estate mortgage in favor of respondent bank over his four (4) parcels of land, all situated at Barangay Carmen, Cagayan de Oro City.

The loan was renewed for another year secured by the same real estate mortgage. Petitioner signed a promissory note dated March 14, 1997 fixing the rate of interest at "15.446% per annum for the first 30 days, subject to upward/downward adjustment every 30 days thereafter"; and a penalty charge of 18% per annum "based on any unpaid principal to be computed from date of default until payment of the obligation." The promissory note likewise provides that:

> The rate of interest and/or bank charges herein stipulated, during the term of this Promissory Note, its extension, renewals or other modifications, may be increased, decreased, or otherwise changed from time to time by the Bank without advance notice to me/us in the event of changes in the interest rate prescribed by law or the Monetary Board of the Central Bank of the Philippines, in the rediscount rate of member banks with the Central Bank of the Philippines, in the interest rates on savings and time deposits, in the interest rates on the bank's borrowings, in the reserve requirements, or in the overall costs of funding or money;
>
> I/We hereby expressly consent to any extension and/or renewal hereof in whole or in part and/or partial payment on account which may be requested by and/or granted to anyone of us for the payment of this note upon payment of the corresponding renewal or extension fee.

On July 11, 1997, respondent bank started imposing higher interest rates on petitioner's loan which varied through the months, in fact, as high as 30.244% in October 1997. As a result, petitioner could no longer pay the high interest rates charged by respondent bank. Thus, he negotiated for the renewal of his loan. Respondent bank agreed provided petitioner would pay the arrears in interest amounting to the total sum of P163,138.33. Despite payment by petitioner, respondent bank, instead of renewing the loan, filed with the Office of the Clerk of Court

and Provincial Sheriff, RTC, Cagayan de Oro City a petition for foreclosure of mortgage which was granted. On August 17, 1998, the auction sale was set.

Prior thereto or on August 11, 1998, petitioner filed with the RTC, Branch 39, same city, a complaint for reformation of real estate mortgage contract and promissory note, docketed as Civil Case No. 98-476. Referring to the real estate mortgage and the promissory note as "contracts of adhesion," petitioner alleged that the increased interest rates unilaterally imposed by respondent bank are scandalous, immoral, illegal and unconscionable. He also alleged that the terms and conditions of the real estate mortgage and the promissory note are such that they could be interpreted by respondent bank in whatever manner it wants, leaving petitioner at its mercy. Petitioner thus prayed for reformation of these documents and the issuance of a temporary restraining order (TRO) and a writ of preliminary injunction to enjoin the foreclosure and sale at public auction of his four (4) parcels of land.

On August 14, 1998, the RTC issued a TRO and on September 3, 1998, a writ of preliminary injunction.

In its answer to the complaint, respondent bank asserted that the interest stipulated by the parties in the promissory note is not per annum but on a month to month basis. The 15.446% interest appearing therein was good only for the first 30 days of the loan, subject to upward and downward adjustment every 30 days thereafter. The terms of the real estate mortgage and promissory note voluntarily entered into by petitioner are clear and unequivocal. There is, therefore, no legal and factual basis for an action for reformation of instruments.

On February 22, 2001, the RTC rendered a Judgment (1) dismissing the complaint for reformation of instruments, (2) dissolving the writ of preliminary injunction and (3) directing the sale at public auction of petitioner's mortgaged properties. The RTC ruled:

> In order that an action for reformation of an instrument may prosper, the following requisites must occur:
>
> 1.) There must have been a meeting of the minds upon the contract;
>
> 2.) The instrument or document evidencing the contract does not express the true agreement between the parties; and
>
> 3.) The failure of the instrument to express the agreement must be due to mistake, fraud, inequitable conduct or accident. (National Irrigation Administration v. Gamit, G.R. No. 85869, November 5, 1992)
>
> x x x
>
> A perusal further of the complaint and the evidences submitted by the parties convinced the court that there was certainly a meeting of the minds between the parties. Plaintiff and defendant bank entered into a contract of loan, the terms and conditions of which, especially on the rates of interest, are clearly and unequivocally spelled out in the promissory note. The court believes that there was absolutely no mistake, fraud or anything that could have prevented a meeting of the minds between the parties.
>
> The RTC upheld the validity of the escalation clause, thus:
>
> Escalation clauses are valid stipulations in commercial contract to maintain fiscal stability and to retain the value of money in loan term contracts, (Llorin v. CA, G.R. No. 103592, February 4, 1993).
>
> x x x x x x x x x
>
> x x x the Court has no other alternative to resolve Issue No. 1 that defendant bank is allowed to impose the interest rate questioned by plaintiff considering that Exhibit "B" and "B-1," which is Exhibit "1" and "1-A" of defendant bank is very clear that the rate of interest is 15.446% per annum for the first 30 days subject to upward/downward adjustment every 30 days thereafter.

Bar review courses, mock exams and a study planner that keeps you on pace - batas.org

On the issue of the validity of the foreclosure of the real estate mortgage, the RTC ruled that:

> It is a settled rule that in a real estate mortgage when the obligation is not paid when due, the mortgagee has the right to foreclose the mortgage and to have the property seized and sold in view of applying the proceeds to the payment of the obligation (Estate Investment House v. CA, 215 SCRA 734).

On May 2, 2001, petitioner filed a motion for reconsideration but it was denied for lack of merit.

Hence, the instant petition.

The fundamental issue for our resolution is whether the mortgage contract and the promissory note express the true agreement between the parties herein.

Petitioner contends that the "escalation clause" in the promissory note imposing 15.446% interest on the loan "for the first 30 days subject to upward/downward adjustment every 30 days thereafter" is illegal, excessive and arbitrary. The determination to increase or decrease such interest rate is primarily left to the discretion of respondent bank.

We agree.

We hold that the increases of interest rate unilaterally imposed by respondent bank without petitioner's assent are violative of the principle of mutuality of contracts ordained in Article 1308 of the Civil Code[3] which provides:

> Article 1308. The contract must bind both contracting parties; its validity or compliance cannot be left to the will of one of them.

The binding effect of any agreement between the parties to a contract is premised on two settled 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.[4] 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. Any stipulation regarding the validity or compliance of the contract which is left solely to the will of one of the parties is likewise invalid.[5]

The provision in the promissory note authorizing respondent bank to increase, decrease or otherwise change from time to time the rate of interest and/or bank charges "without advance notice" to petitioner, "in the event of change in the interest rate prescribed by law or the Monetary Board of the Central Bank of the Philippines," does not give respondent bank unrestrained freedom to charge any rate other than that which was agreed upon. Here, the monthly upward/downward adjustment of interest rate is left to the will of respondent bank alone. It violates the essence of mutuality of the contract.

In Philippine National Bank v. Court of Appeals,[6] and in later cases,[7] we held:

> 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 v. 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 v. 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.

In New Sampaguita Builders Construction, Inc. (NSBCI) v. Philippine National Bank,[8] we ruled that while it is true that escalation clauses are valid in maintaining fiscal stability and retaining the value of money on long term contracts, however, giving respondent an unbridled right to adjust the interest independently and upwardly would completely take away from petitioner the right to assent to an important modification in their agreement, hence, would negate the element of mutuality in their contracts. Such escalation clause would make the fulfillment of the contracts dependent exclusively upon the uncontrolled will of respondent bank and is therefore void. In the present case, the promissory note gives respondent bank authority to increase the interest rate at will during the term of the loan. This stipulation violates the principle of mutuality between the parties. It would be converting the loan agreement into a contract of adhesion where the parties do not bargain on equal footing, the weaker party's (petitioner's) participation being reduced to the alternative "to take it or leave it.[9] While the Usury Law ceiling on interest rate was lifted by Central Bank Circular No. 905, nothing therein could possibly be read as granting respondent bank carte blanche authority to raise interest rate to levels which would either enslave its borrower (petitioner herein) or lead to hemorrhaging of his assets.[10]

In Philippine National Bank v. Court of Appeals,[11] we declared void the escalation clause in the Credit Agreement between petitioner bank and private respondents whereby the "Bank reserves the right to increase the interest rate within the limit allowed by law at any time depending on whatever policy it may adopt in the future xxx." We held:

> It is basic that there can be no contract in the true sense in the absence of the element of agreement, or of mutual assent of the parties. If this assent is wanting on the part of one who contracts, his 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, it cannot be gainsaid that the rate of interest is always a vital component, for it can make or break a capital venture. Thus, any change must be mutually agreed upon, otherwise, it is bereft of any binding effect.
>
> We cannot countenance petitioner bank's posturing that that escalation clause at bench gives it unbridled right to unilaterally upwardly adjust the interest on private respondents' loan. That would completely take away from private respondents the right to assent to an important modification in their agreement, and would negate the element of mutuality in contracts.

Under Article 1310 of the Civil Code, courts are granted authority to reduce/increase interest rates equitably, thus:

> Article 1310. The determination shall not be obligatory if it is evidently inequitable. In such case, the courts shall decide what is equitable under the circumstances.

In the other Philippine National Bank v. Court of Appeals[12] case, we disauthorized petitioner bank from unilaterally raising the interest rate on the loan of private respondent from 18% to 32%, 41% and 48%. In Almeda v. Court of Appeals,[13] where the interest rate was increased from 21% to as high as 68% per annum, we declared arbitrary "the galloping increases in interest rate imposed by respondent bank on petitioners' loan, over the latter's vehement protests." In Medel v. Court of Appeals,[14] the stipulated interest of 5.5% per month or 66% per annum on a loan amounting to P500,000.00 was equitably reduced for being iniquitous, unconscionable and exorbitant. In Solangon v. Salazar,[15] the stipulated interest rate of 6% per month or 72% per annum was found to be "definitely outrageous and inordinate" and was reduced to 12% per annum which we deemed fair and reasonable. In Imperial v. Jaucian,[16] we ruled that the trial court was justified in reducing the stipulated interest rate from 16% to 1.167% or 14% per annum and the stipulated penalty charge from 5% to 1.167% per month or 14% per annum.

In this case, respondent bank started to increase the agreed interest rate of 15.446% per annum to 24.5% on July 11, 1997 and every month thereafter; 27% on August 11, 1997; 26% on September 10, 1997; 33% on October 15, 1997; 26.5% on November 27, 1997; 27% on December 1997; 29% on January 13, 1998; 30.244% on February 7, 1998; 24.49% on March 9, 1998; 22.9% on April 18, 1998; and 18% on May 21, 1998. Obviously, the rate increases are excessive and arbitrary. It bears reiterating that respondent bank unilaterally increased the interest rate without petitioner's knowledge and consent.

As mentioned earlier, petitioner negotiated for the renewal of his loan. As required by respondent bank, he paid the interests due. Respondent bank then could not claim that there was no attempt on his part to comply with his obligation. Yet, respondent bank hastily filed a petition to foreclose the mortgage to gain the upperhand in taking petitioner's four (4) parcels of land at bargain prices. Obviously, respondent bank acted in bad faith.

In sum, we find that the requisites for reformation of the mortgage contract and promissory note are present in this case. There has been meeting of minds of the parties upon these documents. However, these documents do not express the parties' true agreement on interest rates. And the failure of these documents to express their agreement on interest rates was due to respondent bank's inequitable conduct.

WHEREFORE, we GRANT the petition. The Judgment dated February 22, 2001 of the RTC of Cagayan de Oro City, Branch 39 in Civil Case No. 98-476 is REVERSED. The real estate mortgage contract and the promissory note agreed upon by the parties are reformed in the sense that any increase in the interest rate beyond 15.446% per annum should not be imposed by respondent bank without the consent of petitioner. The interest he paid in excess of 15.446% should be applied to the payment of the principal obligation.

SO ORDERED.

Puno, C.J., (Chairperson), Corona, Azcuna, and Garcia, JJ., concur.

---

[1] Annex "J" of the petition, rollo, pp. 86-95.

[2] Annex "O" of the petition, id., p. 112.

[3] Spouses Florendo v. Court of Appeals, G.R. No. 101771, December 17, 1996, 265 SCRA 678, citing Philippine National Bank v. Court of Appeals, 196 SCRA 536 (1991).

[4] Garcia v. Rita Legarda, Inc., No. L-20175, October 30, 1967, 21 SCRA 555, citing 8 Manresa 556; Almeda v. Court of Appeals, G.R. No. 113412, April 17, 1996, 256 SCRA 292; Philippine National Bank v. Court of Appeals, G.R. No. 88880, April 30, 1991, 196 SCRA 536.

[5] Almeda v. Court of Appeals, supra.

[6] Supra, at footnote 4.

[7] Philippine National Bank v. Court of Appeals, G.R. No. 107569, November 8, 1994, 238 SCRA 20; Philippine National Bank v. Court of Appeals, G.R No. 109563, July 9, 1996, 258 SCRA 549; Spouses Florendo v. Court of Appeals, supra, at footnote 3.

[8] G.R. No. 148753, July 20, 2004, 435 SCRA 565, citing Polotan Sr. v. Court of Appeals, 296 SCRA 247 (1998); Philippine National Bank v. Court of Appeals, supra, at footnote 7; Garcia v. Rita Legarda, Inc., supra, at footnote 4; Qua Chee Gan v. Law Union and Rock Insurance Co. Ltd., 98 Phil. 85 (1955); and Imperial v. Jaucian, supra, at footnote 10.

Bar review courses, mock exams and a study planner that keeps you on pace - batas.org

[9] Ibid., citing Philippine National Bank v. Court of Appeals, supra, at footnote 4.

[10] Ibid., citing Imperial v. Jaucian, 427 SCRA 517 (2004); Spouses Solangon v. Salazar, 360 SCRA 379 (2001) and Almeda v. Court of Appeals, supra, at footnote 4.

[11] Supra, at footnote 7.

[12] Supra, at footnote 4.

[13] Supra, at footnote 4.

[14] G.R. No. 131622, November 27, 1998, 299 SCRA 481.

[15] G.R. No. 125944, June 29, 2001, 360 SCRA 379.

[16] Supra, at footnote 10.

Study hands-free: podcast-style lessons with read-along highlighting - batas.org

ABOUT BATAS.ORG

Study smarter at BATAS.org

The Philippine bar review and law-school companion built around how your brain actually remembers.

The complete Philippine law library - free for everyone.

More than 100,000 Supreme Court decisions, Republic Acts, and executive issuances - full-text searchable, browsable by category and year, and always free. No paywall, no login. This PDF came from it.

Audio case-brief lectures.

Any decision becomes a podcast-style lecture - facts, issues, ruling, and doctrine - with read-along highlighting and a hands-free presentation mode. Study while commuting, working out, or resting your eyes.

Bar review built on the science of memory.

Complete, sequenced courses for all eight bar subjects, narrated like podcasts and reinforced with retrieval practice and spaced review - the study techniques with the strongest evidence behind them.

The full law-school curriculum.

One subscription unlocks the entire J.D. curriculum - every subject, every lesson, with your progress tracked down to the paragraph so you can pick up exactly where you left off, on any device.

Mock exams that tell you where you stand.

Timed multiple-choice exams graded instantly, with per-subject score breakdowns and focus suggestions that point you at your weakest topics first.

A study planner that keeps you on pace.

Set your schedule and BATAS tells you every day whether you are on track for bar day - and exactly which lesson to take next.

Start free at https://batas.org

The law library is free forever - and your first lesson is one click away.

The text of this document is an official public record and remains in the public domain. Formatting, presentation, and compilation © 2026 batas.org.

Downloaded free from the batas.org Law Library. Share it freely - the library is free for every law student, bar reviewee, and practitioner.