

PABLO P. GARCIA, PETITIONER, VS. YOLANDA VALDEZ VILLAR, RESPONDENT.

G.R. No. 158891. June 27, 2012

Ponente: LEONARDO-DE CASTRO, J.

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LEONARDO-DE CASTRO, J.:

This is a petition for review on certiorari[1] of the February 27, 2003 Decision[2] and July 2, 2003 Resolution[3] of the Court of Appeals in CA-G.R. SP No. 72714, which reversed the May 27, 2002 Decision[4] of the Regional Trial Court (RTC), Branch 92 of Quezon City in Civil Case No. Q-99-39139.

Lourdes V. Galas (Galas) was the original owner of a piece of property (subject property) located at Malindang St., Quezon City, covered by Transfer Certificate of Title (TCT) No. RT-67970(253279).[5]

On July 6, 1993, Galas, with her daughter, Ophelia G. Pingol (Pingol), as co-maker, mortgaged the subject property to Yolanda Valdez Villar (Villar) as security for a loan in the amount of Two Million Two Hundred Thousand Pesos (P2,200,000.00).[6]

On October 10, 1994, Galas, again with Pingol as her co-maker, mortgaged the same subject property to Pablo P. Garcia (Garcia) to secure her loan of One Million Eight Hundred Thousand Pesos (P1,800,000.00).[7]

Both mortgages were annotated at the back of TCT No. RT-67970 (253279), to wit:

REAL ESTATE MORTGAGE

Entry No. 6537/T-RT-67970(253279) MORTGAGE – In favor of Yolanda Valdez Villar m/to Jaime Villar to guarantee a principal obligation in the sum of P2,200,000- mortgagee's consent necessary in case of subsequent encumbrance or alienation of the property; Other conditions set forth in Doc. No. 97, Book No. VI, Page No. 20 of the Not. Pub. of Diana P. Magpantay

Date of Instrument: 7-6-93

Date of Inscription: 7-7-93

SECOND REAL ESTATE MORTGAGE

Entry No. 821/T-RT-67970(253279) MORTGAGE – In favor of Pablo Garcia m/to Isabela Garcia to guarantee a principal obligation in the sum of P1,800,000.00 mortgagee's consent necessary in case of subsequent encumbrance or alienation of the property; Other conditions set forth in Doc. No. 08, Book No. VII, Page No. 03 of the Not. Pub. of Azucena Espejo Lozada

Date of Instrument: 10/10/94

Date of Inscription: 10/11/94

LRC Consulta No. 169[8]

On November 21, 1996, Galas sold the subject property to Villar for One Million Five Hundred Thousand Pesos

(P1,500,000.00), and declared in the Deed of Sale[9] that such property was “free and clear of all liens and encumbrances of any kind whatsoever.”[10]

On December 3, 1996, the Deed of Sale was registered and, consequently, TCT No. RT-67970(253279) was cancelled and TCT No. N-168361[11] was issued in the name of Villar. Both Villar’s and Garcia’s mortgages were carried over and annotated at the back of Villar’s new TCT.[12]

On October 27, 1999, Garcia filed a Petition for Mandamus with Damages[13] against Villar before the RTC, Branch 92 of Quezon City. Garcia subsequently amended his petition to a Complaint for Foreclosure of Real Estate Mortgage with Damages.[14] Garcia alleged that when Villar purchased the subject property, she acted in bad faith and with malice as she knowingly and willfully disregarded the provisions on laws on judicial and extrajudicial foreclosure of mortgaged property. Garcia further claimed that when Villar purchased the subject property, Galas was relieved of her contractual obligation and the characters of creditor and debtor were merged in the person of Villar. Therefore, Garcia argued, he, as the second mortgagee, was subrogated to Villar’s original status as first mortgagee, which is the creditor with the right to foreclose. Garcia further asserted that he had demanded payment from Villar,[15] whose refusal compelled him to incur expenses in filing an action in court.[16]

Villar, in her Answer,[17] claimed that the complaint stated no cause of action and that the second mortgage was done in bad faith as it was without her consent and knowledge. Villar alleged that she only discovered the second mortgage when she had the Deed of Sale registered. Villar blamed Garcia for the controversy as he accepted the second mortgage without prior consent from her. She averred that there could be no subrogation as the assignment of credit was done with neither her knowledge nor prior consent. Villar added that Garcia should seek recourse against Galas and Pingol, with whom he had privity insofar as the second mortgage of property is concerned.

On May 23, 2000, the RTC issued a Pre-Trial Order[18] wherein the parties agreed on the following facts and issue:

STIPULATIONS OF FACTS/ADMISSIONS

The following are admitted:

- the defendant admits the second mortgage annotated at the back of TCT No. RT-67970 of Lourdes V. Galas with the qualification that the existence of said mortgage was discovered only in 1996 after the sale;
- the defendant admits the existence of the annotation of the second mortgage at the back of the title despite the transfer of the title in the name of the defendant;
- the plaintiff admits that defendant Yolanda Valdez Villar is the first mortgagee;
- the plaintiff admits that the first mortgage was annotated at the back of the title of the mortgagor Lourdes V. Galas; and
- the plaintiff admits that by virtue of the deed of sale the title of the property was transferred from the previous owner in favor of defendant Yolanda Valdez Villar.

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ISSUE

Whether or not the plaintiff, at this point in time, could judicially foreclose the property in question.

On June 8, 2000, upon Garcia’s manifestation, in open court, of his intention to file a Motion for Summary Judgment,[19] the RTC issued an Order[20] directing the parties to simultaneously file their respective memoranda within 20 days.

On June 26, 2000, Garcia filed a Motion for Summary Judgment with Affidavit of Merit[21] on the grounds that there was no genuine issue as to any of the material facts of the case and that he was entitled to a judgment as a matter of law.

On June 28, 2000, Garcia filed his Memorandum[22] in support of his Motion for Summary Judgment and in compliance with the RTC's June 8, 2000 Order. Garcia alleged that his equity of redemption had not yet been claimed since Villar did not foreclose the mortgaged property to satisfy her claim.

On August 13, 2000, Villar filed an Urgent Ex-Parte Motion for Extension of Time to File Her Memorandum.[23] This, however, was denied[24] by the RTC in view of Garcia's Opposition.[25]

On May 27, 2002, the RTC rendered its Decision, the dispositive portion of which reads:

WHEREFORE, the foregoing premises considered, judgment is hereby rendered in favor of the plaintiff Pablo P. Garcia and against the defendant Yolanda V. Villar, who is ordered to pay to the former within a period of not less than ninety (90) days nor more than one hundred twenty (120) days from entry of judgment, the sum of P1,800,000.00 plus legal interest from October 27, 1999 and upon failure of the defendant to pay the said amount within the prescribed period, the property subject matter of the 2[nd] Real Estate Mortgage dated October 10, 1994 shall, upon motion of the plaintiff, be sold at public auction in the manner and under the provisions of Rules 39 and 68 of the 1997 Revised Rules of Civil Procedure and other regulations governing sale of real estate under execution in order to satisfy the judgment in this case. The defendant is further ordered to pay costs.[26]

The RTC declared that the direct sale of the subject property to Villar, the first mortgagee, could not operate to deprive Garcia of his right as a second mortgagee. The RTC said that upon Galas's failure to pay her obligation, Villar should have foreclosed the subject property pursuant to Act No. 3135 as amended, to provide junior mortgagees like Garcia, the opportunity to satisfy their claims from the residue, if any, of the foreclosure sale proceeds. This, the RTC added, would have resulted in the extinguishment of the mortgages.[27]

The RTC held that the second mortgage constituted in Garcia's favor had not been discharged, and that Villar, as the new registered owner of the subject property with a subsisting mortgage, was liable for it.[28]

Villar appealed[29] this Decision to the Court of Appeals based on the arguments that Garcia had no valid cause of action against her; that he was in bad faith when he entered into a contract of mortgage with Galas, in light of the restriction imposed by the first mortgage; and that Garcia, as the one who gave the occasion for the commission of fraud, should suffer. Villar further asseverated that the second mortgage is a void and inexistent contract considering that its cause or object is contrary to law, moral, good customs, and public order or public policy, insofar as she was concerned.[30]

Garcia, in his Memorandum,[31] reiterated his position that his equity of redemption remained "unforeclosed" since Villar did not institute foreclosure proceedings. Garcia added that "the mortgage, until discharged, follows the property to whomever it may be transferred no matter how many times over it changes hands as long as the annotation is carried over." [32]

The Court of Appeals reversed the RTC in a Decision dated February 27, 2003, to wit:

WHEREFORE, the decision appealed from is REVERSED and another one entered DISMISSING the complaint for judicial foreclosure of real estate mortgage with damages.[33]

The Court of Appeals declared that Galas was free to mortgage the subject property even without Villar's consent as the restriction that the mortgagee's consent was necessary in case of a subsequent encumbrance was absent in the Deed of Real Estate Mortgage. In the same vein, the Court of Appeals said that the sale of the subject property

to Villar was valid as it found nothing in the records that would show that Galas violated the Deed of Real Estate Mortgage prior to the sale.[34]

In dismissing the complaint for judicial foreclosure of real estate mortgage with damages, the Court of Appeals held that Garcia had no cause of action against Villar “in the absence of evidence showing that the second mortgage executed in his favor by Lourdes V. Galas [had] been violated and that he [had] made a demand on the latter for the payment of the obligation secured by said mortgage prior to the institution of his complaint against Villar.”[35]

On March 20, 2003, Garcia filed a Motion for Reconsideration[36] on the ground that the Court of Appeals failed to resolve the main issue of the case, which was whether or not Garcia, as the second mortgagee, could still foreclose the mortgage after the subject property had been sold by Galas, the mortgage debtor, to Villar, the mortgage creditor.

This motion was denied for lack of merit by the Court of Appeals in its July 2, 2003 Resolution.

Garcia is now before this Court, with the same arguments he posited before the lower courts. In his Memorandum,[37] he added that the Deed of Real Estate Mortgage contained a stipulation, which is violative of the prohibition on pactum commissorium.

Issues

The crux of the controversy before us boils down to the propriety of Garcia’s demand upon Villar to either pay Galas’s debt of P1,800,000.00, or to judicially foreclose the subject property to satisfy the aforesaid debt. This Court will, however, address the following issues in seriatim:

- Whether or not the second mortgage to Garcia was valid;
- Whether or not the sale of the subject property to Villar was valid;
- Whether or not the sale of the subject property to Villar was in violation of the prohibition on pactum commissorium;
- Whether or not Garcia’s action for foreclosure of mortgage on the subject property can prosper.

Discussion

Validity of second mortgage to Garcia and sale of subject property to Villar

At the onset, this Court would like to address the validity of the second mortgage to Garcia and the sale of the subject property to Villar. We agree with the Court of Appeals that both are valid under the terms and conditions of the Deed of Real Estate Mortgage executed by Galas and Villar.

While it is true that the annotation of the first mortgage to Villar on Galas’s TCT contained a restriction on further encumbrances without the mortgagee’s prior consent, this restriction was nowhere to be found in the Deed of Real Estate Mortgage. As this Deed became the basis for the annotation on Galas’s title, its terms and conditions take precedence over the standard, stamped annotation placed on her title. If it were the intention of the parties to impose such restriction, they would have and should have stipulated such in the Deed of Real Estate Mortgage itself.

Neither did this Deed proscribe the sale or alienation of the subject property during the life of the mortgages. Garcia’s insistence that Villar should have judicially or extrajudicially foreclosed the mortgage to satisfy Galas’s

debt is misplaced. The Deed of Real Estate Mortgage merely provided for the options Villar may undertake in case Galas or Pingol fail to pay their loan. Nowhere was it stated in the Deed that Galas could not opt to sell the subject property to Villar, or to any other person. Such stipulation would have been void anyway, as it is not allowed under Article 2130 of the Civil Code, to wit:

Art. 2130. A stipulation forbidding the owner from alienating the immovable mortgaged shall be void.

Prohibition on pactum commissorium

Garcia claims that the stipulation appointing Villar, the mortgagee, as the mortgagor's attorney-in-fact, to sell the property in case of default in the payment of the loan, is in violation of the prohibition on pactum commissorium, as stated under Article 2088 of the Civil Code, viz:

Art. 2088. The creditor cannot appropriate the things given by way of pledge or mortgage, or dispose of them. Any stipulation to the contrary is null and void.

The power of attorney provision in the Deed of Real Estate Mortgage reads:

5. Power of Attorney of MORTGAGEE. – Effective upon the breach of any condition of this Mortgage, and in addition to the remedies herein stipulated, the MORTGAGEE is likewise appointed attorney-in-fact of the MORTGAGOR with full power and authority to take actual possession of the mortgaged properties, to sell, lease any of the mortgaged properties, to collect rents, to execute deeds of sale, lease, or agreement that may be deemed convenient, to make repairs or improvements on the mortgaged properties and to pay the same, and perform any other act which the MORTGAGEE may deem convenient for the proper administration of the mortgaged properties. The payment of any expenses advanced by the MORTGAGEE in connection with the purpose indicated herein is also secured by this Mortgage. Any amount received from the sale, disposal or administration abovementioned maybe applied by assessments and other incidental expenses and obligations and to the payment of original indebtedness including interest and penalties thereon. The power herein granted shall not be revoked during the life of this Mortgage and all acts which may be executed by the MORTGAGEE by virtue of said power are hereby ratified.[38]

The following are the elements of pactum commissorium:

- (1) There should be a property mortgaged by way of security for the payment of the principal obligation; and
- (2) There should be a stipulation for automatic appropriation by the creditor of the thing mortgaged in case of non-payment of the principal obligation within the stipulated period.[39]

Villar's purchase of the subject property did not violate the prohibition on pactum commissorium. The power of attorney provision above did not provide that the ownership over the subject property would automatically pass to Villar upon Galas's failure to pay the loan on time. What it granted was the mere appointment of Villar as attorney-in-fact, with authority to sell or otherwise dispose of the subject property, and to apply the proceeds to the payment of the loan.[40] This provision is customary in mortgage contracts, and is in conformity with Article 2087 of the Civil Code, which reads:

Art. 2087. It is also of the essence of these contracts that when the principal obligation becomes due, the things in which the pledge or mortgage consists may be alienated for the payment to the creditor.

Galas's decision to eventually sell the subject property to Villar for an additional P1,500,000.00 was well within the scope of her rights as the owner of the subject property. The subject property was transferred to Villar by virtue of another and separate contract, which is the Deed of Sale. Garcia never alleged that the transfer of the subject property to Villar was automatic upon Galas's failure to discharge her debt, or that the sale was simulated to cover up such automatic transfer.

Propriety of Garcia's action
for foreclosure of mortgage

The real nature of a mortgage is described in Article 2126 of the Civil Code, to wit:

Art. 2126. The mortgage directly and immediately subjects the property upon which it is imposed, whoever the possessor may be, to the fulfillment of the obligation for whose security it was constituted.

Simply put, a mortgage is a real right, which follows the property, even after subsequent transfers by the mortgagor. "A registered mortgage lien is considered inseparable from the property inasmuch as it is a right in rem." [41]

The sale or transfer of the mortgaged property cannot affect or release the mortgage; thus the purchaser or transferee is necessarily bound to acknowledge and respect the encumbrance. [42] In fact, under Article 2129 of the Civil Code, the mortgage on the property may still be foreclosed despite the transfer, viz:

Art. 2129. The creditor may claim from a third person in possession of the mortgaged property, the payment of the part of the credit secured by the property which said third person possesses, in terms and with the formalities which the law establishes.

While we agree with Garcia that since the second mortgage, of which he is the mortgagee, has not yet been discharged, we find that said mortgage subsists and is still enforceable. However, Villar, in buying the subject property with notice that it was mortgaged, only undertook to pay such mortgage or allow the subject property to be sold upon failure of the mortgage creditor to obtain payment from the principal debtor once the debt matures. Villar did not obligate herself to replace the debtor in the principal obligation, and could not do so in law without the creditor's consent. [43] Article 1293 of the Civil Code provides:

Art. 1293. Novation which consists in substituting a new debtor in the place of the original one, may be made even without the knowledge or against the will of the latter, but not without the consent of the creditor. Payment by the new debtor gives him the rights mentioned in articles 1236 and 1237.

Therefore, the obligation to pay the mortgage indebtedness remains with the original debtors Galas and Pingol. [44] The case of *E.C. McCullough & Co. v. Veloso and Serna* [45] is square on this point:

The effects of a transfer of a mortgaged property to a third person are well determined by the Civil Code. According to article 1879 [46] of this Code, the creditor may demand of the third person in possession of the property mortgaged payment of such part of the debt, as is secured by the property in his possession, in the manner and form established by the law. The Mortgage Law in force at the promulgation of the Civil Code and referred to in the latter, provided, among other things, that the debtor should not pay the debt upon its maturity after judicial or notarial demand, for payment has been made by the creditor upon him. (Art. 135 of the Mortgage Law of the Philippines of 1889.) According to this, the obligation of the new possessor to pay the debt originated only from the right of the creditor to demand payment of him, it being necessary that a demand for payment should have previously been made upon the debtor and the latter should have failed to pay. And even if these requirements were complied with, still the third possessor might abandon the property mortgaged, and in that case it is considered to be in the possession of the debtor. (Art. 136 of the same law.) This clearly shows that the spirit of the Civil Code is to let the obligation of the debtor to pay the debt stand although the property mortgaged to secure the payment of said debt may have been transferred to a third person. While the Mortgage Law of 1893 eliminated these provisions, it contained nothing indicating any change in the spirit of the law in this respect. Article 129 of this law, which provides the substitution of the debtor by the third person in possession of the property, for the purposes of the giving of notice, does not show this change and has reference to a case where the action is directed only against the property burdened with the mortgage. (Art. 168 of the Regulation.) [47]

This pronouncement was reiterated in *Rodriguez v. Reyes*[48] wherein this Court, even before quoting the same above portion in *E.C. McCullough & Co. v. Veloso and Serna*, held:

We find the stand of petitioners-appellants to be unmeritorious and untenable. The maxim “caveat emptor” applies only to execution sales, and this was not one such. The mere fact that the purchaser of an immovable has notice that the acquired realty is encumbered with a mortgage does not render him liable for the payment of the debt guaranteed by the mortgage, in the absence of stipulation or condition that he is to assume payment of the mortgage debt. The reason is plain: the mortgage is merely an encumbrance on the property, entitling the mortgagee to have the property foreclosed, i.e., sold, in case the principal obligor does not pay the mortgage debt, and apply the proceeds of the sale to the satisfaction of his credit. Mortgage is merely an accessory undertaking for the convenience and security of the mortgage creditor, and exists independently of the obligation to pay the debt secured by it. The mortgagee, if he is so minded, can waive the mortgage security and proceed to collect the principal debt by personal action against the original mortgagor.[49]

In view of the foregoing, Garcia has no cause of action against Villar in the absence of evidence to show that the second mortgage executed in favor of Garcia has been violated by his debtors, Galas and Pingol, i.e., specifically that Garcia has made a demand on said debtors for the payment of the obligation secured by the second mortgage and they have failed to pay.

WHEREFORE, this Court hereby AFFIRMS the February 27, 2003 Decision and March 8, 2003 Resolution of the Court of Appeals in CA-G.R. SP No. 72714.

SO ORDERED.

Bersamin, Del Castillo, Villarama, Jr., and Perlas-Bernabe,[**] JJ., concur.
Leonardo-De Castro,[*] (Acting Chairperson).

[*] Per Special Order No. 1226 dated May 30, 2012.

[**] Per Special Order No. 1227 dated May 30, 2012.

[1] 1997 RULES OF COURT, Rule 45.

[2] Rollo, pp. 9-17; penned by Associate Justice Marina L. Buzon with Associate Justices Josefina Guevara-Salonga and Danilo B. Pine, concurring.

[3] Id. at 23-24.

[4] Records, pp. 93-96.

[5] Id. at 9-10.

[6] Id. at 11-15.

[7] Id. at 16-17.

[8] Id. at 10 (dorsal side).

[9] Id. at 18-20.

[10] Id. at 19.

[11] Id. at 21.

- [12] *Id.* at 21 (dorsal side).
- [13] *Id.* at 3-8.
- [14] *Id.* at 31.
- [15] *Id.* at 72-73.
- [16] *Id.* at 31.
- [17] *Id.* at 38-41.
- [18] *Id.* at 61-63.
- [19] *Id.* at 65.
- [20] *Id.* at 66.
- [21] *Id.* at 67-68.
- [22] *Id.* at 75-80.
- [23] *Id.* at 84.
- [24] *Id.* at 85.
- [25] *Id.* at 81-83.
- [26] *Id.* at 95-96.
- [27] *Id.* at 94.
- [28] *Id.* at 95.
- [29] *Id.* at 98.
- [30] CA rollo, pp. 17-18.
- [31] *Id.* at 10-14.
- [32] *Id.* at 12-13.
- [33] Rollo, p. 17.
- [34] *Id.* at 14.
- [35] *Id.* at 17.
- [36] *Id.* at 18-21.
- [37] *Id.* at 99-102.
- [38] Records, pp. 13-14.
- [39] *Development Bank of the Philippines v. Court of Appeals*, 348 Phil. 15, 31 (1998).
- [40] *Id.* at 29.
- [41] *Philippine National Bank v. RBL Enterprises, Inc.*, G.R. No. 149569, May 28, 2004, 430 SCRA 299, 307.
- [42] *Ganzon v. Inserto*, 208 Phil. 630, 637 (1983).

[43] *Rodriguez v. Reyes*, 147 Phil. 176, 183 (1971).

[44] *Id.*

[45] 46 Phil. 1 (1924).

[46] NEW CIVIL CODE, now Art. 2129.

[47] *E.C. McCullough & Co. v. Veloso and Serena*, *supra* note 45 at 4-5.

[48] *Supra* note 43.

[49] *Id.* at 182-183.

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