

Title:

****Philippine National Bank vs. Court of Appeals and Spouses Maria Amor and Marciano Bascos****

Facts:

The Bascos couple obtained a loan of Php 15,000 from the Philippine National Bank (PNB) on June 4, 1979. The loan was secured by a real estate mortgage and was to be repaid within 365 days, with an interest rate of 12% per annum, which PNB could increase within legal limits. An extension converted the loan to a medium-term loan, and the interest rate escalated several times, culminating at 28% per annum by April 10, 1984.

The Bascos defaulted, leading to the scheduled extrajudicial foreclosure of the mortgage. The Bascos countered by suing PNB, alleging the illegality of the interest rate increases under various legal grounds. They sought to enjoin the auction and nullify the interest rate hikes. They also made partial payments towards their loan.

The Regional Trial Court (RTC) ruled in favor of the Bascos, declaring the interest rate increases null and void and capping the rate at 12%. PNB appealed, but the Court of Appeals affirmed the RTC's decision, which led to PNB's petition for review with the Supreme Court.

Issues:

1. The legality of unilateral interest rate increases by PNB under the promissory note and mortgage agreement.
2. The validity of an escalation clause without a corresponding de-escalation clause.
3. The interpretation of contracts of adhesion in favor of the non-drafting party.

Court's Decision:

The Supreme Court affirmed the Court of Appeals' decision. It held that:

- Unilateral interest rate increases by PNB were invalid as they violated the principle of mutuality of contracts. Any change in the interest rate must be consensual.
- An escalation clause must be accompanied by a de-escalation clause to avoid being deemed as one-sided and unreasonable.
- Contracts of adhesion are to be interpreted against the party who drafted them, especially when such contracts place the other party at a disadvantage.

Doctrine:

The court established that escalation clauses in loan agreements must be accompanied by

corresponding de-escalation clauses to ensure the contract's mutuality, fairness, and reasonableness. Furthermore, any changes to the interest rate based on such clauses require the agreement of both parties.

Class Notes:

- Principle of Mutuality: A contract must bind both parties equally; its validity cannot depend solely on the will of one of the parties.
- Escalation and De-escalation Clauses: Loan agreements that allow for the adjustment of interest rates must include both escalation and de-escalation clauses to ensure fairness and mutuality.
- Contracts of Adhesion: Such contracts, typically drafted by one party without negotiation, must be interpreted in favor of the party that did not draft the contract.

Historical Background:

This case reflects the judiciary's stance on protecting borrowers from potentially exploitative lending practices and the importance of contract fairness. It underscores the balance between banks' rights to adjust loan terms based on market conditions and borrowers' protection against unilateral and disadvantageous changes.