

REAL ESTATE MORTGAGE

Articles 2124 – 2131

I. Concept (characteristics)

A. As a right

- It is a real right over immovables constituted by the owner to guarantee an obligation which if not paid is to be satisfied from the proceeds of the sale of such property.

B. As a contract

- It is a contract whereby the debtor guarantees the performance of a principal obligation subjecting as security therefor real properties or real rights in case such obligation is not complied with, within the time stipulated.
- It is a real, accessory and subsidiary contract
- It is likewise unilateral: only on the part of the creditor who must first free the property from the encumbrance once the obligation is fulfilled

II. Elements

A. Parties

- a.** The mortgagor (who need not be the principal debtor) must have free disposal and be the absolute owner of the security; otherwise he must be properly authorized.
 1. Where a mortgage is a nullity, having been executed by an unauthorized person, registration under the Land Registration Act will not validate it (how bout the mortgagee in good faith doctrine bullshit chuva? I think depende ra sa situation and sa parties involved on the fucking degree of diligence required. Alien? ALIEN!)
- b.** The mortgagee must have capacity to contract.

Note: As a general rule, mortgagor retains possession because debtor merely subjects the property to a lien but ownership is not parted with. However, compliance with such rule is not an essential requisite of the contract

It is not also an essential requisite of the contract of mortgage that the principal of the mortgage credit bears interest, or that the interest as compensation for the use of the principal enjoyment of its fruits be in the form of a certain percent thereof.

- c.** Registration of mortgage to the registry of deeds (look at discussion in form)

B. Object – which may only be: (Art. 2124)

- a.** Immovables
- b.** Alienable real rights imposed upon immovables in accordance with the law (real property)

Right of possession can be mortgaged

Note: a building by itself may be mortgaged apart from the land on which it is built

A mortgage may secure future obligation, BUT a future property cannot be object of a contract of mortgage. A mortgagor could not legally mortgage any property he did not yet own. However, a stipulation subjecting to the mortgage lien, properties (improvements) which the mortgagor may subsequently acquire, install, or use in connection with real property already mortgaged belonging to the mortgagor is valid.

- C.** Consideration – same as of the principal contract, without which it cannot exist as an independent contract
- Valid if the principal obligation is valid, and cannot be avoided on the ground of lack of consideration

Note: mortgage must sufficiently describe the debt sought to be secured

Case: PNB vs. RDA Ent.

- there was lack of consideration but mortgage deal was already executed (before application, mortgage deal was already signed)
 - 50T was released by the bank but the mortgage was for 100T
 - Q: is the mortgage valid?
- A: Valid but unenforceable to the extent of the failure of consideration. During the foreclosure sale, you can only sell 50% of the property

D. Form –

- a.** for validity (Art. 2125)
CUYCO VS CUYCO

Facts: Petitioners, spouses Adelina and Feliciano Cuyco, obtained a loan in the amount of P1,500,000.00 from respondents, spouses Renato and Filipina Cuyco, payable within one year at 18% interest per annum, and secured by a Real Estate Mortgage. Subsequently, petitioners obtained additional loans from the respondents in the aggregate amount of P1,250,000.00, broken down as follows: (1) P150,000.00 on May 30, 1992; (2) P150,000.00 on July 1, 1992; (3) P500,000.00 on September 5, 1992; (4) P200,000.00 on October 29, 1992; and (5) P250,000.00 on January 13, 1993.

Petitioners made payments amounting to P291,700.00, but failed to settle their outstanding loan obligations. Respondents filed a case against petitioner, they alleged that petitioners' loans were secured by the real estate mortgage; that as of August 31, 1997, their indebtedness amounted to P6,967,241.14, inclusive of the 18% interest compounded monthly; and that petitioners' refusal to settle the same entitles the respondents to foreclose the real estate mortgage.

The RTC rendered judgment in favor of the respondents. Petitioners appealed to the CA reiterating their previous claim that only the amount of P1,500,000.00 was secured by the real estate mortgage.

CA held that by express intention of the parties, the real estate mortgage secured the original P1,500,000.00 loan and the subsequent loans of P150,000.00 and P500,000.00 obtained on July 1, 1992 and September 5, 1992, respectively. As regards the loans obtained on May 31, 1992, October 29, 1992 and January 13, 1993 in the amounts of P150,000.00, P200,000.00 and P250,000.00, respectively, the appellate tribunal held that the parties never intended the same to be secured by the real estate mortgage.

Issue: WON the mortgage contract contains blanket mortgage clause.

Held: No. While a real estate mortgage may exceptionally secure future loans or advancements, these future debts must be sufficiently described in the mortgage contract. An obligation is not secured by a mortgage unless it comes fairly within the terms of the mortgage contract. A "dragnet clause" operates as a convenience and accommodation to the borrowers as it makes available additional funds without their having to execute additional security documents, thereby saving time, travel, loan closing costs, costs of extra legal services, recording fees, et cetera.

There is no stipulation that the mortgaged realty shall also secure future loans and advancements. Even if the parties intended the additional loans of P150,000.00 obtained on May 30, 1992, P150,000.00 obtained on July 1, 1992, and P500,00.00 obtained on September 5, 1992 to be secured by the same real estate mortgage, as shown in the acknowledgement receipts, it is not sufficient in law to bind the realty for it was not made substantially in the form prescribed by law.

b. Between the parties –

- 1.** Under the Real Estate (Spanish Sardines) Mortgage Law – To be legally created in a valid manner it is necessary that the mortgage be constituted by a public instrument.
- 2.** Under the Land Registration Act – Mortgages whether registered or unregistered shall be sufficient in law and shall be effective to encumber lands provided that every such instrument shall be signed by the person executing the same, in the presence of two witnesses, and shall be acknowledged to be his free act and deed before the judge of a

court of record or clerk of a court of record or a notary public or a justice of peace who shall certify to such acknowledgement (Sec. 127, Act No. 496) (check PD 1529)

Note: a duly executed mortgage is presumed to be valid until the contrary is shown. To the party attacking, rests the burden of proving its invalidity due to fraud, duress or illegality

Q: in what for should a mortgage be to be valid?

A: it should be recorded in the Registry of property (in order to bind 3rd person). Thus, unrecorded mortgage is binding between parties.

Remember: if a mortgagor was not duly authorized to enter into such contract but said contract was registered, the recording will not give it any validity because from the very start, the contract is not valid.

Note: once a mortgage has been signed in due form, the mortgagee is entitled to its registration as a matter of right. Registration then is a mere ministerial act. It must follow as a necessary consequence that registration must first be allowed and its validity or effect litigated afterwards.

Effect of Unregistered Mortgage Between the Parties

Mobil Oil Phil. Inc. vs Diocares
29 SCRA 656, Sept. 30, 1969

Facts:

Plaintiff MOBIL extended a P45,000 loan to defendant Diocares payable in monthly installments and secured by a first mortgage on 2 parcels of land. The defendant also agreed to buy from the plaintiff their petroleum requirements in an amount not less than 50,000 liters per month. It was further agreed that in case of defendant's failure to pay any installment due and purchase a minimum of 50,000 liters per month of petroleum, the plaintiff has the right to foreclose the mortgage or recover payment of the entire obligation. The defendant paid only P1,901 and failed to buy on cash basis the agreed minimum amount of petroleum.

Plaintiff filed an action for payment of the balance of the debt and in default of such payment, mortgaged property be sold and proceeds applied to defendant's obligation. The lower court ordered the defendant to pay the plaintiff said obligation but did not order foreclosure of the mortgage upon the ground that it does not appear from the copy of the loan and real estate mortgage that said mortgage had been registered and therefore, the loan agreement although binding among the parties merely created a personal obligation but did not establish a real estate mortgage. Plaintiff appealed.

Issue:

Whether or not a real estate mortgage was created.

SC Ruling:

Art. 2125 of the New Civil Code provides: "In addition to the requisites stated in article 2085, it is indispensable, in order that a mortgage may be validly constituted, that the document in which it appears be recorded in the Registry of Property. *If the instrument is not recorded, the mortgage is nevertheless binding between the parties.*"

The lower court regarded the categorical nature of "it is indispensable" but ignored the succeeding sentence "the mortgage is nevertheless binding upon the parties." The law is clear. The Mortgage subsists. As between the parties, the mere fact that there is as yet no compliance with the requirement that it be recorded cannot be a bar to foreclosure. No interpretation of the law is needed, only its application.

In the language of the Report of the Code commission: "in Art. 2125 an additional provision is made that if the instrument of mortgage is not recorded, the mortgage is nevertheless binding between the parties." This is indicative of the legislative intent.

Moreover, equity so demands and justice is served. There is thus a full acknowledgement of the binding effect of a promise, which must be lived up to. It could be said that to allow foreclosure in the absence of such a formality is to offend against the demands of jural symmetry. What is indispensable may be dispensed with. Such an objection is far from fatal. This would not be the first time when logic yields to what is fair and what is just. To such an overmastering requirement, law is not immune.

Order affirmed with modifications.

- c. As to strangers(third person) – the document in which the mortgage appears must be recorded in the Registry of Property of the province where the land is located.

Validity of Private Document evidencing mortgage

Hechanova vs. Adil
GR L49940, Sept. 25, 1986

Facts:

The case under review is for the annulment of a deed of sale dated March 11, 1978, executed by defendant Jose Y. Servando in favor of his co-defendants, the petitioners herein, covering three parcels of land situated in Iloilo City. Claiming that the said parcels of land were mortgaged to him in 1970 by the vendor, who is his cousin, to secure a loan of P20,000.00, the plaintiff Pio Servando impugned the validity of the sale as being fraudulent, and prayed that it be declared null and void and the transfer certificates of title issued to the vendees be cancelled, or alternatively, if the sale is not annulled, to order the defendant Jose Servando to pay the amount of P20,000.00, plus interests, and to order defendants to pay damages. Attached to the complaint was a copy of the private document evidencing the alleged mortgage (Annex A), which is quoted hereunder:

August 20, 1970

This is to certify that I, Jose Yusay Servando, the sole owner of three parcel of land under Tax Declaration No. 28905, 44123 and 31591 at Lot No. 1, 1863-Portion of 1863 & 1860 situated at Sto. Nino St., Arevalo, Compania St. & Compania St., Interior Molo, respectively, have this date mortgaged the said property to my cousin Pio Servando, in the amount of TWENTY THOUSAND

PESOS (P20,000.00), redeemable for a period not exceeding ten (10) years, the mortgage amount bearing an interest of 10% per annum.

I further certify that in case I fail to redeem the said properties within the period stated above, my cousin Pio Servando, shall become the sole owner thereof.

(SGD.) JOSE YUSAY SERVANDO

WITNESSES:

(Sgd) Ernesto G. Jeruta

(Sgd) Francisco B. Villanueva

SC Ruling:

It is clear from the records of this case that the plaintiff has no cause of action. Plaintiff has no standing to question the validity of the deed of sale executed by the deceased defendant Jose Servando in favor of his co-defendants Hechanova and Masa. No valid mortgage has been constituted plaintiff's favor, the alleged deed of mortgage being a mere private document and not registered; moreover, it contains a stipulation (pacto comisorio) which is null and void under Article 2088 of the Civil Code. Even assuming that the property was validly mortgaged to the plaintiff, his recourse was to foreclose the mortgage, not to seek annulment of the sale.

The complaint filed by plaintiff dated February 4, 1978 is hereby dismissed.

- A.** Supplementary law – the Real Estate Mortgage Law of 1889 (Ley Hipotecaria de Filipinas) and the Land Registration Act (Act. No. 496), and also the Property Registration Decree (PD 1529)

Doctrine of Mortgagee in Good Faith

- A mortgagee has a right to rely in good faith on the certificate of title of the mortgagor of the property given as security and in the absence of any sign that might arouse suspicion, has no obligation to undertake further investigation
- This doctrine presupposes, however, that the mortgagor, who is not the rightful owner of the property, has already succeeded in obtaining a Torrens title over the property in his name and that, after obtaining the said title, he succeeds in mortgaging the property to another who relies on what appears on the said title
- Exception to the rule as where the purchaser or mortgagee has knowledge of a defect or lack of title in the vendor, or the mortgagee does not directly deal with the registered owner of the property
- Another exception: greater care and diligence required of mortgagee-bank or others in the business of lending money

Registration of Mortgage: (which are preferred?)

- A registered mortgage right over property previously sold is INFERIOR to the buyer's unregistered right. The unrecorded sale is preferred for the reason that if the original owner (seller) had parted with his ownership of the thing sold then he no longer had ownership and free disposal of the thing so as to be able to mortgage it

- A registered mortgage, however, is SUPERIOR to a contract to sell, subject to any liabilities of the buyer (vendor, mortgagor) may have incurred in favor of the buyer. In a contract to sell, title is retained by the vendor until full payment of the price
- A prior registration of a lien creates a preference; hence the subsequent annotation of an adverse claim cannot defeat the rights of the mortgagee or the purchaser at the auction sale whose rights were derived from a prior mortgage validly registered.

III. Classes

- A.** Voluntary – one which is agreed to between the parties or constituted by the will of the owner of the property on which it is created. (Contractual Mortgage)
- B.** Legal – one required by law to be executed in favor of certain persons.
- C.** Equitable Mortgage – one which, although it lacks the proper formalities of a mortgage required by law nevertheless shows the intention of the parties to burden the property as a security for a debt. --- (pacto de retro sale)

IV. Effects

A. As to the property mortgaged

a. Creation of real right (Article 2126)

- A registered mortgage creates right in rem, a real right, a lien inseparable from the property mortgaged, which is enforceable against the whole world, affording specific security for the satisfaction of a debt. The personality of the owner is disregarded. Until discharged upon payment of the obligation, it follows the property wherever it goes and subsists notwithstanding changes of ownership.

Cancellation of mortgage in lieu of surety bond (Q: can a mortgagor compel the mortgagee to accept in lieu of the mortgage of the security bond?)

A: Case: Ganzon vs Inserto

- Mortgagor cannot compel because mortgage has of greater value than that of a surety.
- Applying the principles underlying the nature of a mortgage, the real estate mortgage can not be substituted by a surety bond as ordered by the trial court. The mortgage lien in favor of Petitioner Rodolfo Ganzon is inseparable from the mortgaged property. It is a right in rem, a lien on the property. To substitute the mortgage with a surety bond would convert such lien from a right in rem, to a right in personam. This conversion cannot be ordered for it would abridge the rights of the mortgagee under the mortgage contract.

Effect of sale of mortgaged property

Note: a mortgage is merely a security for a debt, an encumbrance upon the property and does not extinguish the title of the debtor who does not lose his principal attribute as owner, that is, the right to dispose. Indeed, the law considers void any stipulation forbidding the owner from alienating the immovable mortgaged.

What is divested from the mortgagor is only his full right as owner thereof to dispose of and sell the property, that is, the mortgagor does not have the unconditional power to absolutely sell the property since the same is encumbered by a lien of a third person.

Bonnevie vs. CA

G.R. No. L-49101 October 24, 1983

Facts:

It is not disputed that spouses Lozano were the owners of the property which they mortgaged on December 6, 1966, to secure the payment of the loan of P75,000.00 they were about to obtain from defendant Philippine Bank of Commerce; that on December 8, 1966, they executed in favor of plaintiff Honesto Bonnevie the Deed of Sale with Assumption of Mortgage, for an in consideration of the sum of P100,000.00, P25,000 of which amount being payable to the Lozano spouses upon the execution of the document, and the balance of P75,000 being payable to defendant bank.

Defendant applied for the foreclosure of the mortgage. Petitioners sought the annulment of the Deed of Mortgage and alleged among others that the mortgage was executed by one who was not the owner of the mortgaged property.

Issue:

Whether the real estate mortgage executed by the spouses Lozano in favor of respondent bank was validly and legally executed.

SC Ruling:

YES. Petitioners admit that they did not secure the consent of respondent Bank to the sale with assumption of mortgage. Coupled with the fact that the sale/assignment was not registered so that the title remained in the name of the Lozano spouses, insofar as respondent Bank was concerned, the Lozano spouses could rightfully and validly mortgage the property. Respondent bank had every right to rely on the certificate of title. It was not bound to go behind the same to look for flaws in the mortgagor's title, the doctrine of innocent purchaser for value being applicable to an innocent purchaser for value.

A mortgage follows the property whoever the possessor may be and subjects the fulfillment of the obligation for whose security it was constituted.

RIGHT TO FORECLOSE WHEN LAND WAS SOLD AFTER THE MORTGAGE

Paderes vs. CA

G.R. No. 147074; July 15, 2005

Facts:

On September 1982, Manila International Construction Corporation (MICC) executed a real estate mortgage over 21 registered parcels of land including the improvements thereon in favor of Banco Filipino in order to secure a loan of P1,885,000.00. The 21 mortgaged properties included two lots, which was subsequently sold by MICC on August 1983 to petitioners. Neither sale was registered, however.

For failure of MICC to settle its obligations, Banco Filipino filed a verified petition for the extra-judicial foreclosure of MICC's mortgage. Thereafter, a writ of possession was issued ordering the petitioners to vacate the premises within 7 days from receipt thereof.

Petitioners argued that having purchased their respective properties in good faith from MICC, they are third parties whose right thereto are superior to that of Banco Filipino; they are still entitled to redeem the properties and in fact a binding agreement between them and the bank had been reached; their respective houses should not have been included in the auction sale of the mortgaged properties.

Held:

Petitioners position clashes with precepts well-entrenched in law. By Article 2126 of the Civil Code, a "mortgage directly and immediately subjects the property on which it is imposed, whoever the possessor may be, to the fulfillment of the obligation for whose security it was constituted." Sale or transfer cannot affect or release the mortgage.

A purchaser is necessarily bound to acknowledge and respect the encumbrance to which is subjected the purchased thing and which is at the disposal of the creditor "in order that he, under the terms of the contract, may recover the amount of his credit therefrom." For, a recorded real estate mortgage is a right *in rem*, a lien on the property whoever its owner may be. Because the personality of the owner is disregarded; the mortgage subsists notwithstanding changes of ownership; the last transferee is just as much of a debtor as the first one; and this, independent of whether the transferee knows or not the person of the mortgagee. So it is, that a mortgage lien is *inseparable* from the property mortgaged. All subsequent purchasers thereof must respect the mortgage, whether the transfer to them be *with or without the consent of the mortgagee.* For, the mortgage, until discharge, follows the property

Example Situation: READ PAGE 387 OF BOOK (ILLUSTRATIVE CASE) --- VERY IMPORTANT TO UNDERSTAND

Effect of death of mortgagor

Jacob vs. CA

184 SCRA 294; April 6, 1990

Facts:

Petitioner contends that the extrajudicial foreclosure proceedings and the sale of the property mortgaged under the amended real estate mortgage after the mortgagor died are null and void. It is pointed out that Dr. Jacob died on March 9, 1979 and that the extrajudicial foreclosure proceedings

were effected after his death, that is, the public auction sale was made on May 11, 1979. Petitioner argues that such extrajudicial foreclosure can only be prosecuted during the lifetime of Dr. Jacob for the reason that such kind of foreclosure under Act No. 3135, as amended, is authorized only because of the special power of attorney inserted in the mortgage deed; and that said special power of attorney cannot extend beyond the lifetime of the supposed mortgagor.

Issue:

Whether or not an extrajudicial foreclosure of a mortgage may proceed even after the death of the mortgagor.

SC Ruling:

YES. The power to foreclose a mortgage is not an ordinary agency that contemplated exclusively the representation of the principal by the agent but is primarily an authority conferred upon the mortgagee for the latter's own protection. That power survives the death of the mortgagor. The right of the mortgagee bank to extrajudicially foreclose the mortgage after the death of the mortgagor, acting through his attorney-in-fact, did not depend on the authority in the deed of mortgage executed by the latter.

b. Extension to accessions and accessories (Article 2127)

- GR: A real estate mortgage constituted on immovable property is not limited to the property itself but also extends to all its accessions, improvements, growing fruits and rents or income as well as to the proceeds of insurance should the property be destroyed, or the expropriation value of the property should it be expropriated.
- EXC: Unless there is an express stipulation to the effect of excluding them.

Effect of mortgage of hacienda/where mortgagee transferred his credit:

Bischoff vs. Pomar

12 Phil 690; February 2, 1909

Facts:

In July 1900, Lazaro Mota loaned to Romana Ganzon P11, 209 payable in 2 years and secured by a mortgage consisting of hacienda San Jose. Additional loans were granted with further stipulations that in case of debtor's failure to pay the creditor, the mortgaged hacienda would be disposed of at public auction to satisfy the said indebtedness. This last instrument was entered in the registry of property.

In September 1902, Ganzon sold to plaintiff Bischoff the machineries and tramway in the hacienda under a pacto de retro. In September 1904, Mota transferred said credit to defendant Cia. General de Tabaco. Ganzon executed a mortgage in favor of Cia. General de Tabaco on the hacienda as security

for the loan of P53, 042. In 1905, the receiver of Ganzon took possession of said properties. The plaintiff filed a complaint praying for the delivery of the machineries and tramway sold to him. The trial court decided for the defendant but with plaintiff having a reserved right against Ganzon for the sum paid for said properties.

Issue:

Whether or not the machineries and tramway are included in the mortgage.

SC Ruling:

In the instruments of mortgage, executed prior to the sale to the plaintiff with pacto de retro, the improvements already mounted appear as expressly mortgaged at the time of executing the first mortgage in 1902 and later on to the transfer of credit to Cia general de tabaco in 1904. From none of said instruments does it appear that the contracting parties had expressly agreed to exclude the said machineries and tramway from the repeated mortgages of said hacienda.

It is a rule that in a mortgage of real estate, the improvements on the same are included; therefore, all objects permanently attached to a mortgaged building or land, although they may have been placed there after the mortgage was constituted, are also included.

Assuming that the owner of a mortgaged property is entitled to dispose of the same, such disposal however, does not release it from the mortgage with which it is encumbered, inasmuch as the right of the creditor curtails that of the said owner of the mortgaged property, and the purchaser is necessarily bound to acknowledge and respect the encumbrances which is at the disposition of the creditor in order that under the terms of the contract, he may recover his credit from the value thereof.

Bischoff can not acquire any right to indemnity for loss or damages, for the reason that he purchased goods that were already liable to the mortgage. The sale was effected long after the property was mortgaged. He therefore did not obtain possession of the same.

Effect of mortgage of lots on house built thereon

Paderes vs. CA

G.R. No. 147074; July 15, 2005

Facts:

On September 1982, Manila International Construction Corporation (MICC) executed a real estate mortgage over 21 registered parcels of land including the improvements thereon in favor of Banco Filipino in order to secure a loan of P1,885,000.00. The 21 mortgaged properties included two lots, which was subsequently sold by MICC on August 1983 to petitioners. Neither sale was registered, however.

For failure of MICC to settle its obligations, Banco Filipino filed a verified petition for the extra-judicial foreclosure of MICC's mortgage. Thereafter, a writ of possession was issued ordering the petitioners to vacate the premises within 7 days from receipt thereof.

Petitioners argued that having purchased their respective properties in good faith from MICC, they are third parties whose right thereto are superior to that of Banco Filipino; they are still entitled to redeem the properties and in fact a binding agreement between them and the bank had been

reached; their respective houses should not have been included in the auction sale of the mortgaged properties.

Held:

Petitioners position clashes with precepts well-entrenched in law. By Article 2126 of the Civil Code, a "mortgage directly and immediately subjects the property on which it is imposed, whoever the possessor may be, to the fulfillment of the obligation for whose security it was constituted." Sale or transfer cannot affect or release the mortgage.

A purchaser is necessarily bound to acknowledge and respect the encumbrance to which is subjected the purchased thing and which is at the disposal of the creditor "in order that he, under the terms of the contract, may recover the amount of his credit therefrom." For, a recorded real estate mortgage is a right *in rem*, a lien on the property whoever its owner may be. Because the personality of the owner is disregarded; the mortgage subsists notwithstanding changes of ownership; the last transferee is just as much of a debtor as the first one; and this, independent of whether the transferee knows or not the person of the mortgagee. So it is, that a mortgage lien is *inseparable* from the property mortgaged. All subsequent purchasers thereof must respect the mortgage, whether the transfer to them be *with or without the consent of the mortgagee*. For, the mortgage, until discharge, *follows the property*

Note: when a mortgage is *made to include new or future improvements on registered land, said lien attaches and vests not at the time said improvements are constructed but on the date of the recording and registration of the deed of mortgage.*

A Mortgage with "DRAGNET" clauses to secure future advancements (subsume all debts of past or future origin) is valid and binding between the parties. The purpose of such clause is that it enables the parties to provide continuous dealings, the nature or extent of which may not be known or anticipated at the time, and they avoid the expense and inconvenience of executing a new security on each new transaction.

c. Pactum de non alienando

- Stipulations forbidding the owner from alienating the immovable are void. (Article 2130)
- The mortgaged can simply withhold his consent thereby prevent the mortgagor from selling the property. This creates an unconscionable advantage for the mortgagee and amounts to a virtual prohibition on the owner to sell his mortgaged property.

SERVICEWIDE SPECIALIST INC. VS CA

Facts:

Respondent spouses Ponce bought on installment a Holden Torana vehicle from C. R. Tecson Enterprises. They executed a promissory note and a chattel mortgage on the vehicle dated December 24, 1975 in favor of the latter to secure payment of the note. The mortgage was registered both in the Registry of Deeds and the Land Transportation Office. On the same date, C.R. Tecson Enterprises, in turn, executed a deed of assignment of said promissory note and chattel

mortgage in favor of Filinvest Credit Corporation with the conformity of respondent spouses. The latter were aware of the endorsement of the note and the mortgage to Filinvest as they in fact availed of its financing services to pay for the car.

Respondent spouses transferred and delivered the vehicle to Conrado R. Tecson by way of sale with assumption of mortgage. Subsequently, in 1978, Filinvest assigned all its rights and interest over the same promissory note and chattel mortgage to petitioner Servicewide Specialists Inc. without notice to respondent spouses. Due to the failure of respondent spouses to pay the installments under the promissory note, petitioner filed before in the RTC a complaint for *replevin*. In their answer, respondent spouses denied any liability claiming they had already returned the car to Conrado Tecson pursuant to the Deed of Sale with Assumption of Mortgage.

Ruling:

In the case at bar, what is relevant is not the assignment of credit between petitioner and its assignor, but the knowledge or consent of the creditor's assignee to the debtor-mortgagor's sale of the property to another.

When the credit was assigned to petitioner, only notice to but not the consent of the debtor-mortgagor was necessary to bind the latter. Applying Article 1627 of the Civil Code,^[3] the assignment made to petitioner includes the accessory rights such as the mortgage. Article 2141, on the other hand, states that the provisions concerning a contract of pledge shall be applicable to a chattel mortgage, such as the one at bar. As provided in Article 2096 in relation to Article 2141 of the Civil Code,^[4] a thing pledged may be alienated by the pledgor or owner "with the consent of the pledgee."

In any case, applying by analogy Article 2128 of the Civil Code^[2] to a chattel mortgage, it appears that a mortgage credit may be alienated or assigned to a third person. Since the assignee of the credit steps into the shoes of the creditor-mortgagee to whom the chattel was mortgaged, it follows that the assignee's consent is necessary in order to bind him of the alienation of the mortgaged thing by the debtor-mortgagor.

In this case, *however*, since the alienation by the respondent spouses of the vehicle occurred prior to the assignment of credit to petitioner, it follows that the former were not bound to obtain the consent of the latter as it was not yet an assignee of the credit at the time of the alienation of the mortgaged vehicle.

When Tecson Enterprises assigned the promissory note and the chattel mortgage to Filinvest, it was made with respondent spouses' tacit approval. When Filinvest in turn, as assignee, assigned it further to petitioner, the latter should have notified the respondent spouses of the assignment in order to bind them. This, they failed to do.

One thing, however, that militates against the posture of respondent spouses is that although they are not bound to obtain the consent of the petitioner before alienating the property, they should have obtained the consent of Filinvest since they were already aware of the assignment to the latter.

Therefore, for failure of respondent spouses to obtain the consent of Filinvest thereto, the sale of the vehicle to Conrado R. Tecson was not binding on the former. When the credit was assigned by Filinvest to petitioner, respondent spouses stood on record as the debtor-mortgagor.

Respondents Jesus Ponce and Elizabeth Ponce are ORDERED to pay petitioner, jointly and severally and the third party defendant Tecson is ordered to reimburse respondents Ponce.

GO CINCO VS CA

Petitioner Manuel Cinco (*Manuel*) obtained a commercial loan in the amount of P700,000.00 from respondent Maasin Traders Lending Corporation (*MTLC*). The loan was evidenced by a promissory note and secured by a real estate mortgage executed on December 15, 1987 over the spouses Go Cinco's land and 4-storey building located in Maasin, Southern Leyte. To be able to pay the loan in favor of MTLC, the spouses Go Cinco applied for a loan with the Philippine National Bank, Maasin Branch and offered as collateral the same properties they previously mortgaged to MTLC. The PNB approved the loan application, however, was conditioned on the cancellation of the mortgage in favor of MTLC.

Manuel executed a Special Power of Attorney (*SPA*) authorizing Ester to collect the proceeds of his PNB loan but they required Ester to first sign a deed of release/cancellation of mortgage before they could release the proceeds of the loan to her. Outraged that the spouses Go Cinco used the same properties mortgaged to MTLC as collateral for the PNB loan, Ester refused to sign the deed and did not collect the P1.3 Million loan proceeds.

Ester instituted foreclosure proceedings against the spouses Go Cinco. The spouses Go Cinco alleged that foreclosure of the mortgage was no longer proper as there had already been settlement of Manuel's obligation in favor of MTLC. They claimed that the assignment of the proceeds of the PNB loan amounted to the payment of the MTLC loan.

ISSUE: *WON the loan due the MTLC had been extinguished.*

WON respondent's contention that as a prior mortgagee the spouses Go Cinco should have obtained her consent before offering the properties already mortgaged to her as security for the PNB loan is correct.

RULING:

a) *No.*

Article 1233 of the Civil Code states that "a debt shall not be understood to have been paid unless the thing or service in which the obligation consists has been completely delivered or rendered, as the case may be". In contracts of loan, the debtor is expected to deliver the sum of money due the creditor. In the present case, Manuel sought to pay Ester by authorizing her, through an SPA, to collect the proceeds of the PNB loan — an act that would have led to payment if Ester had collected the loan proceeds as authorized. Admittedly, the delivery of the SPA was not, strictly speaking, a delivery of the sum of money due to MTLC, and Ester could not be compelled to accept it as payment based on Article 1233. Had Ester presented the SPA to the bank and signed the deed of release/cancellation of mortgage, the delivery of the sum of money would have been effected and

the obligation extinguished. As the records show, Ester refused to collect and allow the cancellation of the mortgage.

b) Incorrect.

There is nothing legally objectionable in a mortgagor's act of taking a second or subsequent mortgage on a property already mortgaged; a subsequent mortgage is recognized as valid by law and by commercial practice, subject to the prior rights of previous mortgages. Under Article 2130 of the Civil Code, a stipulation forbidding the owner from alienating the immovable mortgaged is considered void. Ester, therefore, could not validly require the spouses Go Cinco to first obtain her consent to the PNB loan and mortgage. Besides, with the payment of the MTLC loan using the proceeds of the PNB loan, the mortgage in favor of the MTLC would have naturally been cancelled.

No reason exists under this legal situation why we cannot compel MTLC and Ester: (1) to release the mortgage to MTLC as a condition to the release of the proceeds of the PNB loan, upon PNB's acknowledgment that the proceeds of the loan are ready and shall forthwith be released; and (2) to accept the proceeds, *sufficient to cover the total amount of the loan to MTLC*, as payment for Manuel's loan with MTLC.

Note: there is nothing wrong in a stipulation granting the mortgagee the right of first refusal over the mortgaged property in the even the mortgagor decides to sell the same. The consideration for the loan-mortgage may be said to include the consideration for the right of first refusal. A sale made in violation of the mortgagee's contractual right of first refusal is rescissible.

B. Effects as to the Mortgagee

- The mortgage credit may be alienated or assigned to a third person, in whole or in part, with the formalities required by law. (Article 2128)
- A "mortgagee in possession" is subject to the rules of antichresis in that he assumes the obligations of an antichretic creditor.
- Since the mortgage credit is a real right such right may be alienated or assigned to a third person, in whole or in part, by the mortgagee who is the owner of said right and assignee may foreclose the mortgage in case of nonpayment of the mortgage indebtedness

Q: Does mortgagee need the consent of mortgagor?

A: No. Mortgagee only needs to notify the mortgagor who the transferee is in case the debtor opts to pay. Informing the mortgagor is not the obligation of the transferee.

Note: the alienation or assignment is valid even if it is not registered. Registration is necessary only to affect third persons.

Where mortgagee transferred his credit: Please refer to the case of Bischoff vs. Pomar

Article 2129

- The fact that the mortgagor has transferred the mortgaged property to a third person does not relieve him from his obligation to pay the debt to the mortgage creditor in the absence of novation.
- The mortgage credit being a real right which follows the property, the creditor may demand from any possessor the payment only of the part of the credit secured by said property.
- The spirit of this law is to let the obligation of the debtor to pay the debt to stand although the property mortgaged to secure the payment of said debt may have been transferred to a third person.

Situation:

Q: if A mortgage his property to B and was registered on 6/30/11 but then executes another to C which was registered on 5/1/11, what are the rights of B and C?

A: The right of C is to redeem first the mortgage before he can foreclose. (Subject to the prior right of the 1st mortgagee). So in foreclosure: satisfy B first. If there is something left, you satisfy C.

V. Foreclosure – Modes

Foreclosure – is the remedy available to the mortgagee by which he subjects the mortgaged property to the satisfaction of the obligation to secure which the mortgage was given

- It is the necessary consequence of non-payment of a mortgage indebtedness.
- The right of foreclosure cannot be exercised by any person other than the creditor-mortgagee or his assigns.
- Foreclosure must be limited to the amount mentioned in the mortgage document
- As a GR, a demand before foreclosure is essential

Note: once the proceeds have been applied to the payment of the obligation, the debtor cannot anymore be required to pay, unless, of course, there is a deficiency between the amount of the loan and the foreclosure sale price, because the obligation has already been extinguished.

Foreclosure proceedings are presumed to be REGULAR.

2 KINDS OF FORECLOSURE

- The two kinds must be distinguished from an ordinary execution sale which is governed by rule 39 of the rules of court

A. Judicial

- By ordinary action by the mortgagee

- Bring an action for that purpose, in the proper court which has jurisdiction over the area wherein the real property involved or a portion thereof, is situated
- A proceeding for judicial foreclosure of mortgage is an action QUASI IN REM --- it is based on a personal claim against a specific property of the defendant
- An action for foreclosure of a mortgage is an action which survives the death of the mortgagor because the claim against him is not a pure money claim but an action to enforce a mortgage lien (may be enforced by a writ of execution)

RULE 68, Rules of Court: FORECLOSURE OF REAL ESTATE MORTGAGE

Section 1. Complaint in action for foreclosure.

In an action for the foreclosure of a mortgage or other encumbrance upon real estate, the complaint shall set forth the date and due execution of the mortgage; its assignments, if any; the names and residences of the mortgagor and the mortgagee; a description of the mortgaged property; a statement of the date of the note or other documentary evidence of the obligation secured by the mortgage, the amount claimed to be unpaid thereon; and the names and residences of all persons having or claiming an interest in the property subordinate in right to that of the holder of the mortgage, all of whom shall be made defendants in the action.

Sec. 2. Judgment on foreclosure for payment or sale.

If upon the trial in such action the court shall find the facts set forth in the complaint to be true, it shall ascertain the amount due to the plaintiff upon the mortgage debt or obligation, including interest and other charges as approved by the court, and costs, and shall render judgment for the sum so found due and order that the same be paid to the court or to the judgment obligee within a period of not less than ninety (90) days nor more than one hundred twenty (120) days from the entry of judgment, and that in default of such payment the property shall be sold at public auction to satisfy the judgment.

Sec. 3. Sale of mortgaged property; effect.

When the defendant, after being directed to do so as provided in the next preceding section, fails to pay the amount of the judgment within the period specified therein, the court, upon motion, shall order the property to be sold in the manner and under the provisions of Rule 39 and other regulations governing sales of real estate under execution (sold to the highest bidder at public auction). Such sale shall not affect the rights of persons holding prior encumbrances upon the property or a part thereof, and when confirmed by an order of the court, also upon motion, it shall operate to divest the rights in the property of all the parties to the action and to vest their rights in the purchaser, subject to such rights of redemption as may be allowed by law.

Upon the finality of the order of confirmation or upon the expiration of the period of redemption when allowed by law, the purchaser at the auction sale or last redemptioner, if any, shall be entitled to the possession of the property unless a third party is actually holding the same adversely to the judgment obligor. The said purchaser or last redemptioner may secure a writ of possession, upon motion, from the court which ordered the foreclosure.

Sec. 4. Disposition of proceeds of sale.

The amount realized from the foreclosure sale of the mortgaged property shall, after deducting the costs of the sale, be paid to the person foreclosing the mortgage, and when there shall be any balance or residue, after paying off the mortgage debt due, the same shall be paid to junior encumbrancers in the order of their priority, to be ascertained by the court, or if there be no such encumbrancers or there be a balance or residue after payment to them, then to the mortgagor or his duly authorized agent, or to the person entitled to it.

Note: if the mortgagee is retaining more of the proceeds of the sale than he is entitled to, this fact alone will not affect the validity of the foreclosure sale but simply gives the mortgagor a cause of action to recover such surplus.

Sec. 5. How sale to proceed in case the debt is not all due.

If the debt for which the mortgage or encumbrance was held is not all due as provided in the judgment, as soon as a sufficient portion of the property has been sold to pay the total amount and the costs due, the sale shall terminate; and afterwards, as often as more becomes due for principal or interest and other valid charges, the court may, on motion, order more to be sold. But if the property cannot be sold in portions without prejudice to the parties, the whole shall be ordered to be sold in the first instance, and the entire debt and costs shall be paid, if the proceeds of the sale be sufficient therefor, there being a rebate of interest where such rebate is proper.(????)

Sec. 6. Deficiency judgment.

If upon the sale of any real property as provided in the next preceding section there be a balance due to the plaintiff after applying the proceeds of the sale, the court, upon motion, shall render judgment against the defendant for any such balance for which, by the record of the case, he may be personally liable to the plaintiff, upon which execution may issue immediately if the balance is all due at the time of the rendition of the judgment; otherwise, the plaintiff shall be entitled to execution at such time as the balance remaining becomes due under the terms of the original contract, which time shall be stated in the judgment.

Sec. 7. Registration.

A certified copy of the final order of the court confirming the sale shall be registered in the registry of deeds. If no right of redemption exists, the certificate of title in the name of the mortgagor shall be cancelled, and a new one issued in the name of the purchaser.

Where a right of redemption exists, the certificate of title in the name of the mortgagor shall not be cancelled, but the certificate of sale and the order confirming the sale shall be registered and a brief memorandum thereof made by the registrar of deeds upon the certificate of title. In the event the property is redeemed, the deed of redemption shall be registered with the registry of deeds, and a brief memorandum thereof shall be made by the registrar of deeds on said certificate of title.

If the property is not redeemed, the final deed of sale executed by the sheriff in favor of the purchaser at the foreclosure sale shall be registered with the registry of deeds; whereupon the certificate of title in the name of the mortgagor shall be cancelled and a new one issued in the name of the purchaser.

Note: the proper remedy to seek reversal of a judgment in an action for foreclosure of real estate mortgage is an appeal from the judgment itself or from the order confirming the sale of the foreclosed real estate.

B. Extrajudicial

- By foreclosure by the mortgagee under power of sale contained in the mortgage
- The power to decide to foreclose or not is the prerogative of the mortgagee

Procedure

A.M. No. 99-10-05-0, August 7, 2001: PROCEDURE IN EXTRA-JUDICIAL FORECLOSURE OF MORTGAGE

The following procedures are hereby prescribed in extrajudicial foreclosure of mortgages:

1. All applications for extra-judicial foreclosure of mortgage whether under the direction of the sheriff or a notary public shall be filed with the Executive Judge, through the Clerk of court who is also the Ex-Officio Sheriff.
2. Upon receipt of an application for extra-judicial foreclosure of mortgage, it shall be the duty of the Clerk of Court to:
 - a. receive and docket said application and to stamp thereon the corresponding file number, date and time of filing;
 - b. collect the filing fees and issue the corresponding official receipt;
 - c. examine, in case of real estate mortgage foreclosure, whether the applicant has complied with all the requirements before the public auction is conducted under the direction of the sheriff or a notary public
 - d. sign and issue the certificate of sale, subject to the approval of the Executive Judge, or in his absence, the Vice-Executive Judge. No certificate of sale shall be issued in favor of the highest bidder until all fees shall have been paid; *Provided*, that in no case shall the amount payable exceed P100,000.00;
 - e. after the certificate of sale has been issued to the highest bidder, keep the complete records, while awaiting any redemption within a period of one (1) year from date of registration of the certificate of sale with the Register of Deeds concerned, after which, the records shall be archived. Notwithstanding the foregoing provision, juridical persons whose property is sold pursuant to an extra-judicial foreclosure, shall have the right to redeem the property until, but not after, the registration of the certificate of foreclosure sale which in no case shall be more than three (3) months after foreclosure, whichever is earlier.

Where the application concerns the extrajudicial foreclosure of mortgages of real estates and/or chattels in different locations covering one indebtedness, only one filing fee corresponding to such indebtedness shall be collected. The collecting Clerk of Court shall, apart from the official receipt of the fees, issue a certificate of payment indicating the amount of indebtedness, the filing fees collected, the mortgages sought to be foreclosed, the real estates and/or chattels mortgaged and their respective locations, which certificate shall serve

the purpose of having the application docketed with the Clerks of Court of the places where the other properties are located and of allowing the extrajudicial foreclosures to proceed thereat.

3. The notices of auction sale in extrajudicial foreclosure for publication by the sheriff or by a notary public shall be published in a newspaper of general circulation.

Q: why do you have to give notices? What is the real objective of giving such?

A: Notices are given for the purpose of securing bidders and to prevent a sacrifice of the property. IF these objects are attained, immaterial errors and mistakes will not affect the sufficiency of the notice.

Q: where and when or up to when should the notices be posted?

A: at least 3 public places not less than 20 days prior to the scheduled public sale.

Q: Is it required to publish the notice?

A: if property is worth more than P400, you should publish in a newspaper of General Circulation in the place where the property is located. You publish once a week for 3 consecutive weeks. (ex. Every Monday for 3 Mondays)

Note: failure to comply with notice or publication will render the notice void. Notice to the mortgagor is not required where there is no contractual stipulation therefor.

Q: what is contained in the notice? (C-T)

A: (1) correct certificate number and correct technical description of the real property to be sold, (2) time, place and date of public sale and the terms of the sale

Note: a certificate of posting is not required, much less considered indispensable for the validity of a foreclosure sale. Such certificate is significant only when it becomes necessary to prove compliance with the required notice of posting.

Remember: You cannot waive posting. To allow the parties to waive the posting and publication requirements would result in converting into a private sale what ought to be a public auction. It has been held, however, that the failure to post a notice is not per se a ground for invalidating a foreclosure sale provided that the notice thereof is duly published in a newspaper of general circulation

4. The Executive Judge shall, with the assistance of the Clerk of Court, raffle applications for extrajudicial foreclosure of mortgage under the direction of the sheriff among all sheriffs, including those assigned to the Office of the Clerk of Court and Sheriffs IV assigned in the branches.
5. The name/s of the bidder/s shall be reported by the sheriff or the notary public who conducted the sale to the Clerk of Court before the issuance of the certificate of sale.

Notes in Class...

In a real estate mortgage, mortgagee CANNOT as a matter of right initiate extrajudicial foreclosure.

Q: When does he have a right to demand such?

A: only if he is given the authority in the mortgage deed or in a separate document (special power of attorney)

Note: the authority to sell is not extinguished by the death of the mortgagor or mortgagee as it is an essential and inseparable party of a bilateral agreement

Q: What then is his remedy?

A: Initiate a Judicial Foreclosure proceedings

Q: where do you hold the public sale?

A: If place is ascertained in contract, the public sale will be held in the general location of the place or province where the property is located or at the municipal hall where the property is located

Note: the indivisibility of a real estate mortgage is not violated by conducting two separate foreclosure proceedings on mortgaged properties located in different cities or municipalities as long as each parcel of and is answerable for the entire debt.

Q: who conducts the public sale?

A: the sheriff or the notary public as provided for in the administrative matter. For the sheriff, the cases are raffled.

Q: But the law mentions of the Justice of the Peace (MTC Judge). Is the MTC judge precluded in the A.M. to conduct public sale?

A: MTC judges are NOT precluded

Q: if auction sale is published on a certain date, what time should it be held?

A: 9 am – 4 pm

Note: in a public sale of a movable, if there is no other bidder, you postpone the sale to another schedule (rule in Pledge).

Q: is such rule applicable to a mortgage foreclosure?

A: No. you don't have to schedule another auction sale. You can have 1 bidder only. SC reasoned that the notice posted and publication of notice is sufficient to inform 3rd persons.

Q: when there is already a winning bidder, what is issued and who issues?

A: For an auction sale conducted by either the sheriff or notary public, the clerk of court issues the certificate of sale

Note: when the creditor is not a banking institution but is a NATURAL person, he has 1 year redemption period from the time of registration. Between the period of redemption, the creditor or the highest bidder can ask for a WRIT OF POSSESSION (this is not a litigated proceeding) to be in possession of the property. The issuance of the writ to a purchaser in an extrajudicial foreclosure is merely a ministerial function. Any question regarding the validity of the mortgage or its foreclosure is not a legal ground for refusing the issuance of the writ.

Q: what is required so that the highest bidder can ask for a writ of possession?

A: one major consideration is that the property is in the hands of the mortgagor or of an agent or tenant who is the extension of the mortgagor.

Q: when the court issues this writ but later on it was determined that the sale should be annulled, will the highest bidder who was awarded possession be asked to return possession to the debtor?

A: No. the highest bidder remains in possession until the judgment of annulment becomes final and executor. Thus, pending appeal, highest bidder remains in possession.

The debtor can object to this by filing a PETITION FOR ANNULMENT OF THE SALE in the same proceeding by way of a counterclaim. Such petition can be based on two grounds: (1) mortgage was not violated (there was really no default/ debt was already paid) and (2) sale was defectively made (ex. No compliance of publication)

Note: the debtor can assign his right to redeem. However, the redemption period is NEVER EXTENDED.

If within the 1 year period of redemption no redemption is within (within registration sale), the buyer is entitled of a CONFORMATORY DEED OF SALE issued by the clerk of court. This instrument is a confirmation of the sale which is issued after the lapse of the redemption period.

Note however: the highest bidder can allow the debtor for an extension of redemption period.

Q: what happens to the Surplus proceeds form foreclosure sale?

A: They are constructively, at least, real property and belong to the mortgagor or his assigns. Surplus money gains much significance when there are junior encumbrancers on the mortgaged property. When there are several liens upon the property, the surplus money must be applied to their discharge in the order of their priority. The lien of the junior mortgagee on the property, after satisfying any prior mortgage is transferred to the surplus fund.

Q: Can the creditor recover the deficiency? How?

A: yes he can recover from the debtor. He should file an action for recovery of deficiency and this is when property is attached, or he can file for ordinary collection of money or for specific performance.

Remember: an extrajudicial foreclosure effected with fraud is null and void abinitio.

Deficiency Rule

- Mortgage is merely a security and not a satisfaction of an obligation. Therefore if there is a balance due to the mortgagee after applying the proceeds of the sale, the mortgagee is entitled to recover the deficiency.
- However, when a third person is the mortgagor, he is not liable for any deficiency in the absence of a contrary stipulation. The action for the recovery of such deficiency must be directed against the debtor
- The action to recover a deficiency after foreclosure prescribes after 10 years from the time the right of action accrues

DEVELOPMENT BANK OF THE PHILIPPINES vs. ALEJANDRO and ADELAIDA LICUANAN

G.R. No. 150097, February 26, 2007

Facts:

Respondent spouses Alejandro and Adelaida Licuanan were granted a piggery loan in the amount of ₱4,700 by petitioner, evidenced by a promissory note dated September 20, 1974 and secured by a real estate mortgage over a 980-square meter parcel of land with a two-storey building. The loan's maturity date was September 23, 1979. Petitioner granted respondents an additional loan of ₱12,000 evidenced by a promissory note dated May 29, 1975 payable on or before the year 1980. This was secured by a real estate mortgage over four parcels of land situated in Pangasinan. On October 2, 1975, petitioner granted respondent spouses another loan of ₱22,000 evidenced by a promissory note maturing on October 3, 1985. This was secured by a real estate mortgage executed in favor of petitioner over another three parcels of land

On July 6, 1981, petitioner sent a letter by registered mail to respondents informing them that, since the conditions of the mortgage had been breached, petitioner would have the mortgaged properties sold by the sheriff under Act 3135. The total amount due from the three loans had by then ballooned to ₱75,298.32.

On July 20, 1981, petitioner filed an application for extrajudicial foreclosure. The mortgaged properties were sold in a public auction on December 16, 1981. Petitioner, as the highest bidder, acquired them for a total of ₱16,340. The certificate of sale was registered on January 25, 1982.

On February 4, 1983, petitioner consolidated its ownership over the properties. After more than a year or on October 16, 1984, petitioner wrote respondents by registered mail, informing them that the properties (now acquired assets of the bank) would be disposed of by public auction. On November 11, 1984, petitioner published an advertisement stating that on November 14, 1984, the properties would be sold by oral bidding. On this date, however, there were no bidders.

On November 16, 1984, petitioner sent respondents a letter informing them that the properties could be reacquired by negotiated sale for cash or installment. Three days later, however, on November 19, 1984, the properties were sold through negotiated sale to one Emelita A. Peralta. Respondents were informed of the sale by petitioner through a letter dated December 6, 1984.

On the same day, petitioner executed a deed of conditional sale in favor of Peralta. On December 11, 1984, respondents offered to repurchase the properties from petitioner but they had already been sold to Peralta. Respondents then filed a complaint for recovery of real properties and damages.

Issue:

Whether or not respondents are liable for the deficiency claim of petitioner.

Take Note: The price in which the mortgaged property was sold was ₱104,000 which was less than the amount of respondents' indebtedness which is ₱131,642.33.

SC Ruling:

No. the respondents are not responsible for the deficiency claim. While it is true that in extrajudicial foreclosure of mortgage, the mortgagee has the right to recover the deficiency from the debtor this presupposes that the foreclosure must first be valid.

But in this case, the foreclosure is invalid. If demand was made and duly received by the respondents and the latter still did not pay, then they were already in default and foreclosure was proper. However, if demand was not made, then the loans had not yet become due and demandable. This meant that respondents had not defaulted in their payments and the foreclosure by petitioner was premature. Foreclosure is valid only when the debtor is in default in the payment of his obligation.

V. Redemption

- Transaction by which the mortgagor reacquires or buys back the property which may have passed under the mortgage or divests the property of the lien which the mortgage may have created.
- This right is an absolute privilege, the exercise of which is entirely dependent upon the will and discretion of the redemptioner.
- This right is a mere statutory privilege, hence it must be exercised in the mode and within the period prescribed by the statute.
- What actually is effected where redemption is seasonable exercised by the judgment or mortgage debtor is not the recovery of the property which ownership is never lost. Rather, the redemption by the debtor eliminates but from his title the lien created by the levy or attachment or judgment or registration of the mortgage thereon. The redemption defeats the inchoate right of the purchaser and restores the property to the same condition as if no sale had been made.

Q: what do you need to preserve the right of redemption?

A: being optional and not compulsory, a formal offer to redeem accompanied by a bona fide tender of the redemption price within the prescribed period of redemption is only essential to preserve the right of redemption for future enforcement even beyond such period. But where the right to redeem is exercised thru the filing of judicial action, within the period of redemption, such filing is equivalent to a formal offer to redeem and have the effect of preserving the right of redemption.

Note: redemption is inconsistent with the claim of the invalidity of the sale

Remember: The right of the purchaser at the foreclosure sale is merely inchoate until after the period of redemption has expired without the right being exercised.

Remember: where there is a right to redeem, inadequacy of price is not material because the judgment debtor may reacquire the property or sell his right to redeem and thus recover any loss he claims to have suffered by reason of the price obtained at the auction sale.

Requisites of a Valid Redemption (1-P-W)

1. The redemption must be made within one year from the date of registration of the certificate of sale
2. Payment of the purchase price of the property plus 1% interest per month together with the taxes thereon, if any, paid by the purchaser and the amount of his prior lien, if any, with the same rate of interest computed from the date of registration of the sale, up to the time of redemption
3. Written notice of redemption must be served on the officer who made the sale and a duplicate filed with the proper Register of deeds

A. Rules

- the right of redemption, as long as within the period prescribed, may be exercised irrespective of whether or not the mortgagee has subsequently conveyed the property to some other party.

Judicial Foreclosure and Extrajudicial Foreclosure

Foreclosure	Mortgagor	
	Natural	Juridical
Extrajudicial	1 year from the registration of the certificate of sale (Right of redemption)	Until but not later than registration of the certificate of foreclosure sale which in no case shall be more than 90 days from the foreclosure sale whichever comes first
Judicial	Equity of Redemption from finality (between 90 to 120 days from finality of judgment)	Not less than 90 days nor greater than 120 days From the finality of judgment.

Mortgage: Bank

Foreclosure	Mortgagor	
	Natural	Juridical
Extrajudicial	1 year from SALE	Until, but not later than the registration of sale but in no cause more than 90 days from the sale

Judicial	1 year from sale or foreclosure date of sale	1 year from sale
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Right of Redemption vs. Equity of Redemption

- *Equity of Redemption* – the right of the mortgagor in case of judicial foreclosure to redeem the mortgaged property after his default in the performance of the condition of the mortgage but before the confirmation of the sale of the mortgaged property
 - This is simply the right of the mortgagor to extinguish the mortgage and retain ownership of the property by paying the secured debt within the 120-day period from the entry of judgment , or even after the foreclosure sale but prior to its confirmation
 - In judicial foreclosure, the mortgagor may exercise his equity of redemption before but not after the sale is confirmed by the court
 - A second mortgagee acquired only the equity of redemption vested in the mortgagor and his rights are strictly subordinate to the superior lien of the first mortgagee
 - Note: confirmation retroacts to the day the day of the sale. In order that foreclosure sale may be validly confirmed by the court, it is necessary that a hearing be given the interested parties, at which they may have an opportunity to show cause why the sale should not be confirmed.
- *Right of Redemption* – the right of the mortgagor in case of extrajudicial foreclosure to redeem the mortgaged property within a certain period from and after it was sold for the satisfaction of the mortgage debt
 - Note: the filing of an action by the redemptioner to enforce his right to redeem does not suspend the running of the statutory period to redeem the property
 - The one-year period is subject to the provisions of special laws. The statutory period of redemption is only directory and can be extended by agreement of the parties but two requisites must be established:
 - Voluntary agreement of the parties to extend the period
 - The debtor's commitment to pay the redemption price on a fixed date

HUERTA ALBA RESORT INC. vs. COURT OF APPEALS and SYNDICATED MANAGEMENT GROUP INC
G.R. No. 128567, September 1, 2000

Facts:

In a complaint for judicial foreclosure of mortgage with preliminary injunction filed on October 19, 1989, the herein private respondent sought the foreclosure of four (4) parcels of land mortgaged by petitioner to Intercon Fund Resource, Inc. ("Intercon").

Private respondent instituted the case as mortgagee-assignee of a loan amounting to P8.5 million obtained by petitioner from Intercon, in whose favor petitioner mortgaged the aforesaid parcels of land as security for the said loan.

In its answer below, petitioner questioned the assignment by Intercon of its mortgage right thereover to the private respondent, on the ground that the same was *ultra vires*. Petitioner also questioned during the trial the correctness of the charges and interest on the mortgage debt in question.

On April 30, 1992, the trial court, came out with its decision granting herein private respondent SMGI's complaint for judicial foreclosure of mortgage. Upon appeal, it was dismissed on the ground of late payment of docket fees. Later, the decision became final and executory.

On July 4, 1994, private respondent filed with the trial court of origin a motion for execution of the Decision promulgated on April 30, 1992 in Civil Case No. 89-5424. The said motion was granted on July 15, 1994. Accordingly, on July 15, 1994 a writ of execution issued and, on July 20, 1994, a Notice of Levy and Execution was issued by the Sheriff concerned, who issued on August 1, 1994 a Notice of Sheriff's Sale for the auction of subject properties on September 6, 1994.

On August 23, 1994, petitioner filed with the same trial court an Urgent Motion to Quash and Set Aside Writ of Execution ascribing to it grave abuse of discretion in issuing the questioned Writ of Execution. To support its motion, petitioner invited attention and argued that the records of the case were still with the Court of Appeals and therefore, issuance of the writ of execution was premature since the 150-day period for petitioner to pay the judgment obligation had not yet lapsed and petitioner had not yet defaulted in the payment thereof since no demand for its payment was made by the private respondent. In petitioner's own words, the dispute between the parties was "principally on the issue as to when the 150-day period within which Huerta Alba may exercise its equity of redemption should be counted."

Issue:

Whether or not the petitioner has the one-year right of redemption of subject properties under Section 78 of Republic Act No. 337 otherwise known as the General Banking Act.

SC Ruling:

No. The petitioner can no longer invoke Section 78 of Republic Act No. 337 because it failed to seasonably invoke the said provision.

On the distinction between the *equity* of redemption and right of redemption, the case of *Gregorio Y. Limpin vs. Intermediate Appellate Court*, comes to the fore. Held the Court in the said case:

"The *equity of redemption* is, to be sure, different from and should not be confused with the *right of redemption*.

The *right of redemption* in relation to a mortgage – understood in the sense of a prerogative to re-acquire mortgaged property after registration of the foreclosure sale – exists only in the case of

the extrajudicial foreclosure of the mortgage. No such right is recognized in a judicial foreclosure except only where the mortgagee is the Philippine National Bank or a bank or banking institution.

Where a mortgage is *foreclosed extrajudicially*, Act 3135 grants to the mortgagor the right of redemption within one (1) year from the registration of the sheriff's certificate of foreclosure sale.

Where the *foreclosure is judicially effected*, however, no equivalent right of redemption exists. The law declares that a *judicial foreclosure sale 'when confirmed be an order of the court. . . shall operate to divest the rights of all the parties to the action and to vest their rights in the purchaser, subject to such rights of redemption as may be allowed by law.'* Such rights exceptionally 'allowed by law' (i.e., even after confirmation by an order of the court) are those granted by the charter of the Philippine National Bank (Acts No. 2747 and 2938), and the General Banking Act (R.A. 337). *These laws confer on the mortgagor, his successors in interest or any judgment creditor of the mortgagor, the right to redeem the property sold on foreclosure — after confirmation by the court of the foreclosure sale — which right may be exercised within a period of one (1) year, counted from the date of registration of the certificate of sale in the Registry of Property.*

But, to repeat, no such right of redemption exists in case of judicial foreclosure of a mortgage if the mortgagee is not the PNB or a bank or banking institution. In such a case, the foreclosure sale, 'when confirmed by an order of the court. . . shall operate to divest the rights of all the parties to the action and to vest their rights in the purchaser.' There then exists only what is known as the equity of redemption. *This is simply the right of the defendant mortgagor to extinguish the mortgage and retain ownership of the property by paying the secured debt within the 90-day period after the judgment becomes final, in accordance with Rule 68, or even after the foreclosure sale but prior to its confirmation.*

Section 2, Rule 68 provides that —

' . . If upon the trial . . the court shall find the facts set forth in the complaint to be true, it shall ascertain the amount due to the plaintiff upon the mortgage debt or obligation, including interest and costs, and shall render judgment for the sum so found due and order the same to be paid into court within a period of not less than ninety (90) days from the date of the service of such order, and that in default of such payment the property be sold to realize the mortgage debt and costs.'

This is the mortgagor's *equity (not right) of redemption* which, as above stated, may be exercised by him even beyond the 90-day period 'from the date of service of the order,' and even after the foreclosure sale itself, provided it be before the order of confirmation of the sale. After such order of confirmation, no redemption can be effected any longer." (Emphasis supplied)

It is bear stressing that petitioner avers in its petition that the Intercom, predecessor in interest of the private respondent, is a credit institution, such that Section 78 of Republic Act No. 337 should apply in this case. Stated differently, it is the submission of petitioner that it should be allowed to redeem subject properties within one year from the date of sale as a result of the foreclosure of the mortgage constituted thereon.

The pivot of inquiry here therefore, is whether the petitioner seasonably invoked its asserted right under Section 78 of R.A. No. 337 to redeem subject properties.

The court finds that in light of the aforestated facts, it was too late in the day for petitioner to invoke a right to redeem under Section 78 of R.A. No. 337. Petitioner failed to assert a right to redeem in several crucial stages of the proceedings.

Indeed, at the earliest opportunity, when it submitted its answer to the complaint for judicial foreclosure, petitioner should have alleged that it was entitled to the beneficial provisions of Section 78 of R.A. No. 337 but again, it did not make any allegation in its answer regarding any right thereunder. It bears stressing that the applicability of Section 78 of R.A. No. 337 hinges on the factual question of whether or not private respondent's predecessor in interest was a credit institution. As was held in *Limpin*, a judicial foreclosure sale, "when confirmed by an order of the court, . . . shall operate to divest the rights of all the parties to the action and to vest their rights in the purchaser, *subject to such rights of redemption as may be allowed by law*," which confer on the mortgagor, his successors in interest or any judgment creditor of the mortgagor, the right to redeem the property sold on foreclosure after confirmation by the court of the judicial foreclosure sale. Thus, the claim that petitioner is entitled to the beneficial provisions of Section 78 of R.A. No. 337 —since private respondent's predecessor-in-interest is a credit institution — is in the nature of a compulsory counterclaim which should have been averred in petitioner's answer to the complaint for judicial foreclosure.

The failure of petitioner to seasonably assert its alleged right under Section 78 of R.A. No. 337 precludes it from so doing at this late stage case. Estoppel may be successfully invoked if the party fails to raise the question in the early stages of the proceedings. Thus, "a party to a case who failed to invoke his claim in the main case, while having the opportunity to do so, will be precluded, subsequently, from invoking his claim, even if it were true, after the decision has become final, otherwise the judgment may be reduced to a mockery and the administration of justice may be placed in disrepute."

B. How Done

- You tender the following:
 - o Make a formal offer to redeem
 - o Tender the actual price interest of 1% per month
 - o Pay tax and assessment paid by the buyer
 - o 1% interest of the tax and assessment

Remember: both should be made within 12 months period. You cannot UNILATERALLY extend the redemption period

BANCO FILIPINO SAVINGS AND MORTGAGE BANK *vs.* COURT OF APPEALS and SANTIAGO (Isabela) MEMORIAL PARK, INC.
G.R. No. 143896, July 8, 2005

Facts:

On December 20, 1993, private respondent Santiago (Isabela) Memorial Park, Inc. filed a complaint for redemption and specific performance with the Regional Trial Court of Santiago, Isabela, Branch 21, against herein petitioner Banco Filipino Savings & Mortgage Bank., the material and relevant allegations of which read as follows:

COMPLAINT

Plaintiff, by counsel, to this Honorable Court most respectfully alleges:

1. .
2. .
3. *That in February 1981, plaintiff mortgaged the above described property in favor of defendant to secure a loan of ₱500,000.00 obtained by plaintiff from defendant;*
4. *That due to the failure of plaintiff to pay the aforementioned loan, defendant foreclosed the mortgage and in consequence thereof Sheriff David R. Medina of this Honorable Court issued a SHERIFF'S CERTIFICATE OF SALE in favor of defendant which is dated October 9, 1990 and which instrument was inscribed at the back of TCT T-128647 of Isabela on January 21, 1991;*
5. *That in a letter of the President of plaintiff dated August 6, 1991, plaintiff made manifest its interest to exercise its right of redemption and made an offer of ₱700,000.00 as redemption to defendant through the then Deputy Liquidator, ROSAURO NAPA; this started the negotiation for the redemption of the above described property;*
6. *That in a letter of the Deputy Liquidator dated January 23, 1992, plaintiff was given up to the end of March 1992 to negotiate and make special arrangement for any satisfactory plan of payment for the redemption;*
7. *That in a letter of the Deputy Liquidator dated March 12, 1992, plaintiff was directed to remit at least ₱50,000.00 to defendant which would manifest the interest and willingness of plaintiff to redeem the property, and forthwith on March 24, 1992, plaintiff remitted the sum of ₱50,000.00 to defendant which was duly receipted by the latter under Official Receipt No. 279968 A dated March 24, 1992;*
8. *That in a letter of the President of plaintiff dated January 20, 1993, plaintiff amended its first offer and made an offer of ₱1,000,000.00 as redemption which offer included a plan of payment;*
9. *That between January 20, 1993 to November 1993, plaintiff exerted earnest efforts in order to finally effect the redemption, but defendant dilly dallied on the matter.*
10. *That in a letter of Atty. ORLANDO O. SAMSON, Senior Vice President of defendant, dated November 5, 1993, there is a turn-around by defendant and is now demanding ₱5,830,000.00 as purchase price of the property, instead of the original agreed redemption;*
11. *That the delay of the defendant in the finalization of the terms of redemption did not in any manner alter the right of plaintiff to redeem the property from defendant;*
12. *That plaintiff is still in actual possession of the property and intend to remain in actual possession of the property, while defendant was never in actual possession of said property;*
13. *That plaintiff is ready and willing to pay the redemption money, which is the total bank claim of ₱925,448.17 plus lawful interest and other allowable expenses incident to the foreclosure proceedings;*
14. *That the latest actuations of defendant are indicative of the refusal of defendant to allow the exercise of redemption by herein plaintiff, reason for which there is a need for judicial determination of the rights and obligations of the parties to this case;*
15. *That on account of the unlawful actuations of defendant in refusing the redemption of the property by plaintiff, the latter engaged the services of counsel for a fee of ₱30,000.00 which defendant should pay to plaintiff.*

Issue:

Whether private respondent's complaint for redemption and specific performance states a cause of action against petitioner.

SC Ruling:

Based on the allegations in the complaint, we find that private respondent has no cause of action for redemption against petitioner.

Paragraph 4 of the complaint states:

4. That due to the failure of plaintiff to pay the aforementioned loan, defendant foreclosed the mortgage and in consequence thereof Sheriff David R. Medina of this Honorable Court issued a SHERIFF'S CERTIFICATE OF SALE in favor of defendant which is dated October 9, 1990 and which instrument was inscribed at the back of TCT T-128647 of Isabela on January 21, 1991;

The sheriff's certificate of sale was registered on January 21, 1991. Section 6 of Act 3135 provides for the requisites for a valid redemption, thus:

SEC. 6. In all cases in which an extrajudicial sale is made under the special power hereinbefore referred to, the debtor, his successors in interest or any judicial creditor or judgment creditor of said debtor, or any person having a lien on the property subsequent to the mortgage or deed of trust under which the property is sold, may redeem the same at any time within the term of one year from and after the date of sale; and such redemption shall be governed by the provisions of sections four hundred and sixty-four to four hundred and sixty-six, inclusive, of the Code of Civil Procedure, insofar as these are not inconsistent with the provisions of this Act.

However, considering that petitioner is a banking institution, the determination of the redemption price is governed by Section 78 of the General Banking Act which provides:

In the event of foreclosure, whether judicially or extrajudicially, of any mortgage on real estate which is security for any loan granted before the passage of this Act or under the provisions of this Act, the mortgagor or debtor whose real property has been sold at public auction, judicially or extrajudicially, for the full or partial payment of an obligation to any bank, banking or credit institution, within the purview of this Act shall have the right, within one year after the sale of the real estate as a result of the foreclosure of the respective mortgage, to redeem the property by paying the amount fixed by the court in the order of execution, or the amount due under the mortgage deed, as the case may be, with interest thereon at the rate specified in the mortgage, and all the costs, and judicial and other expenses incurred by the bank or institution concerned by reason of the execution and sale and as a result of the custody of said property less the income received from the property.

Clearly, the right of redemption should be exercised within the specified time limit, which is one year from the date of registration of the certificate of sale. The redemptioner should make an actual tender in good faith of the full amount of the purchase price as provided above, *i.e.*, the amount fixed by the court in the order of execution or the amount due under the mortgage deed, as the case may be, with interest thereon at the rate specified in the mortgage, and all the costs, and judicial and other expenses incurred by the bank or institution concerned by reason of the execution and sale and as a result of the custody of said property less the income received from the property.

In case of disagreement over the redemption price, the redemptioner may preserve his right of redemption through judicial action which in every case must be filed within the one-year period of

redemption. The filing of the court action to enforce redemption, being equivalent to a formal offer to redeem, would have the effect of preserving his redemptive rights and 'freezing the expiration of the one-year period. In this case, the period of redemption expired on January 21, 1992. The complaint was filed on December 20, 1992.

Moreover, while the complaint alleges that private respondent made an offer to redeem the subject property on August 6, 1991, which was within the period of redemption, it is not alleged in the complaint that there was an actual tender of payment of the redemption price as required by the rules. It was alleged that private respondent merely made an offer of P700,000.00 as redemption price, which however, as stated under paragraph 13 of the same complaint, the redemption money was the total bank claim of P925,448.17 plus lawful interest and other allowable expenses incident to the foreclosure proceedings. Thus, the offer was even very much lower than the price paid by petitioner as the highest bidder in the auction sale.

In *BPI Family Savings Bank, Inc. vs. Veloso*, we held that the general rule in redemption is that it is not sufficient that a person offering to redeem manifests his desire to do so. The statement of intention must be accompanied by an actual and simultaneous tender of payment. This constitutes the exercise of the right to repurchase.

Q: Who are entitled to redeem? (M-S-R)

A: the following are entitled to redeem:

1. Mortgagor or one in privity of title with mortgagor
2. Successor in interest
3. Under the rules of court: Redemptioner - a creditor having a lien by attachment, judgment or mortgage on the property sold or some part thereof, subsequent to the judgment under which the property was sold

C. What is to be paid

- the tender of payment must be for the full amount of the purchase price; otherwise, to allow payment by installments would be to allow the indefinite extension of the redemption period
- Redemption within the period allowed by law is not a matter of intent but a question of payment or valid tender of the full redemption price within the said period
- The purchaser is entitled to reimbursement of the reasonable cost of improvements made by him to preserve the property during the period of redemption

Q: who is entitled to the received rentals from the property?

A: The purchaser or redemptioner shall not be entitled to receive the rents, earnings and income of the property sold on execution, or the value of the use and occupation thereof when such property is in the possession of a tenant which rents, etc. Shall belong to the judgment obligor until the expiration of the period of redemption

CHINA BANKING CORPORATION vs. HON. COURT OF APPEALS, PAULINO ROXAS CHUA and KIANG MING CHU CHUA

G.R. No. 129644, September 7, 2001

Facts:

By virtue of an adverse decision in a case, entitled *"Metropolitan Bank and Trust Company v. Pacific Multi Commercial Corporation and Alfonso Roxas Chua,"* the residential land (TCT No. 410603) in the name of spouses Alfonso Roxas Chua and Kiang Ming Chu Chua was levied on execution. Kiang Ming Chu Chua filed an action questioning the levy on the ground that the land was conjugal partnership property. This resulted in a compromise agreement to the effect that the levy shall be valid only to the extent of the $\frac{1}{2}$ share pertaining to Alfonso Roxas Chua. After the execution sale, a certificate of sale was executed in favor of Metrobank, the judgment creditor, and the same was annotated on TCT No. 410603 on December 22, 1987.

Meanwhile, China Banking Corporation filed a complaint for sum of money against Pacific Multi Agro-Industrial Corporation and Alfonso Roxas Chua. On November 7, 1985, judgment was rendered ordering defendants to pay Chinabank the aggregate amount of P2,500,000.00 plus interests, penalties and attorney's fees. Defendants appealed to the Court of Appeals but the same was dismissed for failure to file appellants' brief. Thus, notice of levy on execution was issued on February 4, 1991 against the right and interest of Alfonso Roxas Chua in the residential land (TCT No. 410603). The same was later sold at public auction and a certificate of sale was executed in favor of Chinabank, and inscribed on TCT 410603 on May 4, 1992.

Previously, however, on November 21, 1988, Alfonso Roxas Chua executed in favor of his son, Paulino Roxas Chua, an "Assignment of Right to Redeem," pertaining to his right to redeem the $\frac{1}{2}$ undivided portion of the land sold to Metrobank. On January 11, 1989, Paulino redeemed the property from Metrobank. On March 14, 1989, the Assignment of Right to Redeem and the redemption by Paulino Roxas Chua of the property from Metrobank were annotated on TCT No. 410603.

Private respondents Paulino Roxas Chua and Kiang Ming Chu Chua filed a case, alleging that Paulino has a prior and better right over Chinabank inasmuch as the assignment to him of the right to redeem and his redemption of Alfonso's share in the property were inscribed on the title on an earlier date than the annotation of the notice of levy and certificate of sale in favor of Chinabank. Both the trial court and the Court of Appeals ruled in favor of private respondents and enjoined Chinabank, the Sheriff of Manila and the Register of Deeds of San Juan from causing the transfer of possession, ownership and certificate of title, or otherwise disposing of the property covered by TCT No. 410603 in favor of Chinabank or any other person.

Issue:

Whether or not the conveyance of the property in question to Paulino Roxas Chua was done for valuable consideration and in good faith.

SC Ruling:

Yes, it was done for value and in good faith.

Article 1387 of the Civil Code provides that alienations made by a debtor by gratuitous title are presumed fraudulent when the donor did not reserve sufficient property to pay his outstanding debts.

Likewise, alienations by onerous title are presumed fraudulent when made by persons against whom some judgment has been rendered or some writ of attachment has been issued. These, however, are mere presumptions which are in no way conclusive. The presumption of fraud can be overthrown by evidence showing that the conveyance was made in good faith and for a sufficient and valuable consideration.

In the case at bar, private respondents sufficiently established that the conveyance was made in good faith and for valuable consideration. Paulino maintains that he had no knowledge of his father Alfonso's financial problem with petitioner Chinabank until he was about to cause the cancellation of TCT No. 410603. Furthermore, he paid the sum of P100,000.00 to Alfonso for the right to redeem, and paid the redemption amount of P1,463,375.39 to Metrobank.

Expectedly, petitioner refutes these, saying that the amounts paid by Paulino were grossly disproportionate to the right to redeem the property, which is a residential house and lot located in North Greenhills, San Juan, Metro Manila. But as correctly pointed out by private respondents, the amount of P100,000.00 paid by Paulino to Alfonso was not for the property itself, but merely for the right to redeem the same. As a matter of fact, Paulino still had to pay Metrobank the redemption price of P1,463,375.39. Whether or not the latter amount was adequate is beyond the scope of this inquiry. Suffice it to state that Metrobank accepted the same and reconveyed the property to Paulino. Moreover, only Alfonso's conjugal share in the property was affected, and the determination of its value was still subject to liquidation of debts and charges against the conjugal partnership.

Effect of tender of less than purchase price

BPI FAMILY SAVINGS BANK, INC vs. SPS. JANUARIO ANTONIO VELOSO AND NATIVIDAD VELOSO
G.R. No. 141974, August 9, 2004

Facts:

On January 8, 1983, respondent spouses obtained a loan of P1,300,000 from petitioner's predecessor-in-interest Family Bank and Trust Company. To secure payment of the loan, respondent spouses executed in favor of the bank a deed of mortgage over three parcels of land, with improvements, registered in their names under TCT Nos. 272227, 272228 and 272229 of the Registry of Deeds of Quezon City.

On February 9, 1983, respondents, for value received, executed a promissory note for P1,300,000. Subsequently, however, respondents defaulted in the monthly installments due on their loan. When efforts to update the account failed, Family Bank instituted extra-judicial foreclosure proceedings on the respondents' mortgaged properties.

On July 1, 1985, the properties were sold at public auction with Family Bank as the highest bidder for P2,782,554.66. On August 5, 1985, Family Bank assigned all its rights and interests in the foreclosed properties to petitioner BPI Family Bank, Inc. (BPI). On August 28, 1985, the sheriff's certificate of sale was registered with the Registry of Deeds of Quezon City.

On July 24, 1986, respondents, through counsel, wrote BPI offering to redeem the foreclosed properties for P1,872,935. This was, however, rejected by petitioner.

On August 27, 1986, respondents filed in the RTC of Quezon City, Branch 94, a complaint for annulment of foreclosure, with consignment and prayer for damages. On motion of respondents, the

trial court, in an order dated August 27, 1986, allowed respondents to deposit with the clerk of court the sum of ₱1,500,000 representing the redemption price. Thereafter, trial on the merits ensued.

Issue:

Did respondent spouses comply with all the requirements for the redemption of the subject properties?

SC Ruling:

We answer in the negative.

The general rule in redemption is that it is not sufficient that a person offering to redeem manifests his desire to do so. The statement of intention must be accompanied by an actual and simultaneous tender of payment. This constitutes the exercise of the right to repurchase.

In several cases decided by the Court where the right to repurchase was held to have been properly exercised, there was an unequivocal tender of payment for the full amount of the repurchase price. Otherwise, the offer to redeem is ineffectual. *Bona fide* redemption necessarily implies a reasonable and valid tender of the entire repurchase price, otherwise the rule on the redemption period fixed by law can easily be circumvented.

Consequently, in this case, the offer by respondents on July 24, 1986 to redeem the foreclosed properties for ₱1,872,935 and the subsequent consignment in court of ₱1,500,000 on August 27, 1986, while made within the period of redemption, was ineffective since the amount offered and actually consigned not only did not include the interest but was in fact also way below the ₱2,782,554.66 paid by the highest bidder/purchaser of the properties during the auction sale.

In *Bodiongan vs. Court of Appeals*, we held:

In order to effect a redemption, the judgment debtor must pay the purchaser the redemption price composed of the following: (1) the price which the purchaser paid for the property; (2) interest of 1% per month on the purchase price; (3) the amount of any assessments or taxes which the purchaser may have paid on the property after the purchase; and (4) interest of 1% per month on such assessments and taxes x x x.

Furthermore, Article 1616 of the Civil Code of the Philippines provides:

The vendor cannot avail himself of the right to repurchase without returning to the vendee the price of the sale x x x.

It is not difficult to understand why the redemption price should either be fully offered in legal tender or else validly consigned in court. Only by such means can the auction winner be assured that the offer to redeem is being made in good faith.

Effect of Death of Mortgagor

- The secured creditor holding a real estate mortgage has 3 distinct, independent, and mutually EXCLUSIVE remedies that can be ALTERNATIVELY pursued by him for the satisfaction of his credit in case the mortgagor dies: (W-F-R)
 - o To waive the mortgage and claim the entire debt from the estate of the mortgagor as an ordinary claim
 - o To foreclose the mortgage JUDICIALLY and prove any deficiency as an ordinary claim
 - o To rely on the mortgage exclusively, foreclosing the same at any time before it is barred by prescription without right to file a claim for any deficiency --- this includes

extrajudicial foreclosure which bars any subsequent deficiency claim against the estate of the deceased

D. Remedies of Mortgagee in Equitable Mortgage

- ✓ Where a contract purporting to be a pacto de retro sale is in reality a loan with equitable mortgage, the vendor can defeat the contract by resorting to any of the following remedies: (1) by bringing an action for reformation of the instrument into a loan with equitable mortgage; (2) by alleging as a defense that the real intention of the parties was a loan with equitable mortgage, which in effect, is for the reformation of the instrument; and (3) by judicial objection or opposition to the registration of the affidavit or consolidation of ownership on the ground that the real intention of the parties was a loan with equitable mortgage.

Remember:

The mortgagee may institute either a personal action for debt or a real action to foreclose the mortgage. The mortgagee however cannot have both remedies. He has only one cause of action
ooOoo

ANTICHRESIS

Articles 2132 – 2139

I. Concept

- It is a real right established to secure the performance of an obligation and whereby the holder acquires the right to receive the fruit of an immovable with the obligation to apply them to the payment of the interest, if owing and thereafter to the principal of the credit. [Art. 2132]

Q: what is the objective on an antichresis?

A: its objective is to grant the creditor the use of the fruits or to derive its fruits while to obligation of the debtor stands

Characteristics of the Contract:

1. Accessory Contract – it secures the performance of a principal obligation
2. Formal contract – it must be in writing to be valid

Note: Antichresis requires the delivery by the debtor of the property given as security to the creditor. But such delivery is required only in order that the creditor may receive the fruits and not that the contract shall be binding. The contract does not cover the immovable but only its fruits.

A. Similarities and Differences with Real Estate Mortgage

a. Similarities

- both are indivisible
- they may be constituted by the debtor or a stranger
- they must be constituted on immovable (but these must be fruit-bearing (industrial, civil and natural) in antichresis)
- both may secure all kinds of obligation
- both are accessory contracts

b. Differences

<u>ANTICHRESIS</u>	<u>REAL ESTATE MORTGAGE</u>
- The property is delivered to the creditor	- The debtor usually retains possession of the property
- The creditor acquires only the right to receive the fruits of the property --- it <u>does not produce a real right</u>	- Creditor does not have any right to receive the fruits, but mortgage <u>creates a real right</u> over the property which is enforceable against the whole world
- The creditor, unless there is a stipulation to the contrary, is obliged to pay the taxes and charges upon the estate	- The creditor has no such obligation
- It is expressly stipulated that the creditor given possession of the property shall apply the fruits thereof to the payment of interest, if owning, and thereafter to the principal	- There is no such obligation on the part of the mortgagee

Antichresis vs. Pledge

<u>ANTICHRESIS</u>	<u>PLEDGE</u>
Refers to real property	Refers to personal property
Is perfected by mere consent	Perfected by the delivery of the thing pledged
It is a consensual contract	It is a real contract

Article 2133

- the contract does not cover the immovable but only its fruits
- the fruits of the immovable which is the object of the antichresis must be appraised at their actual market value at the time of the application

II. Elements

A. Parties

- The contract of antichresis may be established by one having the right to encumber property.

B. Object

- It may be constituted only on immovable giving fruits.

C. Causa

- The same with that of the principal obligation.

D. Formalities

- The amount of the principal and the interest must be specified in writing; otherwise the contract is void. (Article 2134)
- It must be in a public instrument to affect third persons or recorded if the property involved is registered. [writing in paper can bind the parties. But to bind third person, it must be in a public instrument--- PD 1529]

Note: even if the antichresis is void, the principal obligation, however is still valid. Verbal agreement is not valid, but the underlying obligation still exists

III. Effects

A. Rights of the antichretic creditor

- a. To receive the fruits, applying them at their actual value, as of the time of the application to the interest and the to the capital (art. 2132)
 - Parties may stipulate that the interest be compensated by the fruits, provided that if the value of the fruits exceed the interest allowed by the usury law the excess shall apply to the capital.
 - A provision in the contract that the full amount of the indebtedness must be returned to the lenders before the borrowers could demand the return of the property is contrary to an antichretic contract wherein the products of the land should be applied to the interest and then to the principal.

Q: what if you don't state the value of the interest? Is it enough to state that the principal bears interest?

A: Article 2138: by implication, you need not state the rate of the interest.

Note: if stipulated, fruits can be made payment for the compensation of interest. All the fruits will be paid for interest.

- b. Right of foreclosure: the creditor does not acquire ownership of the immovable for non-payment of the debt (Article 2137).
 - A contrary stipulation is void.
 - The creditor may ask the court for the sale of the property, subject to the foreclosure of mortgages.

Q: what are the remedies of the creditor for nonpayment of the debt? (S-S)

A: (1) to bring an action for specific performance, (2) to petition for the sale of the real property as in a foreclosure of mortgages (judicial foreclosure only)

B. Obligations of the antichretic creditor

- a. To bear necessary expenses for the preservation and repair (Article 2135)

- These are deductible from the fruits
- b. To pay taxes and charges upon the estate (Article 2135)
 1. Reason
 - Otherwise the debtor could deprive the creditor of the security by not paying taxes and causing forfeiture.
 2. Exception
 - When the contrary is stipulated
 3. Effect of non-fulfillment
 - The creditor is liable for damages (failure to pay: property is DISTRAINT).
 - These taxes and charges are deductible from the fruits.
 - Where the debtor has paid for the taxes on the property which the creditor should have paid, the amount is to be applied to the payment of the debt, and the debtor is entitled to the return of the property free from all encumbrances if he, in effect, by advancing the taxes, had already discharged the debt

Q: What if the fruits are not sufficient to pay for the necessary expenses and taxes?

A: even if fruits are not enough, the creditor is still obliged to pay. If he is not willing, he can demand the debtor to again enjoy the property (look at 2136).

Diego vs. Fernando

109 Phil. 143, August 25, 1960

Facts:

Defendant Fernando executed a deed of mortgage in favor of the plaintiff over two parcels of land to secure a loan of two thousand without interest payable within four years. The possession of the mortgaged properties was turned over to the mortgagee. The defendant having failed to pay the loan after four years, the plain tiff made several demands for payment which were unheeded.

Plaintiff filed this action for foreclosure of mortgage. Defendant argues that the true transaction was one of antichresis, and that as plaintiff has received several cavans of palay, from the mortgaged properties, valued at P5,200, his debt has already been paid. The trial court found the transaction to be a mortgage, and possession of the mortgagee of the properties did not alter the transaction. Defendant appealed.

Issue:

Whether or not the contract is one of mortgage or antichresis.

SC Ruling:

It is not an essential requisite of a mortgage that possession of the mortgaged premises be retained by the mortgagor. To be an antichresis, it must be expressly agreed between the creditor and the debtor that the former, having been given possession of the mortgaged properties, is to apply their fruits to the payment of the interest, if owing, and thereafter to the principal of his credit; so that if a contract of loan with security does not stipulate the payment of interest but provides for the delivery of the mortgaged property to creditor, in order that the latter may gather its fruits, without stating that said fruits are to be applied to the payment of interest, if any and afterwards that of the principal, the contract is mortgage and not an antichresis.

The contract, therefore, is true mortgage and not an antichresis. This conclusion however, does not mean that the plaintiff having received the fruits of said properties, will be allowed to appropriate them for himself and not be required to account for them to the defendant. The true possession of the plaintiff under the contract is a mortgage in possession or one who has acquired actual or constructive possession of the premises mortgaged to him, standing upon his rights as a mortgagee and not claiming under another title, for the purpose of enforcing his security upon his property or making its income help to pay the debt. As such mortgagee in possession his rights and obligations are similar to those of an antichretic creditor.

In the present case, the parties having agreed that the loan was to be without interest and the appellant not having expressly waived his right to the fruits of the mortgaged properties during the creditors possession, the latter like an antichretic creditor, must account for the value of the fruits received by him and deduct it from the loan obtained by the appellant.

Article 2136

- The debtor cannot demand the return of the property until the debt is totally paid
- However, if the creditor does not want to pay the taxes and incur the expenses necessary for the preservation and repair of the property, he may compel the debtor to reacquire the enjoyment of the same except when there is a contrary stipulation

Article 2139

- The following provisions are likewise applicable to antichresis:
 - o Article 2085
The following requisites are essential to the contracts of pledge and mortgage:
(1) That they be constituted to secure the fulfillment of a principal obligation;
(2) That the pledgor or mortgagor be the absolute owner of the thing pledged or mortgaged;
(3) That the persons constituting the pledge or mortgage have the free disposal of their property, and in the absence thereof, that they be legally authorized for the purpose.
Third persons who are not parties to the principal obligation may secure the latter by pledging or mortgaging their own property
 - o Article 2089
A pledge or mortgage is indivisible, even though the debt may be divided among the successors in interest of the debtor or of the creditor.
Therefore, the debtor's heir who has paid a part of the debt cannot ask for the proportionate extinguishment of the pledge or mortgage as long as the debt is not completely satisfied.
Neither can the creditor's heir who received his share of the debt return the pledge or cancel the mortgage, to the prejudice of the other heirs who have not been paid.
From these provisions is expected the case in which, there being several things given in mortgage or pledge, each one of them guarantees only a determinate portion of the credit.

The debtor, in this case, shall have a right to the extinguishment of the pledge or mortgage as the portion of the debt for which each thing is specially answerable is satisfied

- Article 2091

The contract of pledge or mortgage may secure all kinds of obligations, be they pure or subject to a suspensive or resolutive condition

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CHATTEL MORTGAGE

Articles 2140 – 2141

Article 2141

- The provisions of this Code on pledge, insofar as they are not in conflict with the chattel mortgage law shall be applicable to chattel mortgage

I. Concept

- Art. 2140: by a chattel mortgage, personal property is recorded in the Chattel Mortgage Register as a security for the performance of an obligation. If the movable, instead of being recorded, is delivered to the creditor or a third person, the contract is a pledge and not a chattel mortgage.

Old Law: Act No. 1508

- Chattel mortgage is a conditional sale of a personal property
- The object is either delivered to creditor or registered in the C.M. registry
- However in the new law, delivery is considered a pledge... this old law is superseded by the new law

II. Nature and Characteristics

A. Obligations that may be secured

- They must be constituted to secure fulfillment of a principal obligation.
 - They may secure all kinds of obligation, pure or conditional
 - The principal obligation may be future but the security obligation does not come into existence until the principal does.
 - The principal obligation may be natural, voidable, rescissible or unenforceable, provided the fact is known to the pledgor or mortgagor.
- These contracts can be constituted only by the absolute owner of the thing pledged or mortgaged.
- The one constituting the pledge or mortgage should have free disposal of the property or should be legally authorized for the purpose.
- Thing pledged or mortgaged may be alienated at the instance of the creditor for payment of the principal obligation.
- Pledge and mortgage are indivisible, even if the principal debt is divided.

Q: can C.M. serve past obligation or obligation concurrent with the mortgage deal or after the execution of the mortgage?

A: It can serve past obligation or obligation concurrent with the mortgage deal but NOT obligations after the execution of the mortgage. Dragnet clause is applicable only to real mortgage but not in chattel mortgage. If included in a C.M. such stipulation is void.

Q: What if aside from a DRAGNET CLAUSE, you include a promise that the property will secure future obligation, what is the creditor's remedy?

A: You demand for specific performance

Acme Shoe, Rubber and Plastic Corp. vs. CA
260 SCRA 714, August 22, 1996

Facts:

Petitioner contracted a three million peso loan from Producers Bank secured by a chattel mortgage. A provision of the chattel mortgage agreement was to the effect-

"In case the MORTGAGOR executes subsequent promissory note or notes either as a renewal of the former note, as an extension thereof, or as a new loan, or is given any other kind of accommodation such as overdrafts, letters of credit, acceptances and bills of exchange, releases of import shipments on Trust receipt etc. this mortgage shall also stand as a security for the payment of the said promissory note or notes or accommodations without the necessity of executing a new contract and this mortgage shall have the same force and effect as if the said promissory note or notes accommodations were existing on the date thereof. This mortgage shall also stand as security for said obligations and any and all other obligations of the MORTGAGOR to the MORTGAGEE of whatever kind and nature, whether such obligations have been contracted before, during or after the constitution of this mortgage"

Petitioner obtained from the bank additional financial accommodations. These borrowing were on due date also fully paid. Later, the bank yet again extended to petitioner loan of one million pesos covered by four promissory notes. Due to financial constraints, the loan was not settled at maturity. Respondent bank thereupon initiated foreclosure proceeding. Ultimately, the court ordered the foreclosure of the chattel mortgage. It held petitioner bound by the stipulations aforequoted, of the chattel mortgage.

SC Ruling:

Contracts of security are either personal or real. In contracts of personal security, such as guaranty or a suretyship, the faithful performance of the obligation by the principal debtor is secured by the personal commitment of another. In contracts of real security, such as pledge, mortgage, or antichresis, that fulfillment is secured by an encumbrance of the property-in pledge, the placing of movable property in the possession of the creditor in chattel mortgage, by execution of the corresponding deed substantially in the form prescribed by law; in real estate mortgage, by the execution of a public instrument encumbering the real property covered thereby; and in atechresis, by a written instrument granting to the creditor the right to receive the fruits of an immovable property with the obligation to apply such fruits to the payment of interest, if owing and thereafter to the principal of his credit-upon the essential condition that if the principal obligation becomes due and the debtor defaults, then the property encumbered can be alienated for the payment of the

obligation, but that should the obligation be fully paid, then the contract is automatically extinguished proceeding from the accessory character of the agreement. As the law so puts it, once the obligation is complied with, then the contract of security becomes ipso facto null and void.

While a pledge, real estate mortgage, or antichresis may exceptionally secure after-incurred obligation so long as these future debts are accurately described, a chattel mortgage however, can only cover obligations existing at the time the mortgage is constituted. Although a promise expressed in the chattel mortgage to include debts that are yet to be contracted can be a binding commitment that can be compelled upon, the security itself, however, does not come into existence or arise until after a chattel mortgage agreement covering the newly contracted debt is executed either by concluding a fresh chattel mortgage or by amending the old contract conformably with the form prescribed by the Chattel Mortgage Law. Refusal on the part of the borrower to execute the agreement so as to cover the after-incurred obligation can constitute as an act of default on the part of the borrower of the financing agreement wherein the promise is written, but of course the remedy of foreclosure can only cover the debts extant at the time of constitution and during the life of the chattel mortgage sought to be foreclosed.

The significance of the ruling to the instant problem would be that since the 1978 chattel mortgage has ceased to exist coincidentally with the full payment of the P3,000,000.00 loan., there no longer was any chattel mortgage that could cover the new loans that were concluded thereafter.

Chattel Mortgage is:

- An accessory contract
- A formal contract because of its validity, registration in the Chattel Mortgage Register is indispensable
- Unilateral because it produces only obligations on the part of the creditor to free the thing from the encumbrance on fulfillment of the obligation

Chattel Mortgage vs. Pledge

<u>CHATTEL MORTGAGE</u>	<u>PLEDGE</u>
The delivery of the personal property to the mortgagee is not necessary	Such delivery is necessary
The registration of the same in the chattel mortgage register is required by law	Registration in the registry of property is not necessary
Procedure for the sale is found in section 14 act no. 1508, as amended	It is found in article 2112 of the civil code
If the property is foreclosed, the excess over the amount due goes to the debtor	The debtor is not entitled to the excess unless it is otherwise agreed or except in the case of a legal pledge
If the property is foreclosed and there is a deficiency, the creditor is entitled to recover the deficiency from the debtor except if the chattel mortgage is a security for the purchase of personal property in installments	If the property is sold and there is a deficiency, the creditor is not entitled to recover the deficiency notwithstanding any stipulation to the contrary

Similarities:

1. Both are executed to secure performance of a principal obligation
2. ... constituted only on personal property
3. ... indivisible
4. ... constitute a lien on the property
5. ... creditor cannot appropriate the property to himself in payment of the debt
6. ... when the debtor defaults, the property must be sold for the payment of the creditor
7. ... extinguished by the fulfillment of the principal obligation or by the destruction of the property pledged or mortgaged

B. Elements

A. Parties

- The mortgagor must have capacity to encumber the property.

B. Object

- It may only be constituted on personal or movable property (Article 2140).
 - o This may include: (I-M-U-V-M-L-S)
 - Interest in a business
 - Machinery treated by the parties as personal property
 - Ungathered crops --- parties may stipulate this. Mortgagor may take care of the crops. If not mortgagee take over the cultivation
 - Vessels recorded in the office of the Philippine Coast Guard of the port of do
 - Motor vehicles but mortgage must also be registered in LTO
 - Certificates of stocks
 - Large cattle
 - Stock in trade

Note: Specific description of every chattel mortgaged in the deed of mortgage is not necessary. What is required is a description of the property be such as to enable the parties to the mortgage or any other person to identify the same after a reasonable investigation and property

Remember: "a chattel mortgage shall be deemed to cover only the property described therein and not like or substituted property thereafter acquired by the mortgagor and placed in the same depository as the property originally mortgaged, anything in the mortgage to the contrary notwithstanding."

- The above provision does not apply to stores open to the public for retail business where the goods are constantly sold and substituted with new stock, such a drugstores, grocery, etc. otherwise, it would be practically impossible to constitute to a mortgage on such stores without closing them contrary to the very spirit and purpose of the Act
- o A chattel mortgage over immovables is void.

- Exception: if the parties agree on constituting the chattel mortgage over an immovable, but it will not bind third parties.

Manarang vs. Ofilada
99 Phil.108, May 18, 1956

Facts:

Manarang obtained a 200 loan from Esteban and to secure payment she executed a chattel mortgage over a house of mixed materials. For non-payment of the loan, judgment was rendered against Manarang and execution was issued against the property mortgaged. Before the property could be sold, Manarang offered to pay the amount of the judgment with interest but refused to pay the publication expenses of the notice of sale in the two newspapers.

SC Ruling:

There can be no question that a building of mixed materials may be subject of a chattel mortgage, in which case it is considered as between the parties a personal property. But this does not make this house a personal property for the purpose of the notice to be given for its sale at public auction. Sales on execution affect the public and third persons. The regulations governing sales on execution are for public officials to follow. The form of the proceedings prescribed for each kind of property is suited to its character, not to the character which the parties have given to it or desire to give it.

TUMALAD V. VICENCIO
41 SCRA 143

Facts:

Vicencio and Simeon executed a chattel mortgage in favor of plaintiffs Tumulad over their house, which was being rented by Madrigal and company. This was executed to guarantee a loan, payable in one year with a 12% per annum interest.

The mortgage was extrajudicially foreclosed upon failure to pay the loan. The house was sold at a public auction and the plaintiffs were the highest bidder. A corresponding certificate of sale was issued. Thereafter, the plaintiffs filed an action for ejectment against the defendants, praying that the latter vacate the house as they were the proper owners.

SC Ruling:

Certain deviations have been allowed from the general doctrine that buildings are immovable property such as when through stipulation, parties may agree to treat as personal property those by their nature would be real property. This is partly based on the principle of estoppel wherein the principle is predicated on statements by the owner declaring his house as chattel, a conduct that may conceivably stop him from subsequently claiming otherwise.

In the case at bar, though there be no specific statement referring to the subject house as personal property, yet by ceding, selling or transferring a property through chattel mortgage could only have meant that defendant conveys the house as chattel, or at least, intended to treat the same as such, so that they should not now be allowed to make an inconsistent stand by claiming otherwise.

Makati Leasing and Finance Corp. vs. Wearever Textile Mills, Inc.
 122 SCRA 296, May 16, 1983

Facts:

In order to obtain financial accommodations from herein petitioner Makati Leasing and Finance Corporation, the private respondent Wearever Textile Mills, Inc. discounted and assigned several receivables with the former under a Receivable Purchase Agreement. To secure the collection of the receivables assigned, private respondent executed a chattel mortgage over certain raw materials inventory as well as machinery described as an Artos Aero Dryer Stentering Range.

SC Ruling:

If a house of strong materials, like what was involved in Tumald vs. Vicencio 41 SCRA 143, may be considered as personal property for purposes of executing a chattel mortgage thereon as long as the parties to the contract so agree and no innocent third party will be prejudiced thereby there is absolutely no reason why a machinery, which is movable in its nature and becomes immobilized only by destination or purpose, may not be likewise treated as such. This is really because one who has agreed is estopped from denying the existence of the chattel mortgage.

In rejecting petitioner's assertion on the applicability of the Tumalad doctrine, the Court of Appeals lay stress on the fact that the house involved therein was built on a land that did not belong to the owner of such house. But the law makes no distinction with respect to the ownership of the land on which the house is built and we should not lay down distinction not contemplated by law.

It must be pointed out that the characterization of the subject machinery as chattel by the private respondent is indicative of intention and impress upon the property the character determined by the parties. As stated in Standard Oil Co. of New York vs. Jaramillo, 44 Phil. 630, it is undeniable that the parties to a contract may by agreement treat as personal property that which by nature would be real property as long as no interest of third parties would be prejudiced.

C. Causa

- Same with the principal obligation.

D. Form

a. To bind the parties

- The instrument need only conform substantially to that form contained in section 5 of Act No. 1508. (it must be in a public document)

SECTION 5. Form. — A chattel mortgage shall be deemed to be sufficient when made substantially in accordance with the following form, and shall be signed by the person or persons executing the same, in the presence of two witnesses, who shall sign the mortgage as witnesses to the execution thereof, and each mortgagor and mortgagee, or, in the absence of the mortgagee, his agent or attorney, shall make and subscribe an affidavit in substance as hereinafter set forth, which affidavit, signed by the parties to the mortgage as above stated, and the certificate of the oath signed by the authority administering the same, shall be appended to such mortgage and recorded therewith.

Note: If the property is situated in a different province from that in which the mortgagor resides, the registration must be in both registers otherwise, the chattel mortgage is void. It has been ruled that if the chattel mortgage is not recorded, it is nevertheless binding between the parties

Q: what are the effects of registration?

A:

1. creates a real right – the registration of the chattel mortgage is an effective and binding notice to other creditors of its existence and creates a real right or a lien which, being recorded, follows the chattel whenever it goes. Registration gives the mortgagee symbolical possession
2. adds nothing to mortgage – registration operates as a constructive notice of the existence of the contract, and the legal effects of the contract must be discovered in the instrument itself in relation with the face of notice

b. To bind third persons – additional requirements

1. Affidavit of Good Faith – is an oath in a contract of chattel mortgage wherein the parties “severally swear that the mortgage is made for the purpose of securing the obligation specified in the conditions thereof and for no other purposes and that the same is a just and valid obligation and one not entered into for the purpose of fraud
 - Signed by mortgagor and mortgagee
 - Constituted to this particular valid debt and for no other purpose

Q: what is the effect of its absence?

A: the absence of the affidavit vitiates a mortgage only as against third persons without notice like creditors and subsequent encumbrancers. The special affidavit is required only for the purpose of transforming an already valid mortgage into “preferred mortgage”.

Q: if you take away the affidavit of good faith it is as if it is a private document. But look at 2140, it requires that the instrument be recorded in the registry. Will it be valid if contract is placed only in a private document?

A: Execution of a public document is NOT sufficient because the registration is what makes the mortgage valid. As provided for in 2130 --- It should be in a public document duly registered

GIBERSON VS. JUREIDINI BROS.

Facts:

H.K. Motoomul & Co. was, at the time mentioned in the complaint, a partnership doing business in the cities of Cebu and Iloilo. Sometime prior to May 24, 1921, the company became financially embarrassed. A.N. Jureidini Bros. Inc., a large creditor of Motoomul & Co., became aware of the precarious condition of the latter, because of the diminishing payments on account of debt. Ultimately, Motoomul & Co., delivered to Jureidini Brothers on May 24, 1921, one of the debtor's

Iloilo stores known as Bazar Aguila de Oro. On the same day also, credits receivables belonging to Motoomul & Co., passed to Jureidini Bros. The documents evidencing these transfers appear in the record.

Within thirty days after these assignments were made, or to be exact, on June 22, 1921, a number of creditors of the H.K. Motoomul & Co. initiated successfully involuntary insolvency proceedings against it. Later, action was brought by the receiver Giberson appointed by the court.

Issue:

W-O-N the chattel mortgage was valid.

SC Ruling:

The trial court held, and properly, that Exhibit 1 was invalid because the oath required by law did not appear therein, and because the subject-matter was not described therein with sufficient particularity. The Chattel Mortgage Law, in its section 5, in describing what shall be deemed sufficient to constitute a good chattel mortgage, includes the requirement of an affidavit of good faith appended to the mortgage and recorded therewith. It has been held by reputable courts that the absence of the affidavit vitiates a mortgage as against creditors and subsequent encumbrancers.

JACA VS. DAVAO LUMBER COMPANY

Facts:

Plaintiff Urbano Jaca, a licensee of a logging concession located in Davao City is engaged in a logging business. Defendant Davao Lumber Company (DLC) is a corporation with which plaintiffs had business dealings covering the sales of his logs.

Sometimes in 1954, the herein parties entered into an agreement whereby plaintiff may secure, by way of advances, either cash or materials, foodstuffs and/or equipment from the defendants. The payment was to be made either in cash and/or plaintiff's turning over his logs to the defendant, and in the latter case, the current price, either export or domestic, of the logs at the time of their delivery was to be considered.

While the relationship was subsisting, defendant made plaintiff execute in its favor a chattel mortgage, a copy of which instrument, however, plaintiff was never furnished.

In November 1963, plaintiff filed with the Davao CFI a complaint for Accounting Return of Price Differentials and Damages against the defendants.

Issue:

W-O-N the chattel mortgage was valid.

SC Ruling:

The defendant's proof of interest in the property is the deed of chattel mortgage executed by the plaintiff in its favor on January 24, 1964. This deed of chattel mortgage is void because it provides that the security stated therein is for the payment of any and all obligations herein before contracted and which may hereafter be contracted by the mortgagor in favor of the mortgagee. In the case of *Belgian Catholic Missionaries vs. Magallanes Press* (49 PHIL 647) this court held:

"A mortgage that contains a stipulation in regard to future advances in the credit will take effect only from the date the same are made and not from the date of the mortgage. x x x Where the statute provides that a parties to a chattel mortgage must take oath that the debt is a just debt, honestly due and owing from the mortgagor to the mortgagee, it is obvious that a valid mortgage cannot be made to secure a debt to be thereafter contracted".

Thus, petition granted.

CEBU INTERNATIONAL FINANCE CORPORATION VS. COURT OF APPEALS

Facts:

JD executed a special power of attorney in favor of AT, authorizing the latter to sell JD's cargo vessel. AT sold the vessel to RO who paid the purchase price by issuing checks. Since the payment was not made in cash, it was specifically stipulated in the deed of sale that the vessel shall not be registered to RO until full payment. RO obtained possession of the vessel and obtained copies of the unauthorized deed of sale purportedly to be shown to the bank for loan purposes. The condition, however, which was handwritten on the original, does not appear in his copies.

RO had his copies notarized and registered the sale in the Philippine Coast Guard without AT's knowledge. RO was issued a Certificate of Ownership and Certificate of Philippine Registry that enabled him to acquire a loan at CIFIC with the vessel as security. The chattel mortgage was duly registered and annotated. Upon default, CIFIC demanded delivery of the vessel, otherwise the mortgage shall be foreclosed or pay the balance. Meanwhile, the checks he issued to AT bounced. JD and AT sued for rescission and replevin with damages. The trial court ruled that the chattel mortgage was null and void and ordered CIFIC to pay AT damages. The Court of Appeals affirmed the decision, hence this petition for review on certiorari.

Issue:

W-O-N the chattel mortgage was valid.

SC Ruling:

The chattel mortgage is valid and subsisting. It should not be viewed in such a myopic context. The key lies in the certificate of ownership issued in RO's name. In the deed of absolute sale, it was also indicated that JD was the seller and RO was the buyer of the vessel. Coupled with the fact that there is no evidence of any transaction between JD or AT and CIFIC, it follows that CIFIC is a creditor-mortgagee and not owner-seller. The form contract used for simple loan with chattel mortgage was filled out by mistake. It is not improbable that such an oversight may have been committed negligently but unintentionally and without malice.

A mortgagee has a right to rely in good faith on the certificate of title of the mortgagor to the property given as security and in the absence of any sign that might arouse suspicion to undertake further investigation. Hence, even if the mortgagor is not the rightful owner of or does not have a valid title to the mortgaged property, the mortgagee or the transferee in good faith is nonetheless entitled to the property. Although this rule generally pertains to real property, particularly registered land, it may also be applied by analogy to personal property, in this case specifically, since shipowners are, likewise required by law to register their vessel with the Philippine Coast Guard.

The special affidavit of good faith is required only for the purpose transforming an already valid mortgage into a preferred mortgage. It is not necessary for the validity of the chattel mortgage itself.

Note: in REM, future obligation can be secured by present property. But in a CM, future property an obligations cannot be secured

2. Description of Property

- There is no need for all the specifics. For as long as you don't need to execute another contract to identify the property
- The test is the REASONABLE DESCRIPTION RULE
- Q: what if there is a catch all clause?
A: It is allowed if by ordinary investigation or analogy, you are still able to find those things.

SALDAÑA VS. PHIL. GUARANTY CO.

Facts:

Eleazar executed in favor of Saldaña, a chattel mortgage, the last paragraph of which states: *"and all other furnitures, fixtures, or equipment found in the said premises"*. Subsequent to the execution of said mortgage, defendant Hospital de San Juan de Dios obtained a judgment against Eleazar. Personal properties of Eleazar were levied upon. Saldaña filed a third-party claim asserting that the properties levied are subject to his chattel mortgage.

Issue: W-O-N there was sufficient description on the properties mortgaged.

SC Ruling:

There is merit in appellant's contention. Section 7 of the Chattel Mortgage Law does not demand a minute and specific description of every chattel mortgaged in the deed of mortgage but only requires that the description of the properties be such "as to enable the parties in the mortgage or any other person, after reasonable inquiry and investigation to identify the same". Gauged by this standard, general descriptions have been held valid by this court. The specification in the last paragraph of the deed in the instant case is in substantial compliance with the "reasonable description rule" fixed by the Chattel Mortgage Law.

The limitation found in Section 7, last paragraph, of the Chattel Mortgage Law on "like or substituted properties" makes reference to those "thereafter acquired by the mortgagor and placed in the same depository as the property originally mortgaged" not to those already existing and originally included at the date of the constitution of the chattel mortgage. A contrary view would unduly impose a more rigid condition than the law prescribes which is, that the description be only such as to enable identification after reasonable inquiry and investigation.

Orders set aside.

3. Registration

i. Place

General Rule: the registries of the place where the mortgagor resides and where the property is located. (note: it is VOID if you only register in one.)

- Except that of vessels must be registered in the office of the collector of customs of the port of documentation (where registered).
- Mortgage of shares of stock must be registered in the province where the corporation has its principal place of business.
- A mortgage over an automobile, in order to affect third persons, should be registered not only in the Chattel Mortgage Registry but also in the Motor Vehicles Office. The mortgagee's failure to annotate the mortgage in the said office renders it ineffective against a purchaser who registers the sale in the Motors Vehicles Office.

Note: there is no need to register in the Security Exchange Commission

C. Effect of Mortgage

A. What it covers

- The mortgage covers only the property described in the contract and excludes like or substituted property thereafter acquired, anything in the contract to the contrary notwithstanding.

a. Exception

- In the case of stock contained in stores, drugstores, or similar businesses of a "revolving or floating" nature.

D. Discharge of Mortgage

A. Requisites

- That there has been performance or tender of performance of the condition;
- That there has been a request for the discharge made by the person entitled to redeem.
*(how discharge is made? -- execute an affidavit of discharge to be recorded in the registry of deeds)

Note: if there is NO DISCHARGE, even if the obligation is extinguished, the mortgage continues to exist because you should REGISTER the discharge. Mortgagor may demand and mortgagee may be penalized

- B. Effect of failure to discharge within ten (10) days – the mortgagee is liable to pay twenty pesos (P20.00) and all damages occasioned thereby

Q: what is the right of subsequent mortgagor of a pervious valid mortgage?

A: Redeem the property from the first mortgagee

E. Redemption (before foreclosure)

A. Who may redeem

- The mortgagor;
- Subsequent mortgagees; (article 2085)
- Subsequent attaching creditors --- he shall be subrogated to the rights of the mortgagee and entitled to foreclose.

Note: if there is a violation of mortgage (default) but no foreclosure yet, subsequent mortgagee can redeem the property.

B. What must be paid

Q: how is redemption made?

A: by paying the:

- The principal obligation and interest thereon;
- Costs and expenses incurred by any breach, before the sale.

C. Effects of Redemption

- upon the sale of personal property at the foreclosure sale, all rights of ownership leave the mortgagor and become vested in the purchaser
- The redemptioner is subrogated to the rights of the mortgagee.
 - 1) He may, therefore, foreclose the mortgage in the same manner.

Note: There is no right to redeem personal property

F. Foreclosure

- the 30-day period to foreclose a chattel mortgage is the minimum period after the violation of the mortgage condition for the mortgage creditor to cause the sale at public auction the mortgaged chattel with at least 10 days notice to mortgagor and posting of public notice period of grace for the mortgagor to discharge the mortgage obligation.

A. Kinds

- a. Judicial
- b. Extra-judicial

1. REQUISITES:

- i. Sale at public auction thirty days after the debtors default (if the debtor refuses to surrender the chattel, action must be brought for its delivery).
- ii. Notice of sale to be posted in two (2) public places ten (10) days before the sale, and notice likewise to be given to the mortgagor in writing, personally or by mail.
- iii. Conducted by a public officer (sheriff).
- iv. Conducted in the municipality where the mortgagor resides OR where the property is located.

EXCEPT: when some other place is stipulated. ---- mortgages options

Note: the mere fact that the mortgagee was the sole bidder for the mortgaged property in the public sale does not warrant the conclusion that the transaction was attended with fraud. Fraud must be proved with full and convincing evidence.

2. DISPOSITION OF PROCEEDS:

- i. Application:
 - a) Costs and expenses of sale;
 - b) The principal obligation and interest;
 - c) Claims of subsequent mortgagees;
 - d) The balance, if any, to the mortgagor.
- ii. In case of deficiency:

- a) The mortgagee may still recover the deficiency from the mortgagor.

Case: In recto law, chattel over movable is sold under installment plan. There is no recovery of deficiency. Property is immediately delivered to the first bidder. Mortgagee was not file action for recovery of property

Case: Pameca Wood Treatment Plant vs. CA

- The theory of the lower court would lead to the absurd conclusion that if the chattels mentioned in the mortgage, given as security, should sell for more than the amount of the indebtedness secured, that the creditor would be entitled to the full amount for which it might be sold, even though that amount was greatly in excess of the indebtedness. Such a result certainly was not contemplated by the legislature when it adopted Act No. 1508. There seems to be no reason supporting that theory under the provision of the law. The value of the chattels changes greatly from time to time, and sometimes very rapidly. If, for example, the chattels should greatly increase in value and a sale under that condition should result in largely overpaying the indebtedness, and if the creditor is not permitted to retain the excess, then the same token would require the debtor to pay the deficiency in case of a reduction in the price of the chattels between the date of the contract and a breach of the condition

- iii. In case of sale of personal property on installment.

Art. 1484(NCC). In a contract of sale of personal property the price of which is payable in installments, the vendor may exercise any of the following remedies:

- (1) Exact fulfillment of the obligation, should the vendee fail to pay;
- (2) Cancel the sale, should the vendee's failure to pay cover two or more installments;
- (3) Foreclose the chattel mortgage on the thing sold, if one has been constituted, should the vendee's failure to pay cover two or more installments. In this case, he shall have no further action against the purchaser to recover any unpaid balance of the price. Any agreement to the contrary shall be void.

B. Right of Redemption

Case: Please refer to Paray vs. Rodriguez (cited in Pledge)

G. Distinctions

	PLEDGE	CHATTEL MORTGAGE	REAL ESTATE MORTGAGE	ANTICHRESIS
a. As to	On movables	On movables	On immovables	On immovables

OBJECT				
b. As to POSSESSION	By the creditor	By the debtor	By the debtor	By the creditor
c. As to PERFECTION	Real Contract	Formal Contract	Formal Contract	Formal contract
d. As to FORM to bind Third Persons	Public instrument containing description of the thing pledged and the date thereof	Recorded public instrument	Recorded public instrument	Recorded public instrument

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CONCURRENCE AND PREFERENCE OF CREDITS

Chapter 1 – General Provisions

Articles 2236 – 2240

I. Concept and General Theory

A. Concurrence

- Implies the Possession by two or more creditors of equal rights or privileges over the same property or all of the property of the debtor.

B. Preference

- Right held by a creditor to be preferred in the payment of his claim above others out of the debtor's assets.
- The rules apply when two or more creditors have separate and distinct claims against the *same* debtor who has insufficient property.

Note: this rule is an exception to the rule thus is strictly construed. Preference could not create an interest in property. It creates simply a right of one creditor to be paid first the proceeds of the sale of property as against another creditor.

It is not a question of who takes or sells; it is one of the application of the proceeds after the sale --- of payment of the debt.

Preference of Credit vs. Lien

A preference applies only to claims which do not attach to specific properties. A lien creates a charge on a particular property.

C. Property not subject to preference and concurrence

Property exempt from liability for fulfilment of obligation:

1. Present property – those provided under Arts. 155 and 205 of the Family Code, Sec. 13, Rule 39 of the Rules of Court, and Sec. 118 of the Public Land Act
2. Future property
3. Property under legal custody and those owned by municipal corporations necessary for governmental purposes

Note: This title refers to credits which are already due.

Chapter 2 – Classification of Credits

Articles 2241 – 2245

I. Classification of Credits

A. General Classification

- a.** Absolutely preferred – Government enjoys absolute preference over other creditors
- b.** Special Preferred Credits - those listed in Arts. 2241 and 2242 shall be considered as mortgages and pledges of real or personal property or liens (Art. 2243). Hence, they are not included in the insolvent debtor's assets.

Note: 2241 and 2242 do not give the order of preference or priority of payment. They merely enumerate the credits which enjoy preference with respect to specific movables or immovables.

With respect to the same specific movable or immovable, creditors, with the exception of the state (no. 1), merely concur. There is no preference among them; there is only concurrence.

- c.** Ordinary Preferred Credits - those listed in Art. 2244 as amended by Art. 110 of the Labor Code.
- d.** Common Credits – those listed under Art. 2245, which shall be paid pro rata regardless of dates.

Ordinary Preferred and Common Credits cover only “free property” of the debtor, or those not subjected to Special Preferred Credit.

B. As to specific movable property

- a.** Duties, taxes and fees due thereon to the State or any subdivision thereof
With reference to specific movable and immovable property of the debtor, the taxes due the State shall first be satisfied.
- b.** Claims arising from misappropriation, breach of trust, or malfeasance by public officials committed in the performance of their duties, on the movables, money or securities obtained by them
- c.** Claims for the unpaid price of movables sold, on said movables, so long as they are in the possession of the debtor, up to the value of the same; and if the movable has been resold by the debtor and the price is still unpaid, the lien may be enforced on the price; this right is not lost by the immobilization of the thing by destination, provided it has not lost its form, substance and identity; neither is the right lost by the sale of the thing together with other property for a lump sum, when the price thereof can be determined proportionally

- d.** Credits guaranteed with a pledge so long as the things pledged are in the hands of the creditor, or those guaranteed by a chattel mortgage, upon the things pledged or mortgaged, up to the value thereof
- e.** Reflectionary Credits
Indebtedness incurred in the repair or reconstruction of something previously made, such repair or reconstruction being made necessary by the deterioration or destruction of the thing as it formerly existed.
- f.** Claims for laborers' wages, on the goods manufactured or the work done
WORKER PREFERENCE IN CASE OF BANKRUPTCY. The law protects workers in case of bankruptcy or insolvency of the employer. This protection is established in Art. 110 of the Labor Code creating a "worker preference" in such an unlimited period, and covers not merely unpaid wages, but other monetary claims as well.
- g.** Other claims and Credits
 - For expenses of salvage, upon the goods salvaged;
 - Credits between the landlord and the tenant, arising from the contract of tenancy on shares, on the share of each in the fruits or harvest;
 - Credits for transportation, upon the goods carried, for the price of the contract and incidental expenses, until their delivery and for thirty days thereafter;
 - Credits for lodging and supplies usually furnished to travellers by hotel keepers, on the movables belonging to the guest as long as such movables are in the hotel, but not for money loaned to the guests;
 - Credits for seeds and expenses for cultivation and harvest advanced to the debtor, upon the fruits harvested;
 - Credits for rent for one year, upon the personal property of the lessee existing on the immovable leased and on the fruits of the same, but not on money or instruments of credit;
 - Claims in favor of the depositor if the depositary has wrongfully sold the thing deposited, upon the price of the sale.

C. Rules as to preferred credits on specific movables

- In the foregoing cases (above), if the movables to which the lien or preference attaches have been wrongfully taken, the creditor may demand them from any possessor, within thirty days from the unlawful seizure.
- The claims or credits enumerated in the articles 2241 and 2241 shall be considered as mortgages or pledges of real or personal property, or liens within the purview of legal provisions governing insolvency. Taxes mentioned in No. 1, Article 2241, and No. 1, Article 2242, shall first be satisfied.

Note: the last paragraph of 2241 applies only when the right of ownership in such property continues in the debtor, and therefore, it is not applicable to cases where the debtor has parted with his ownership therein, as where he sold the property.

D. As to specific immovable property (Art 2242)

The following claims, mortgages and liens shall be preferred, and shall constitute an encumbrance on the immovable or real right:

- (1) Taxes due upon the land or building;
- (2) For the unpaid price of real property sold, upon the immovable sold;
- (3) Claims of laborers, masons, mechanics and other workmen, as well as of architects, engineers and contractors, engaged in the construction, reconstruction or repair of buildings, canals or other works, upon said buildings, canals or other works;
- (4) Claims of furnishers of materials used in the construction, reconstruction, or repair of buildings, canals or other works, upon said buildings, canals or other works;
- (5) Mortgage credits recorded in the Registry of Property, upon the real estate mortgaged;
- (6) Expenses for the preservation or improvement of real property when the law authorizes reimbursement, upon the immovable preserved or improved;
- (7) Credits annotated in the Registry of Property, in virtue of a judicial order, by attachments or executions, upon the property affected, and only as to later credits;
- (8) Claims of co-heirs for warranty in the partition of an immovable among them, upon the real property thus divided;
- (9) Claims of donors of real property for pecuniary charges or other conditions imposed upon the donee, upon the immovable donated;
- (10) Credits of insurers, upon the property insured, for the insurance premium for two years.

E. Ordinary preferred credits (Art 2244)

- In contrast with 2241 and 2242, this article creates no liens on determinate property which follow such property. What 2244 creates are simply rights in favor of certain creditors to have the cash and other assets of the insolvent applied in a certain sequence or order of priority

With reference to other property, real and personal, of the debtor, the following claims or credits shall be preferred in the order named:

- (1) Compensation due the laborers or their dependents under laws providing for indemnity for damages in cases of labor accident, or illness resulting from the nature of the employment;
- (2) Credits for services rendered the insolvent by employees, laborers, or household helpers for one year preceding the commencement of the proceedings in insolvency;
- (3) Expenses during the last illness of the debtor or of his or her spouse and children under his or her parental authority, if they have no property of their own;
- (4) Proper funeral expenses for the debtor, or children under his or her parental authority who have no property of their own, when approved by the court;
- (5) Credits and advancements made to the debtor for support of himself or herself, and family, during the last year preceding the insolvency;
- (6) Support during the insolvency proceedings, and for three months thereafter;
- (7) Fines and civil indemnification arising from a criminal offense;
- (8) Legal expenses, and expenses incurred in the administration of the insolvent's estate for the common interest of the creditors, when properly authorized and approved by the court;
- (9) Taxes and assessments due the national government, other than those mentioned in Articles 2241, No. 1, and 2242, No. 1;
- (10) Taxes and assessments due any province, other than those referred to in Articles 2241, No. 1, and 2242, No. 1;
- (11) Taxes and assessments due any city or municipality, other than those indicated in Articles 2241, No. 1, and 2242, No. 1;

- (12) Damages for death or personal injuries caused by a quasi-delict;
- (13) Gifts due to public and private institutions of charity or beneficence;
- (14) Credits which, without special privilege, appear in (a) a public instrument (ex. Mortgage); or (b) in a final judgment, if they have been the subject of litigation. These credits shall have preference among themselves in the order of priority of the dates of the instruments and of the judgments, respectively.
- (15) unsecured creditors

Note: in a rehabilitation proceedings – workers have no preferred claims (proceedings will not be entertained)

Chapter 3 – Order of Preference of Credits

Articles 2246 – 2251

I. Order of payment

A. Resume:

a. Absolutely preferred credits

Arts. 2241 and 2242, jointly with Arts. 2246 and 2249 establish a *two-tier order of preference*:

1. First tier – includes taxes, duties and fees due the State or any subdivision thereof, on specific movable or immovable property (Absolutely preferred);
2. Second tier – all other special preferred (non-tax) credits shall be satisfied pro-rata, out of any residual value of the specific property to which such credits relate.

b. Specially preferred credits

1. As to specific chattels
2. As to specific immovables

The pro-rata rule does not apply to credits annotated in the Registry of Property by virtue of a judicial order, by attachments and executions, which are preferred as to later credits.

c. Ordinary preferred credits

Art. 2250. The excess, if any, after the payment of the credits which enjoy preference with respect to specific property, real or personal, shall be added to the free property which the debtor may have, for the payment of the other credits (Ordinary preferred credits).

d. Non-preferred credits

Art. 2251. Those credits which do not enjoy any preference with respect to specific property, and those which enjoy preference, as to the amount not paid, shall be satisfied according to the following rules:

- (1) In the order established in Article 2244;
- (2) Common credits referred to in Article 2245 shall be paid pro rata regardless of dates.

Credits which do not enjoy any preference with respect to specific property because they

are not among those mentioned in Arts. 2241 and 2242 and those while included in said articles are unpaid because the value of the property to which the preference refers is less than the preferred credit or credits, shall be satisfied in the order established in Art. 2244 with reference to other real and/or personal property.

Common credits or those which do not fall under Arts. 2241, 2242, and 2244 do not enjoy any preference and shall be paid pro rata regardless of dates.