

**Far Eastern University Institute of Accounts, Business &
Finance**

Law on Obligations and Contracts in the Philippines

An Overview

By: Atty. Christine P. Carpio-Aldeguer



April 19, 2014

INTRODUCTION

To begin, the Law on Obligations and Contracts is defined as s a kind of positive law which deals with the nature and sources of obligations as well as the rights and duties arising from agreements in contracts.¹

Before discussing the particular concepts on the Law on Obligations and Contracts, it is important to know that in every obligation, one must always observe the general principles on human relations, to wit:

“ART. 19. Every person must, in the exercise of his rights and in the performance of his duties, act with justice, give everyone his due, and observe honesty and good faith.”²

Failure to observe the above principle makes a person civilly liable.

Basic provisions on Law on Obligations and Contracts based on the Civil Code of the Philippines will be tackled in this paper. Cases and applications related to business will also be discussed.

OBLIGATION

The Law

Article 1156. An obligation is a juridical necessity to give, to do or not to do.

Discussion of the Law

An obligation is a legal duty, however created, the violation of which may become the basis of an action of law.³

¹ -- De Leon, Law on Obligations and Contracts, 1995 Revised Edition, Rex Bookstore, page 14.

² -- Civil Code of the Philippines.

Every obligation has four definite elements, without which no obligation can exist, to wit: (1) an active subject, also known as the obligee or creditor, who has the power to demand the prestation; (2) a passive subject, also known as the debtor, who is bound to perform the prestation; (3) an object or the prestation, which is an object or undertaking to give, to do or not to do; (4) The juridical or legal tie, the vinculum which binds the contracting parties. The juridical tie or vinculum is based on the sources of obligation arising from either the law or contract. Law is defined as a rule of conduct, just and obligatory, promulgated by the legitimate authority, for common observance and benefit.⁴ On the other hand, contract is defined as “meeting of minds between two persons whereby one binds himself, with respect to the other, to give something or render service.”⁵

It is important to identify the prestation in a certain obligation. Once the prestation is identified, you can determine who the passive subject is whom the active subject can demand fulfillment of the obligation.

A contract of sale and a contract of loan are examples of prestations to give; A contract of labor or a service contract is an example of a prestation to do.

To illustrate:

In an obligation to pay taxes, the passive subject is the taxpayer, the active subject is the government through the Bureau of Internal Revenue, the prestation is “to give,” specifically to pay taxes, the juridical tie is a source of obligation arising from law.

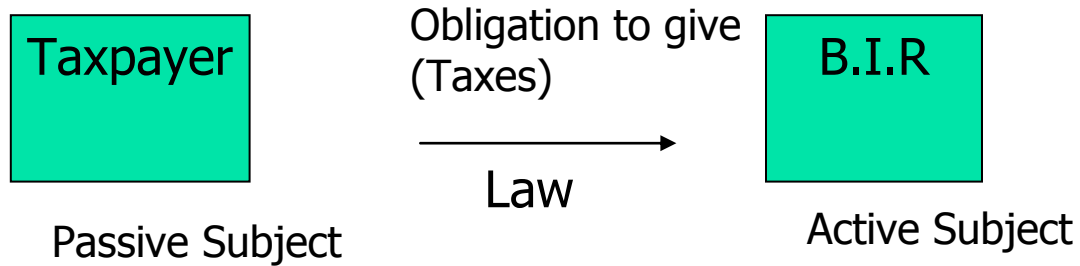
In an obligation to give Avon Products, the passive subject is the seller, the active subject is the buyer, the prestation is “to give,” specifically to deliver the Avon Products, and the juridical tie is a source of obligation arising from contract.

³ -- The Philippine Legal Encyclopedia, by Jose Agaton R. Sibal, 1986 edition, page 635.

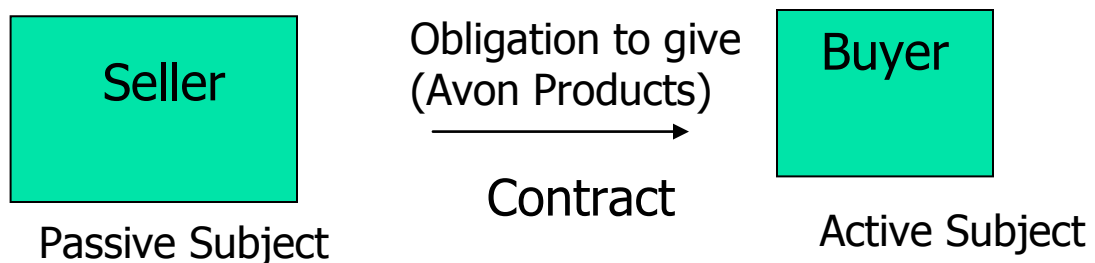
⁴ -- Hector De Leon, Law on Obligations and Contracts, 1995 Revised Edition, Rex Bookstore, page 5.

⁵ -- Article 1305, Civil Code of the Philippines.

Obligation arising from LAW:



Obligation arising from CONTRACT:



The Law

Article. 1157. Obligations arise from:

- (1) *Law;*
- (2) *Contracts;*
- (3) *Quasi-contracts;*
- (4) *Acts or omissions punishable by law; and*
- (5) *Quasi-delicts.* ⁶

Discussion of the Law

There are only two (2) sources of obligations, namely: (1) law; and (2) contracts because obligations arising from quasi-contracts, crimes (No. 4, Article 1157, Civil Code of the Philippines), and quasi-delicts are really imposed by law. (*Leung Ben vs. O'Brien*, 38 Phil. 182).

A contract is a "meeting of the minds between two persons whereby one binds himself, with respect to the other, to give something or to render some service."⁷

⁶ -- Civil Code of the Philippines

Quasi-contract refers to a lawful, voluntary and unilateral act based on the maxim that no one shall unjustly enrich himself at the expense of another.⁸ The two common forms of quasi-contract are: (1) *Solutio indebiti*, which is payment by mistake; (2) *Negotiorum gestio*, which takes place when a person without the consent of the owner, assumes the management of an abandoned business; (3) Article 2169 (NCC)– Government undertaking to do necessary work; and (4) Article 2175 (NCC) – Constrained to pay taxes of another.

Civil obligations arising from criminal offenses are governed: (1) by the provisions of the Revised Penal Code (i.e. restitution, reparation of the damage caused, indemnification of consequential damages; (2) by the provisions of the Civil Code on damages (i.e. moral, exemplary and nominal damages).

Quasi-delict (also called *culpa aquiliana*) is any act or omission which causes damage to another, there being fault or negligence, and there being no preexisting contractual relation between the parties.⁹

The following are some who may be liable for damages arising from quasi delict:

- The owners and managers of an establishment with respect to damage caused by their employees in the service of their branches in which the latter are employed or on the occasion of their function.
- Employers, with respect to damages caused by their employees or household helpers acting within the scope of their assigned tasks.

In order to escape liability on the ground of quasi-delict, one must prove diligence of a good father of a family to prevent the damage.¹⁰

⁷ -- Article 1305, Civil Code of the Philippines.

⁸ -- Refer to Article 2142, Civil Code of the Philippines.

⁹ -- Philippine Legal Encyclopedia, by Jose Agaton R. Sibal, page 809.

¹⁰ -- See Article 2180, Civil Code of the Philippines

Application of the Law

Case: Anabel was crossing the street coming from the hotel to the nearby shopping mall. She was accidentally hit by a hotel car driven by Leandro, a driver employed by the hotel. Can Anabel sue to driver? Can she sue the hotel?

Legal Opinion: Yes, Anabel may sue the driver and the hotel for damages on the ground of *culpa-aquiliana*. The pedestrian may also sue the driver and the owner of the hotel for damages for reckless imprudence arising from a crime under the Revised Penal Code.

Nature and Effects of Obligations

The following are the rights available to a creditor in obligations to give:

If it is a determinate thing:

1. To compel specific performance
2. To recover damages in case of breach
3. Acquires personal right to the fruits of the thing from the time the obligation to deliver arises
4. Acquires real right over the thing once the thing has been delivered to him
5. Rights over the accessories and accessions.

If it is a generic thing:

1. To ask for performance of the obligation
2. To ask that the obligation be complied with at the expense of the debtor.

A determinate thing is one that is particularly designated or physically segregated from all others of the same class.¹¹ A generic thing is one whose determination is confined to that of its nature, to the genus to which it pertains such as a horse, a chair.¹² A contract of sale uses a determinate thing, while a contract of loan uses a generic thing.

The following are the obligations of the passive subject in:

¹¹ -- Article 1460, Civil Code of the Philippines

¹² -- De Leon vs. Soriano, 87 Phil. 196.

a) Obligations to give a determinate thing:

1. To deliver the thing which he has obligated himself to give.¹³
2. To take care of the thing with the proper diligence of a good father of a family.¹⁴
3. To deliver all its accessories and accessions.¹⁵
4. To pay damages in case of breach of obligation.¹⁶

b) Obligations to do:

1. If the debtor fails to do what he is obliged to do, it will be done at his expense.
2. If the work is done in contravention of the tenor of the obligation, it will be re-done at debtor's expense.
3. If the work is poorly done, it will be re-done at debtor's expense.¹⁷

In obligations to do, you will note that you cannot compel the passive subject to perform, otherwise, it will constitute involuntary servitude which is in violation of the Constitution. However, the passive subject may be held liable for damages.

The sources of liability (for damages)¹⁸ of a party in an obligation are as follows:

(1) Fraud. The fraud is incidental fraud (*dolo incidente*) which is fraud incident to the performance of an obligation. In fraud, there is an intent to evade the normal fulfillment of the obligation and to cause damage.

¹³ -- Article 1165, Civil Code of the Philippines

¹⁴ -- Article 1163, Civil Code of the Philippines.

¹⁵ -- Article 1166, Civil Code of the Philippines.

¹⁶ -- Article 1170, Civil Code of the Philippines.

¹⁷ -- Article 1167, Civil Code of the Philippines.

¹⁸ -- Refer to Articles 2199-2201 of the Civil Code of the Philippines.

The fraud is causal (*dolo causante*) or when fraud used to induce a person to agree to a contract. This kind of fraud is a ground for annulment of the contract plus damages;

(2) Negligence. The negligence referred here, in the case of contracts (i.e. common carrier) is culpa contractual, the lack of diligence or carelessness. Negligence consists in the omission of that diligence which is required by the nature of the obligation and corresponds with the circumstances of the persons, or the time and of the place.

Application of the Law

Case: Dr. Felipa Pablo, an associate professor in the University of the Philippines, and a research grantee of the Philippine Atomic Energy Agency was invited to take part at a meeting of the Department of Research and Isotopes of the Joint FAO-IAEA Division of Atomic Energy in Food and Agriculture of the United Nations in Ispra, Italy. To fulfill this engagement, Dr. Pablo booked passage with Alitalia, an Italian airline company. She arrived in Milan on the day before the meeting in accordance with the itinerary and time table set for her by Alitalia. She was however told by the Alitalia personnel there at Milan that her luggage was "delayed inasmuch as the same x x x (was) in one of the succeeding flights from Rome to Milan."

Her luggage consisted of two (2) suitcases: one contained her clothing and other personal items; the other, her scientific papers, slides and other research material. But the other flights arriving from Rome did not have her baggage on board.

Feeling desperate, she went to Rome to try to locate her bags herself. There, she inquired about her suitcases in the domestic and international airports, and filled out the forms prescribed by Alitalia for people in her predicament. However, her baggage could not be found. Completely distraught and discouraged, she returned to Manila without attending the meeting in Ispra, Italy.

As it turned out, Dr. Pablo's suitcases were, in fact, located and forwarded to Ispra, Italy, but only on the day after her scheduled appearance and participation at the U.N. meeting there. Of course, Dr. Pablo was no longer there to accept delivery; she was already on her way home to Manila. And for some reason, the suitcases were not actually restored to Prof. Pablo by Alitalia until eleven (11) months later.

Is Dr. Pablo entitled to damages for the negligence committed by Alitalia?

Legal Opinion: Yes, Prof. Pablo should be entitled to nominal damages. Apart from this, there can be no doubt that Dr. Pablo underwent profound distress and anxiety, which gradually turned to panic and finally despair, from the time she learned that her suitcases were missing up to the time when, having gone to Rome, she finally realized that she would no longer be able to take part in the conference. As she herself put it, she "was really shocked and distraught and confused." Certainly, the compensation for the

injury suffered by Dr. Pablo cannot under the circumstances be restricted to that prescribed by the Warsaw Convention for delay in the transport of baggage.¹⁹

(3) Delay (Mora). The debtor can be held liable for the delay or default in the fulfillment of his obligation only after the creditor has made a demand, judicial or extrajudicial, on the debtor, except:

- When the law expressly provides that demand is not necessary;
- When the contract expressly stipulates that demand is not necessary;
- When time is of the essence;
- When demand would be useless.

In a contract of loan, if a particular rate of interest has been expressly stipulated by the parties, such stipulated interest shall be applied. If the exact rate of interest is not mentioned, the legal rate shall be payable (which is 12% per annum under Sec. 1 of the Usury Law).

It is only in contracts of loan, with or without security, that interest may be stipulated and demanded. This interest by way of compensation, must be in writing, otherwise, no interest by way of compensation may be collected.

The debtor in delay is also liable to pay legal interest by way of indemnity for damages, which interest may be agreed upon, and in the absence of any stipulation, the legal interest shall be 12% per annum.

In all cases, interest due shall earn legal interest from the time it is judicially demanded although the obligation may be silent upon this point.

(4) Contravention of the tenor of the obligation. Performance in contravention of the tenor or terms of the obligations means where performance is contrary to what is agreed upon or stipulated thus making the debtor liable for damages.²⁰

¹⁹ -- Alitalia vs. Intermediate Appellate Court, G.R. No. 71929, December 4, 1990.

²⁰ -- Article 1170, Civil Code of the Philippines.

Application of the Law

Case: This is an action for damages for alleged breach of contract. Nicolas L. Cuenca, then Commissioner for Public Highways of the Republic of the Philippines filed a case against Northwest Airlines, Inc. The facts reveal that Mr. Cuenca boarded Northwest Airlines in Manila with a first class ticket to Tokyo. Upon arrival at Okinawa, Mr. Cuenca was transferred to the tourist class compartment. Although he revealed that he was traveling in his official capacity as official delegate of the Republic to a conference in Tokyo, an agent of Northwest Airlines rudely compelled him, in the presence of other passengers, to move, over his objection, to the tourist class, under threat of otherwise leaving him in Okinawa. In order to reach the conference on time, respondent had no choice but to obey. Is Mr. Cuenca entitled to damages for culpa contractual?

Legal Opinion: Yes, Mr. Cuenca is entitled to nominal damages. At any rate, considering that petitioner's agent had acted in a wanton, reckless and oppressive manner, said award may, also, be considered as one for exemplary damages.²¹

Case: Mr. Rafael Carrascoso is a civil engineer who was a member of a group of 48 Filipino pilgrims that left Manila for Lourdes on March 30, 1958. On March 28, 1958, Air France, through its authorized agent, Philippine Air Lines, Inc., issued to Mr. Carrascoso a 'first class' round trip airplane ticket from Manila to Rome. From Manila to Bangkok, Mr. Carrascoso traveled in 'first class', but at Bangkok, the Manager of the Air France airline forced him to vacate the 'first class' seat that he was occupying because there was a 'white man', who, the Manager alleged, had a 'better right to the seat.' When asked to vacate his 'first class' seat, Mr. Carrascoso, as was to be expected, refused. A commotion ensued but Mr. Carrascoso reluctantly gave his 'first class' seat in the plane." In its defense, Air France alleged that although Mr. Carrascoso was issued a first-class ticket, it was no guarantee that the passenger to whom the same had been issued would be accommodated in the first-class compartment, for the passenger has yet to make arrangements upon arrival at every station for the necessary first class reservation.

Is Mr. Carrascoso entitled to the 'first-class' seat? Is Mr. Carrascoso entitled to damages?

Legal Opinion: Mr. Carrascoso should have been entitled to the 'first-class' seat and must not have been forced by the Airline Manager to vacate his seat. There was a contract to furnish Mr. Carrascoso a first class passage. The reservation for a 'first class' accommodation for him was confirmed. Hence, said contract was breached when Air France failed to furnish first class transportation. As a rule, a written document speaks a uniform language. If only to achieve stability in the relations between passenger and air carrier, adherence to the ticket so issued is desirable.

Lastly, passengers do not contract merely for transportation. They have to be treated by the carrier's employees with kindness, respect, courtesy and due consideration. They are entitled to be protected against personal misconduct, injurious

²¹ -- Northwest Airlines, Inc. vs. Cuenca, G.R. No. L-22425, August 31, 1965.

language, indignities and abuses from such employees. Any rude or discourteous conduct on the part of employees towards a passenger gives the latter an action for damages against the carrier. There was bad faith when the employee of Air France forced Mr. Carrasco to leave his first class accommodation berth "after he was already seated" and to take a seat in the tourist class, by reason of which he suffered inconvenience, embarrassment and humiliation, thereby causing him mental anguish, serious anxiety, wounded feelings and social humiliation, resulting in moral damages. In addition, exemplary damages are well awarded. The Civil Code gives the Court ample power to grant exemplary damages — in contracts and quasi-contracts. The only condition is that defendant should have "acted in a wanton, fraudulent, reckless, oppressive, or malevolent manner." The manner in which Mr. Carrasco was ejected from his first class seat fits into this legal precept.²²

Rule when a determinate thing is lost through a fortuitous event:

The obligation is extinguished and the debtor is not liable, except:

- a) When the object is generic
- b) When the debtor incurs in delay
- c) When the law or contract expressly provides that the obligation will not be extinguished.

Effect when goods are lost through a fortuitous event in a contract of sale:

- Before perfection of a contract – the seller bears the loss.
- After perfection but before delivery – the seller bears the loss as he remains to be the owner. There is no transfer of ownership until there is delivery of the goods. In case down payment has been made before delivery, the buyer may recover the price. Since a contract of sale is reciprocal in nature, once the obligation to deliver is extinguished, the correlative obligation to pay the price must also be extinguished. This is also based on equity and justice and in line with the principle of "res perit domino"
- After the delivery – buyer bears the loss as he now becomes the owner

²² -- Air France vs. Carrasco, G.R. No. L-21438, September 28, 1966, 18 SCRA 155.

Remedies of the Creditor against his debtor:

1. Sue the debtor for collection;
2. Attachment of debtor's property, real or personal, except those which are exempt from execution;
3. Exercise all the rights and actions which the debtor may have against third persons, except those which are inherently personal to the debtor;
4. To impugn or contest acts of debtor which are intended to defraud his creditor (Action pauliana);

Transmissibility of rights:

Subject to such laws, all rights acquired by virtue of an obligation are transmissible. Heirs shall be liable only to the extent of what they stand to inherit.

Exceptions:

- 1) When the law prohibits transmission of rights
- 2) When the contract stipulates no transmission of rights
- 3) When the nature of the obligation does not permit transmission of rights, as when the obligation is personal in nature.

The Law**Classification of Obligations****(1) Primary classification of obligations under the Civil Code:**

- (a) Pure and conditional obligations (Articles 1179-1192);
- (b) Obligations with a period (Articles 1193-1198);
- (c) Alternative (1199-1205) and facultative obligations (Article 1206);
- (d) Joint and solidary obligations (Articles 1207-1222);
- (e) Divisible and indivisible obligations (Articles 1223-1225); and
- (f) Obligations with a penal clause (Articles 1226-1230)

(2) Secondary classification of obligations under the Civil Code:

- (a) Unilateral and bilateral obligations (Articles 1169-1191);
- (b) Real and personal obligations (Articles 1163-1168);

- (c) Civil and natural obligations (Articles 1423); and
- (d) Legal, conventional, and penal obligations (Articles 1157, 1159, 1161)

Discussion of the Law

A pure obligation is one which is not subject to any condition and no specific date is mentioned for its fulfillment and is, therefore, immediately demandable.

Example: Ariel promises to pay Brenda P1,000.

A conditional obligation is one whose consequences are subject in one way or another to the fulfillment of a condition. Example: Carol promises to pay B P1,000.00 if Darren remains to become an outstanding employee of the hotel for the month of May.

A condition is defined as future and uncertain event which may or may not happen.

The following are the different kinds of condition:

- Suspensive Condition– the happening of which gives rise to an obligation
- Resolutive Condition – the happening of which extinguishes the obligation
- Potestative condition – where the fulfillment depends upon one’s will (either the debtor, creditor or a third person)
- Casual condition – when the fulfillment of the condition depends upon chance
- Mixed condition – when the fulfillment of the condition depends partly upon one’s will and partly upon chance.
- Impossible Condition – that which is not capable of fulfillment because it is contrary to the law of nature or contrary to law, morals, public order or public policy.

An obligation with a period is one whose consequences are subject in one way or another to the expiration of the said period or term.²³ Example: Alfredo (the owner of the hotel) promises to pay Britney (employee of the hotel) P5,000.00 on or before December 30, 2007 as part of the staff incentive program. A judicial period is a period

²³ -- Philippine Legal Encyclopedia, by Jose Agaton R. Sibal, page 639.

which is fixed by the courts. The courts are empowered to fix the duration of a period in an obligation in the following instances:

1. If the debtor binds himself when his means permit him to do so.
2. If the obligation does not fix a period but it can be inferred that a period was intended by the parties.

Joint obligations are those where, although there concur two or more creditors and debtors, in one and the same obligation, there is no right to demand nor a duty on the part of each of the latter to render entire compliance of the entire obligation.

Solidary obligations are those in which concur several debtors or creditors or both, and where each creditor has the right to demand, and each debtor is bound to perform, in its entirety, the prestation constituting the object of the obligation. The term “joint and several” used in contracts is applied to liability in an obligation made by several obligors when the obligee may at his option hold one or all liable together. However, this situation arises only when the obligation expressly so states or when the law or nature of the obligation requires solidarity.²⁴

The contract is presumed to be joint unless the obligation expressly states for its solidarity; or when the law expressly provides for its solidarity. The term “joint and several” used in contracts is applied to liability in an obligation made by several obligors when the obligee may at his option hold one or all liable together. Situations where the law expressly states solidarity are as follows:

- When by any wrongful act or omission caused by a partner acting in the course of the business of the partnership against a third person, the partnership and the partner so acting is liable. ²⁵

²⁴ -- Article 1207, Civil Code of the Philippines.

²⁵ -- Article 1882, Civil Code of the Philippines

- When a partner acting within the scope of his authority receives money and misapplies it, or misapplies the money received by the partnership, the partnership is solidarily liable with the partner.²⁶
- Solidary liability of the directors and trustees of corporation who are guilty of gross negligence or bad faith in directing the affairs of the corporation.²⁷
- Solidary liability of a labor-only contracting and the indirect employer.²⁸

Application of the Law

Case: Mr. Danny Ramos, owner of Danny's Grill (a fine dining restaurant), entered into a contract with Chona Romulo and Michael Aldeguer (proprietors of CM Wine Company) with the following stipulation:

“In case of failure to deliver the agreed 150 bottles of Emperor's White Wine on or before December 30, 2007, Chona Romulo and Michael Aldeguer shall be liable to Dan Ramos, joint and severally, for damages in the total amount of P100,000.00.”

CM Wine Company was not able to fulfill their obligation to Mr. Ramos. For three days that the wines were not delivered, many complaints arose from dining customers for wines ordered that were out of stock. Can Mr. Ramos only hold Mr. Aldeguer liable for damages?

Legal Opinion: In this situation, Mr. Danny Ramos may at his option hold either Chona Romulo or Michael Aldeguer, or both liable when filing a case in court for damages incurred.

An obligation with a penal clause is an obligation which contains an accessory obligation imposing upon the obligor added burdens or which operates as a previously stipulated indemnity, for the purpose of securing the performance of the principal obligation. It substitutes the indemnity for damages and, therefore, it does away with proof of damages suffered in case of breach of the obligation.²⁹ Obligations with a penal clause may be seen from contracts of loan with mortgage, and service contracts.

²⁶ -- Article 1883, Civil Code of the Philippines.

²⁷ -- Section 31, Corporation Code of the Philippines.

²⁸ -- Labor Code of the Philippines.

²⁹ -- Handbook on Obligations and Contracts, by Jose N. Nollado, 1993 Revised Edition, page 138.

The penalty shall substitute the indemnity for damages and the payment of interest in case of non-compliance, if there is no stipulation to the contrary. Damages (Exemplary damages) as well as the penalty (liquidated damages) shall be recovered if obligor refuses to pay the penalty or when the obligor is guilty of fraud.

Case: On January 30, 1911, a firm known as JR & Company, engaged in a retail garment business, found itself in such difficult financial condition that its creditors, Mr. Lambert and Mr. Fox, together with many others, agreed to take over the business, incorporate it and accept stocks therein in payment of their respective credits. When this was done, Mr. Lambert and Mr. Fox became the two largest stockholders in the new corporation called JR & Co., Incorporated. A few days after the incorporation was completed, Mr. Lambert and Mr. Fox entered into the following agreement:

"Whereas the undersigned are, respectively, owners of large amounts of stock in JR & Co., Inc.; and,

"Whereas it is recognized that the success of said corporation depends, now and for at least one year next following, in the larger stockholders retaining their respective interests in the business of said corporation:

"Therefore, the undersigned mutually and reciprocally agree not to sell, transfer, or otherwise dispose of any part of their present holdings of stock in said JR & Co., Inc., until after one year from the date hereof.

"Either party violating this agreement shall pay the other the sum of one thousand (P1,000) pesos as liquidated damages, unless previous consent in writing to such sale, transfer, or other disposition be obtained."

Notwithstanding this contract, Mr. Fox on October 19, 1911, sold his stock in the said corporation to E. D. McCullough of the firm of E. C. McCullough & Co. of Manila, a strong competitor of the said JR & Co., Inc. This sale was made by Mr. Fox against the protest of Mr. Lambert and with the warning that he would be held liable under the contract hereinabove set forth and in accordance with its terms.

Is Mr. Lambert entitled to the liquidated damages in the amount of P1,000.00?

Legal Opinion: Yes, Mr. Lambert is entitled to the liquidated damages in the amount of P1,000.00. In this jurisdiction penalties provided in contracts of this character are enforced. It is the rule that parties who are competent to contract may make such agreements within the limitations of the law and public policy as they desire, and that the courts will enforce them according to their terms. (Civil Code, articles 1152, 1153, 1154, and 1155; Fornow vs. Hoffmeister, 6 Phil. Rep., 33; Palacios vs. Municipality of Cavite, 12 Phil. Rep., 140; Gsell vs. Koch, 16 Phil. Rep., 1). The only case recognized by the Civil Code in which the court is authorized to intervene for the purpose of reducing a penalty stipulated in the contract is when the principal obligation has been partly or irregularly fulfilled and the court can see that the person demanding the penalty has

received the benefit of such part or irregular performance. In such case the court is authorized to reduce the penalty to the extent of the benefits received by the party enforcing the penalty. In this jurisdiction, there is no difference between a penalty and liquidated damages, so far as legal results are concerned. Whatever difference exists between them as a matter of language, they are treated the same legally. In either case the party to whom payment is to be made is entitled to recover the sum stipulated without the necessity of proving damages. Indeed one of the primary purposes in fixing a penalty or in liquidating damages, is to avoid such necessity.

The suspension of the power to sell has a beneficial purpose, results in the protection of the corporation as well as of the individual parties to the contract, and is reasonable as to the length of time of the suspension.³⁰

The implied power to rescind reciprocal obligations

The Law

“ART. 1191. The power to rescind obligations is implied in reciprocal ones, in case one of the obligors should not comply with what is incumbent upon him.

“The injured party may choose between the fulfillment and the rescission of the obligation, with the payment of damages in either case. He may also seek rescission, even after he has chosen fulfillment, if the latter should become impossible.

“The courts shall decree the rescission claimed, unless there is a just cause authorizing the fixing of a period.”³¹

Discussion

This article applies only to reciprocal obligations and there is no express power to rescind.

If one of the parties in reciprocal obligations fails to comply with what is incumbent upon him, there is a right on the part of the other to rescind.

Rescission (Cancellation) can be demanded only if plaintiff is ready, willing and able to comply with his own obligation and the other is not. Slight breaches will not

³⁰ -- Lambert vs. Fox, G.R. No. 7991, January 29, 1914.

³¹ -- Civil Code of the Philippines.

cause rescission. The right to rescind needs judicial approval if there has been delivery. If there is no delivery, judicial approval is not necessary.

The right to rescind is presumed, hence need not be express. The following are the choices of the creditor in enforcing his rights. These choices are alternative, not simultaneous:

1. Specific performance + damages
2. Rescission + damages

The Law

Modes of Extinguishing Obligations

Article 1231. Obligations are extinguished:

- i. By payment or performance;*
- ii. By the loss of the thing due;*
- iii. By the condonation or remission of the debt;*
- iv. By the confusion or merger of the rights of the creditor and debtor;*
- v. By compensation; and*
- vi. By novation;*

Other causes of extinguishment of obligations such as annulment, rescission, fulfillment of a resolutive condition, and prescription, are governed elsewhere in this Code (1156a).

Discussion of the Law

There are other causes of extinguishment of obligation which are not expressly provided under the above provision. *Death* extinguishes obligations which are purely personal in character, such as partnership and agency. Obligations may also be extinguished by the happening of a *fortuitous event*³² or *by will of one of the parties* as in some contracts such as partnership and agency.

³² -- Article 1174, Civil Code of the Philippines

Parties may stipulate any currency for payment of debts to extinguish obligations. In the absence of any stipulation, payments must be made in the currency which is the legal tender in the Philippines (the Philippine Peso). Payment in checks (whether manager's or cashier's checks) will have the effect of payment under Article 1231, Civil Code only when these are already encashed or cleared by the collecting banks.³³ Payment by way of credit cards is equivalent to payment made by a third person (credit card company) who has no interest in the fulfillment of the obligation, in which case, the payer shall have the rights of reimbursement, acquires the rights of a creditor and may recover what has actually paid.³⁴

Fortuitous event, also known as *force majeure* or *caso fortuito*, are terms which exempt an obligor from liability. These are extraordinary events not foreseeable or avoidable, events that could not be foreseen, or which, though foreseen, were inevitable. (Article 1174, Civil Code of the Philippines). It is therefore, not enough that the event could not have been foreseen or anticipated, as is commonly believed, but it must be one impossible to foresee or to avoid.³⁵

Fortuitous events may be produced by two general causes: (1) by Nature, such as earthquakes, storms, floods, epidemics, tsunami, etc., (2) by the act of man, such as armed invasion (or coup d' etat), attack by bandits, governmental prohibitions, robbery, etc. In order that acts of man may constitute fortuitous event, it is necessary that they have the force of an imposition which the debtor could not have resisted. (3 Salvat 83-84). Thus, the outbreak of war which prevents performance exempts a party from liability. (PNB vs. Court of Appeals, 94 SCRA 357.) Fortuitous event includes unavoidable accidents, even if there has been an intervention of human element,

³³ -- Refer to Article 1249, Civil Code of the Philippines.

³⁴ -- Article 1236, par. 2; Article 1237, 1302, 1303, Civil Code of the Philippines.

³⁵ -- Philippine Legal Encyclopedia by Jose Agaton R. Sibal, page 341.

provided fault or negligence cannot be imputed to the debtor. ³⁶ If the thing has been lost through robbery with violence, the debtor must show that he could not resist the violence. If the thing is lost through theft, the debtor is considered negligent in having placed the thing within reach of thieves and not in a secure or safe place; hence, the debtor will be liable for damages. ³⁷

Application of the Law

Case: On November 6, 1968, Philippine Airlines (PAL's) Fokker 'Friendship' PIC-536 left Mactan City for the City of Manila. After the plane had taken off, Florencio O. Villarín, a Senior NBI Agent who was also a passenger of the said plane, noticed a certain 'Zaldy,' a suspect in the killing of Judge Valdez, seated at the front seat near the door leading to the cockpit of the plane. 'Zaldy' had used the name 'Cardente,' in his plane ticket and had three companions on board the plane. Villarín then scribbled a note addressed to the pilot of the plane requesting the latter to contact NBI duty agents in Manila for the said agents to ask the Director of the NBI to send about six NBI agents to meet the plane because the suspect in the killing of Judge Valdez was on board the plane. The said note was handed by Villarín to the stewardess who in turn gave the same to the pilot. After receiving the note, which was about 15 minutes after take off, the pilot of the plane came out of the cockpit and sat beside Villarín at the rear portion of the plane and explained that he could not send the message because it would be heard by all ground aircraft stations. Villarín, however, told the pilot of the danger of commission of violent acts on board the plane by the notorious 'Zaldy' and his three companions. While the pilot and Villarín were talking, 'Zaldy' and one of his companions walked to the rear and stood behind them. The pilot then stood up and went back to the cockpit. 'Zaldy' and his companions returned to their seats. Soon thereafter an exchange of gunshots ensued between Villarín and 'Zaldy' and the latter's companions. 'Zaldy' announced to the passengers and the pilots in the cockpit that it was a "hijack." The hijackers divested the passengers of their belongings. Upon landing at the Manila International Airport, Zaldy and his three companions succeeded in escaping.

Norberto Quisumbing, Sr., one of the passengers of the plane filed an action against Philippine Airlines to recover the value of jewelry, other valuables and money taken from him by four (4) armed robbers on board of the latter's airplane while on a flight from Mactan City to Manila, as well as moral and exemplary damages, attorney's fees and expenses of litigation. Such loss is a result of breach of PAL's contractual obligation to carry him and his belongings and effects to the Manila destination without loss or damage, and constitutes a serious dereliction of PAL's legal duty to exercise extraordinary diligence in the vigilance over the same. In its defense, Philippine Airlines alleges that the robbery during the flight and after the aircraft was forcibly landed at the Manila Airport did indeed constitute *force majeure*.

³⁶ -- Civil Code of the Philippines, Vol. IV, by Arturo M. Tolentino, 1991 edition, page 126-127.

³⁷ -- Ibid., page 337.

Is the incident on board the airplane Flight Fokker 'Friendship' PIC-536 considered *force majeure* which exempts Philippine Airlines (PAL's) from liability?

Legal Opinion: Yes, such hijacking constitutes *force majeure*. Hijackers do not board an airplane through a blatant display of firepower and violent fury. The objective of modern-day hijackers is to display the irresistible force amounting to *force majeure* only when it is most effective and that is when the jetliner is winging its way at Himalayan altitudes and ill-advised heroics by either crew or passengers would send the multimillion peso airplane and the priceless lives of all its occupants into certain death and destruction.

Philippine Airlines could not be faulted for want of diligence. The mandatory use of the most sophisticated electronic detection devices and magnetometers, the imposition of severe penalties, the development of screening procedures, the compilation of hijacker behavioral profiles, the assignment of sky marshals, and the weight of outraged world opinion may have minimized hijackings but all these have proved ineffective against truly determined hijackers. World experience shows that if a group of armed hijackers want to take over a plane in flight, they can elude the latest combined government and airline industry measures. And as our own experience in Zamboanga City illustrates, the use of force to overcome hijackers, results in the death and injury of innocent passengers and crew members. Philippine Airlines has faithfully complied with the requirements of government agencies and adhered to the established procedures and precautions of the airline industry at any particular time.

Under the circumstances of the instant case, the acts of the airline and its crew cannot be faulted as negligence. The hijackers had already shown their willingness to kill one passenger who survived from gunshot wounds. The lives of the rest of the passengers and crew were more important than their properties. Cooperation with the hijackers until they release their hostages at the runway end near the South Superhighway was dictated by the circumstances.³⁸

(Note: In *Gacal vs. Philippine Airlines*, G.R. 55300, March 15, 1990 it was held that Philippine Airlines was not liable for the death and injuries of its passengers due to hijacking of six (6) men who were allegedly members of the Moro National Liberation Front. According to the Supreme Court: "Under normal circumstances, PAL might have foreseen the skyjacking incident which could have been avoided had there been a more thorough frisking of passengers and inspection of baggages as authorized by R.A No. 6235. But the incident in question occurred during Martial Law where there was a military take-over of airport security including the frisking of passengers and the inspection of their luggage preparatory to boarding domestic and international flights. In fact military take-over was specifically announced x x x rendered it impossible for PAL to perform its obligations in a normal manner and obviously it cannot be faulted with negligence in the performance of duty taken over by the Armed Forces of the Philippines to the exclusion of the former.)³⁹

³⁸ -- *Norberto Quisumbing, Sr., and Gunther Loeffler vs. Court of Appeals*, G.R. No. 50076, September 14, 1990.

³⁹ -- Compare with the case of *Fortune Express, Inc. vs. Court of Appeals*, G.R. No. 119756, March 18, 1999 where a bus operator was liable for the death and injuries of its passengers due to hijacking for failure to observe extraordinary diligence.

Payment or Performance

As a mode of extinguishment, it means fulfillment or performance of the obligation by:

- a) Delivery of money in payment of debt
- b) Delivery of the object
- c) Performance or non-performance of the prestation in obligations to do or not to do.

In case of payment made by a third person who has no interest in the obligation:

a) Without knowledge and consent of the debtor.

- Creditor is not bound to accept unless there is stipulation to the contrary
- There is no legal subrogation. Third person cannot collect from the guarantor if the debtor refuses to pay
- Third person can only collect from the debtor whatever has been beneficial to the latter
- Third person cannot collect or recover from the debtor if the debt has already prescribed or has been remitted.

b) With the knowledge and consent of the debtor.

- Legal subrogation takes place and he acquires all the rights of the creditor against the debtor.
- Example: Payment through credit cards.

Dation in payment -- is the conveyance of ownership of a thing as an accepted equivalent of performance.

Illustration: Bank A granted a car loan to B with the car as a chattel mortgage. In case the loan is not paid, Bank A has the right to foreclose the chattel mortgage.

However, Bank A and B may agree that B will instead execute a Deed of Sale of motor vehicle making Bank A as the buyer. The execution of a Deed of Sale may be considered as payment of the loan by means of *datio en pago* or *dation in payment*.

Payment by cession is the abandonment of all property of the debtor for the benefit of his creditors in order that the latter may apply the proceeds thereof to the satisfaction of their credits. The Insolvency Law provides for the procedure in settling all the debts of the debtor who cannot settle all his obligations because he is already insolvent.

Tender of payment is the offer made by the debtor to make payment at or after maturity date. The debtor must have at the time of his offer the thing or money to be paid in his possession or at his disposal.

Consignation is the delivery or deposit of the thing or the money due with a competent court after complying with certain formalities. The requisites of a valid consignation are as follows:

- a) Valid tender of payment
- b) First notice of consignation
- c) Actual deposit/ hearing
- d) Second notice of consignation

Condonation or remission of debt

It is the act of liberality by which the obligee, who receives no price or equivalent thereof, renounces the enforcement of the obligation which is extinguished in its entirety or in part or aspect of the same to which the remission refers.

The requisites of condonation of debt are as follows:

- a) Remission must be gratuitous
- b) Obligation must be due and demandable

c) Debtor must accept

If personal property is involved, remission may be made orally or in writing. But if the personal property exceeds P5,000.00, the same must be in writing. Remission of an obligation involving real property must likewise appear in a public instrument.

Confusion or Merger of Rights

It is the meeting in one person the qualities of a creditor and debtor with respect to the same obligation.

Example: Confusion of rights with respect to a check that is payable to bearer or "PAY TO THE ORDER OF CASH."

Compensation

This takes place when two persons who, in their own right, are creditors and debtors of each other.

The requisites of a valid compensation are as follows:

1. There are two persons who are creditors and debtors of each other
2. There are two or more debts of the same kind, nature and quality
3. The debts to be compensated are due and demandable
4. There is no retention, controversy or adverse claim over anyone of the debts to be compensated.

Fixed, savings and current deposits of money in banks and similar institutions shall be governed by the provisions of the Civil Code concerning simple loan (mutuum). Hence, a debtor-creditor relationship exists between a bank and a depositor. That is why compensation may take place where a bank may validly debit the account of its depositors who are indebted to the bank by way of loan.

Novation

It is the creation of a new obligation to alter, substitute or replace an existing obligation, with the intention of extinguishing or modifying the latter in any of the following ways:

- I. By changing the object of the principal obligation:
 - Requisites:
 - a) There is a prior existing obligation
 - b) There is mutual agreement between the parties to make a new contract
 - c) The new contract is also valid
 - d) The new contract extinguishes the prior contract.
- II. By substituting the person of the debtor
 - Expromision -- when a third person who has no interest in the obligation and with the consent of the creditor, takes the place and assumes the obligation of the original debtor without the latter's knowledge and consent.
 - Delegacion -- when the original debtor recommends to the creditor a third person to take his place as debtor and assume his obligation, and the creditor accepts.

CONTRACTS

The Law

“Article 1305. A contract is a meeting of minds between two persons whereby one binds himself, with respect to the other, to give something or to render some service. (1254a)”⁴⁰

Discussion of the Law

⁴⁰ -- Civil Code of the Philippines.

Characteristics of a Contract

(1) Mutuality of Contracts. Its validity and performance cannot be left to the will of only one of the parties.⁴¹

(2) Autonomy of Contracts. Parties are free to stipulate terms and provisions in a contract, as long as these terms and provisions are not contrary to law, morals, good customs, public order and public policy.⁴²

Application of the Law

Case: In a contract of employment between A and B, the latter agreed that for a period of five years after the termination of his employment, he shall neither engage or interest himself in any business enterprise similar to or in competition with those operated by A, nor enter into the employment of any enterprise in the Philippines, except after obtaining the written permission of A. Is the agreement valid?

Legal Opinion: The agreement is void because it is contrary to public policy. The agreement is clearly one in undie or unreasonable restraint of trade. It is not necessary for the protection of A. Besides, it would practically force B to get our of the country in order to obtain a livelihood in case should declineto give him a written permission to work elsewhere in the country.⁴³

The following are valid stipulations in an employment contract:

- Non-competition agreements – those that impose restrictions on an employer's abliy to compete with a former employer are valid as long as:
 - ✓ It is supported by adequate consideration;
 - ✓ The restraint is confined within the limits that are reasonably necessary for the protecion of the employer's business
 - ✓ Restraint does not impose undue hardship on the employee.

⁴¹ -- Article 1308, Civil Code of the Philippines.

⁴² -- Article 1306, Civil Code of the Philippines.

⁴³ -- Ferrazini vs. Gsell, 34 Phil. 697.

- Non-solicitation agreements – requirement to newly-hired employees to sign a non-solicitation agreement to obligate the employee not to solicit contacts and fellow employees of the employer. Non-solicitation agreements run for an indefinite period.
- Confidentiality – imposes upon an employee a duty to keep confidential trade secrets and other confidential company information during employment and after employment. This may also run for an indefinite period.

A Yellow Dog Contract is a promise exacted from workers as a condition of employment that they are not to belong to, or attempt to foster, a union during their period of employment. This constitutes Unfair Labor Practice and considered an illegal stipulation.

(3) Relativity of Contracts. Contracts are binding only upon the parties and their successors-in-interest.

Exceptions:

- Stipulation in favor of a third person (stipulation pour autrui) as in a beneficiary of an insurance policy.⁴⁴
- Contracts creating real rights
- Third person liable to pay damages in case he induces a party to violate his contract.

Stipulation pour autrui (stipulation in favor of a third person) will prosper as long as the following requisites are present:

- It must be for the benefit or interest of the third person;
- Such benefit must not be merely incidental;

⁴⁴ -- Article 1311, Civil Code of the Philippines.

- Contracting parties must clearly and deliberately conferred such benefit or interest upon the third person
- That the third person must have communicated his acceptance to the obligor before his revocation.

(4) Consensuality of Contracts. Contracts are perfected by mere consent. and no form is prescribed by law for their validity. Exception: (a) real contracts (such as pledge, chattel mortgage); (b) contracts covered under the Statute of Frauds.⁴⁵

(5) Obligatory Force of Contracts. By the obligatory force of contracts, it constitutes the law as between the parties who are compelled to perform under the threat of being sued in the courts of law. ⁴⁶

Application of the Law

Case: Can a hotel evade liability for the loss of items left with it for safekeeping by its guests, by having these guests execute written waivers holding the establishment or its employees free from blame for such loss? Maurice McLoughlin, an Australian businessman-philanthropist sued Tropicana Copacobana Apartment Hotel (Tropicana) for the loss of his American and Australian dollars deposited in the safety deposit box of Tropicana. Mr. McLoughlin is also demanding for liquidating damages, moral and exemplary damages with attorney's fees. It appears that the safety deposit box could only be opened through the use of two keys, one of which is given to the registered guest, and the other remaining in the possession of the management of the hotel. When a registered guest wishes to open his safety deposit box, he alone could personally request the management who then would assign one of its employees to accompany the guest and assist him in opening the safety deposit box with the two keys. In its defense, Tropicana denies liability, relying on the conditions for renting the safety deposit box as signed by Mr. McLoughlin, to wit:

“Undertaking for the Use of Safety Deposit Box,”

“2. To release and hold free and blameless Tropicana Apartment Hotel from any liability arising from any loss in the contents and/or use of the said deposit box for any cause whatsoever, including but not limited to the presentation or use thereof by any other person should the key be lost;

⁴⁵ -- Article 1315, 1316, 1403 (2), Civil Code of the Philippines.

⁴⁶ -- Article 1159, Civil Code of the Philippines.

“4. To return the key and execute the release in favor of Tropicana Apartment Hotel upon giving up the use of the box.

Is Mr. McLoughlin entitled to his claims despite the written waiver which he signed in favor of Tropicana Apartment Hotel?

Legal Opinion: Yes, Mr. McLoughlin is entitled to all his claims despite the written waiver which he signed in favor of Tropicana. The evidence reveals that two keys are required to open the safety deposit boxes of Tropicana. One key is assigned to the guest while the other remains in the possession of the management. If the guest desires to open his safety deposit box, he must request the management for the other key to open the same. In other words, the guest alone cannot open the safety deposit box without the assistance of the management or its employees. With more reason that access to the safety deposit box should be denied if the one requesting for the opening of the safety deposit box is a stranger. Thus, in case of loss of any item deposited in the safety deposit box, it is inevitable to conclude that the management had at least a hand in the consummation of the taking, unless the reason for the loss is *force majeure*. Noteworthy is the fact that the employees of Tropicana had custody of the master key of the management when the loss took place. Yet the management failed to notify Mr. McLoughlin of the incident and waited for him to discover the taking before it disclosed the matter to him. Therefore, Tropicana should be held responsible for the damage suffered by Mr. McLoughlin by reason of the negligence of its employees.

Under Article 1170 of the New Civil Code, those who, in the performance of their obligations, are guilty of negligence, are liable for damages. As to who shall bear the burden of paying damages, Article 2180, paragraph (4) of the same Code provides that the *owners and managers* of an establishment or enterprise are likewise responsible for damages caused by their employees in the service of the branches in which the latter are employed or on the occasion of their functions. Also, if an employee is found negligent, it is presumed that the employer was negligent in selecting and/or supervising him for it is hard for the victim to prove the negligence of such employer. Thus, given the fact that the loss of Mr. McLoughlin’s money was consummated through the negligence of Tropicana’s employees, both the assisting employees and Tropicana, should be held solidarily liable pursuant to Article 2193.

The “*Undertaking for The Use of Safety Deposit Box*” executed by Mr. McLoughlin is tainted with nullity. Article 2003 of the Civil Code is controlling, thus:

‘Article. 2003. The hotelkeeper cannot free himself from responsibility by posting notices to the effect that he is not liable for the articles brought by the guest. Any stipulation between the hotelkeeper and the guest whereby the responsibility of the former as set forth in Articles 1998 to 2001 is suppressed or diminished shall be void.’

Article 2003 was incorporated in the New Civil Code as an expression of public policy precisely to apply to situations such as that presented in this case. The hotel business like the common carrier’s business is imbued with public interest. Catering to the public, hotelkeepers are bound to provide not only lodging for hotel guests and security to their persons and belongings. The twin duty constitutes the essence of the business. The law in turn does not allow such duty to be negated or diluted by any

contrary stipulation in so-called “undertakings” that ordinarily appear in prepared forms imposed by hotel keepers on guests for their signature.⁴⁷

Classification of Contracts

(1) *According to their relation to other contracts:*

(a) *Preparatory* -- or those which have for their object the establishment of a condition in law which is necessary as a preliminary step towards the celebration of another subsequent contract. Examples – partnership, agency, common carrier, insurance.

(b) *Principal* – or those which can subsist independently from other contracts and whose purpose can be fulfilled by themselves. Examples – sale, lease, common carrier, insurance.

(c) *Accessory* – or those which can exist only as a consequence of, or in relation with, another prior contract. Examples – pledge, mortgage.

(2) *According to their perfection:*

(a) *Consensual* – or those which are perfected by the mere agreement of the parties. Examples – sale, lease.

(b) *Real* – or those which require not only the consent of the parties for their perfection, but also the delivery of the object by one party to the other. Examples – commodatum, deposit, pledge.

(3) *According to their form:*

(a) *Common or informal* – those which require no particular form. Example: loan.

⁴⁷ -- YHT Realty Corporation vs. Erlinda Lainez and Anicia Payam, G.R. No. 126780, February 17, 2005.

(b) *Special or formal* – or those which require some particular form. Examples – donation, chattel mortgage.

(4) *According to their purpose:*

(a) *Transfer of ownership.* Example – sale.

(b) *Conveyance of use.* Example – commodatum.

(c) *Rendition of services.* Example – agency, lease of services, labor.

(5) *According to their subject matter:*

(a) *Things.* Examples – sale, deposit, pledge.

(b) *Services.* Examples – agency, lease of services, labor.

(6) *According to the nature of the vinculum which they produce:*

(a) *Unilateral* – or those which give rise to an obligation for only one of the parties. Examples – commodatum, gratuitous deposit.

(b) *Bilateral* – or those which give rise to reciprocal obligations for both parties. Examples – sale, lease.

(7) *According to their cause:*

(a) *Onerous* – or those in which each of the parties aspires to procure for himself a benefit through the giving of an equivalent or compensation. Examples – sale, insurance, common carrier.

(b) *Gratuitous* – or those in which one of the parties proposes to give to the other a benefit without any equivalent or compensation. Example – commodatum.

(8) *According to the risks involved:*

(a) *Commutative* – or those where each of the parties acquires equivalent of his prestation and such equivalent is pecuniarily appreciable and already determined from the moment of the celebration of the contract. Example – lease.

(b) *Aleatory* – or those where each of the parties has to his account the acquisition of an equivalent of his prestation, but such equivalent, although pecuniarily appreciable, is not yet determined at the moment of the celebration of the contract, since it depends upon the happening of an uncertain event, thus charging the parties with the risk of loss or gain. Example – insurance.

(9) *According to their names or norms regulating them:*

(a) *Nominate* – or those which have their own individuality and are regulated by special provisions of law. Examples – sale, lease, common carrier, insurance, deposit, agency.

(b) *Innominate* – or those which lack individuality and are not regulated by special provisions of law. In the Roman Law, the innominate contracts were classified into four groups: *do ut des* (I give and you give), *do ut facias* (I give and you do), *facio ut facias* (I do and you do), and *facio ut des* (I do and you do).⁴⁸

The essential elements of a contract:

The essential elements of a contract are as follows:

(a) Consent, which is manifested by the meeting of the minds of the offer and the acceptance upon the thing and the cause which are to constitute the contract. The offer must be certain and the acceptance absolute;

(b) Object certain, which is the subject matter of the contract; and

(c) Cause of the obligation which is established.⁴⁹

⁴⁸ -- Civil Code of the Philippines, Vol. IV, by Arturo Tolentino, 1991 ed., Central Book Supply, Inc.

⁴⁹ -- Article 1318, Civil Code of the Philippines.

A contract of adhesion is defined as one in which almost all the provisions have been drafted only by one party, usually a corporation or insurance company. The only participation of the other party is the signing of his signature or his adhesion.⁵⁰ Some writers believe that such contract suppresses the will of one of the contracting parties, hence not a true contract. However, this is not always juridically true. Normally, the party who adheres to it is in reality free to reject entirely; if he adheres, then he gives his consent.

Consent

It is manifested by the meeting of the offer (which must be definite) and acceptance (which must be absolute) upon the thing and the cause which constitute the contract.

Acceptance through telegram (or e-mail) shall bind the offeror from the time it came to his knowledge.

An Option to Purchase may be withdrawn anytime if the option is without any consideration (Reservation Fees) separate from the purchase price.

Invitations to Bid. Advertisements for bidders are simply invitations to make proposals and the advertiser is not bound to accept the highest or lowest bidder unless the contrary appears.

The following are the parties who are incapable of giving consent:

1. Minors;

⁵⁰ -- Philippine Legal Encyclopedia, by Jose Agaton R. Sibal, page 20.

2. Insane or demented persons;
3. Deaf-mutes who do not know how to read and write

The following are the instances which vitiate consent:

1) Mistake -- unconscious ignorance or forgetfulness of the existence or non-existence of a fact, past or present, material to the contract. Example: Mistake of object, mistake of identity.

2) Violence -- There is violence when, in order to wrest consent, serious and irresistible force is employed.

3) Intimidation -- There is intimidation when one of the contracting parties is compelled by a reasonable and well-grounded fear of an imminent or grave evil upon his person or property or upon the person or property upon his spouse, descendants, or descendants, to give his consent.

4) Undue Influence -- There is undue influence when a person takes improper advantage of his power over the will of another, depriving the latter of a reasonable **freedom of choice**.

5) Fraud (Causal fraud) -- Insidious words or machinations are employed to induce the party to enter into a contract, without which, he would not have entered into. Usual exaggerations of trade when the other party had the opportunity to know the facts are not fraudulent (LET THE BUYER BEWARE). Mere expression of opinion does not signify fraud unless made by an expert and the other party relied on the former's special knowledge.

Object

It is the subject matter of the contract.

The requisites of a valid object are as follows:

1. Lawful
2. Within the commerce of man
3. Possible
4. Determinate as to its kind
5. Must not be contrary to law, morals, good customs, public order, public policy.

Cause

In onerous contracts, the cause is to be understood, for each contracting party, the prestation or promise of a thing, or service by the other; in remuneratory ones, the service or benefit which is remunerated; and in contracts of pure beneficence, the mere liberality of the benefactor.

The following requisites of a valid cause:

1. It must be true
2. It must exist
3. It must be lawful

Application of the Law:

Case: Mr. Danilo Santos bought 10 boxes of Fundador Brandy at a price of P10,000 pesos per box from his supplier, Mr. John Smith, proprietor of Exquisite Wines & Brandy, Inc. Determine the requisites of such contract of sale.

Legal Opinion: The consent refers to the meeting of minds as when Mr. John Smith (the seller) offered Mr. Danilo Santos to sell the 10 boxes of Fundador Brandy at a price

of P10,000 pesos per box and when Mr. Danilo Santos agreed to buy the said 10 boxes of Fundador Brandy at the price of P10,000 pesos per box. The object or subject matter refers to the 10 boxes of Fundador Brandy at the price of P10,000 pesos per box. As to the seller, the cause is the price of P10,000 pesos per box. As to the buyer, the cause is the 10 boxes of Fundador Brandy.

Form of Contracts

Contracts may be in any form because they are consensual in nature. The following are the exceptions:

1. Real Contracts are perfected not by mere consent but by delivery. Example: pledge, antichresis
2. Donation of personal property exceeds P5,000 – it must be in writing, otherwise, it is void.
3. Donation of real property – it must appear in a public instrument.
4. Chattel mortgage where registration in the chattel mortgage registry is required.
5. Contracts which are required to be in writing or in a memorandum to be enforceable.
6. In case of sale of piece of land is made through an agent, the agent's authority must be in writing, otherwise the sale is void.

Application of the Law

Case: Marlen Dauden, a movie star filed a complaint against X Co. to recover P14,700 representing the balance of her compensation as leading actress in two motion pictures produced by the company. Upon motion of defendant, the lower court dismissed the complaint because “the claim of plaintiff was not evidenced by any written document, either public or private” in violation of Article 1358 of the Civil Code of the Philippines. Is this order of dismissal in accordance with the law?

Legal Opinion: The lower Court's dismissal is not in accordance with the law. In the matter of formalities, contracts are valid and binding from their perfection regardless of form whether they be oral or written. This is plain from Articles 1315 and 135 of the Civil

Code of the Philippines. Consequently, as long as the three elements of a contract exist (consent, object, cause), the contract is generally valid and binding.⁵¹

Reformation of Instruments:

This remedy is applicable when there is meeting of minds as to the object and cause, but the true intention is not expressed in the instrument.

The requisites are as follows:

1. There is meeting of minds of parties in the contract.
2. The true intention of the parties is not expressed in the instrument
3. The true intention is not expressed by reason of mistake, fraud or inequitable conduct.

Interpretation of contracts

The courts of justice are empowered to interpret contracts in case of litigation.

The following are the rules to be observed in the interpretation of contracts.

- The literal meaning shall prevail in the absence of any obscurity therein
- In case of doubt, the intention of the parties shall prevail.
- In case of doubt, a contract of adhesion shall be construed most strongly against the person who caused the ambiguity (as in the one who made it).
- In case of doubt, contracts of labor shall be construed liberally in favor of the laborer.

Kinds of Defective Contracts

a) Rescissible

⁵¹ -- Dauden-Hernaez vs. De los Angeles, 27 SCRA 1276.

Rescissible Contracts are defective by reason of damage or lesion. In this kind of defective contract, mutual return is incumbent upon actual participants. Rescission is instituted only when the party suffering damage has no other legal means to obtain reparation for the same. The action must be commenced within 4 years.

Examples of rescissible contracts are as follows:

1. Those entered into by guardians whenever their wards represent lesion by more than $\frac{1}{4}$ of the value of the thing.
2. Those agreed upon in representation of absentees, if the latter suffer lesion stated in the preceding number.
3. Those undertaken in fraud of creditors.

b) Voidable Contracts

These contracts are alid but subject to annulment by reason of vitiated consent or incapacity of one of the contracting parties. The action to file annulment shall commence within 4 years. The action for annulment shall involve restitution with their fruits, and the price with its interest.

c) Unenforceable Contracts

These contracts are valid but defective because it cannot be enforced in courts.

Examples of unenforceable contracts are as follows:

1. Those entered into in the name of another who has been given no authority or legal representation or who has acted beyond his powers.
2. Those where both parties are incapable of giving consent to a contract.

3. Those that do not comply under the Statute of Frauds (The items covered must appear in writing otherwise it cannot be enforced in courts.)

- An agreement that by its terms is not to be performed within one (1) year;
- A special promise to answer for the debt, default or miscarriage of another
- An agreement for the sale of goods/chattels at a price not less than P500
- Sale of real property
- An agreement for the leasing for a longer period than one year.

Those covered under the Statute of Frauds refer only to executory contracts, and does not refer to executed contracts already.

d) Void Contracts

These are contracts are considered void because the object and cause are illegal, contrary to law, inexistent or considered simulated. These are contracts which are not subject to ratification. The right to bring an action to declare a contract void does not prescribe, the right to raise the defense of illegality cannot be waived and a void contract has no force or effect whatsoever.

Application of the Law

Case: On January 4, 1979, Ronald Coloma sold his hotel in favor of Spouses Leo and Vanessa Uy. A deed of sale was executed but Spouses Uy named Johnny Uy (their unborn son) as the buyer in the contract of sale. Accordingly, Johnny Uy was named as the buyer in the deed of sale by virtue of a Chinese custom naming children as the heir of their parents' properties. It was only on March 1, 1980 that Johnny Uy was born. Is the contract of sale valid?

Legal Opinion: It was held that the contract of sale is void for being simulated and fictitious. Johnny Uy was not even conceived yet at the time of the alleged sale, hence had no legal personality to be named as a buyer in the said deed of sale. Neither could he have given his consent thereto. The contract of sale is perfected at the moment there is a meeting of the minds upon the thing which is the object of the contract and upon the price. Consent is manifested by the meeting of the offer and the acceptance upon the

thing and the cause which are to constitute the contract. Unemancipated minors, insane or demented persons, and deaf-mutes who do not know how to read and write cannot validly give consent to contracts. In the instant case, Johnny Uy could not have validly given his consent to the contract of sale, as he was not even conceived yet at the time of its alleged perfection. Therefore, for lack of consent of one of the contracting parties, the deed of sale is null and void.⁵²

In pari delicto rule

This signifies that both parties are at fault. If both parties are at fault, they cannot sue each other nor demand performance from each other. The courts will leave them as they are and no award shall be granted.

⁵² -- Pepito S. Pua et al. vs. The Hon. Court of Appeals et al., G.R. No. 134992. November 20, 2000.