

GENERAL PROVISIONS OF CONTRACTS

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.

Elements of a Contract

Essential elements – includes consent of the parties, object or subject matter and cause or consideration

Natural elements – its existence is presumed by law unless there is an agreement to the contrary. Ex: warranty in case of eviction in a contract of sale.

Accidental elements – consist of the unusual stipulation of the parties like conditions, terms, etc. Ex: interest agreed upon on loans

Stages of a Contract

1. Preparation or conception
2. Perfection or birth
3. Consummation or termination

Scenario: Teofilo offers to sell his horse to Eduardo for P600,000. Identify the possible procedures that will identify the stages of a contract.

Classification of Contracts

Express and implied: An express contract is one wherein the intent of the parties is shown by words (oral or written). An implied contract is one wherein the intent of the parties is shown by conduct (X renders and Y accepts valuable services)

Executed and executory: An executed contract is one that has already been performed; an executory contract is one that has not yet performed; may sometimes be partly executor and partly executed.

Nominate and innominate contracts: Nominate contracts are those with a special name or designation in the Civil Code.

Consensual and real contracts: A consensual contract is one perfected by mere consent. A real contract is one perfected by the delivery of the thing which is the object of the contract.

Unilateral and Bilateral contracts: In unilateral contract, only one of the parties has an obligation; a bilateral contract creates reciprocal obligations

Article 1306. The contracting parties may establish such stipulations, clauses, terms and conditions as they may deem convenient, provided they are not contrary to law, morals, good customs, public order, or public policy.

Freedom to contract guaranteed

The right to enter into contract is one of the liberties guaranteed to the individual by the Constitution. However, the constitutional prohibition against the impairment of contractual obligations refers only to legally valid contracts. In appropriate cases, it cannot be invoked as against the right of the state to exercise its police power. In other words, an individual does not have an absolute right to enter into any kind of contract.

Limitations on contractual stipulations.

There are limitations to the freedom to contract.

- (1) *Law* — Contract entered into must be in accordance with, and not repulsive to, an applicable statute. Its terms are embodied in every contract. The law thus sets limits.
- (2) *Police power** — When there is no law in existence or when the law is silent, the will of the parties prevails unless their contract contravenes the limitation of morals, good customs, public order, or public policy.

Examples: Which of these contracts are valid?

1. A contract whereby X promised to live as the common-law wife of Y without the benefit of marriage in consideration of P1, 000,000.00 is immoral and, therefore, void.
2. An agreement whereby X is to render service as a servant to Y without compensation as long as X has not paid his debt is reprehensible and censurable. It is also contrary to law.
3. X entered into a contract whereby X binds himself to slap his father. This contract is void because it is against the good custom of showing respect to our parents.
4. A stipulation in a contract of lease whereby the landlord can use force to eject the tenant in case of failure of the latter to pay the rent agreed upon is void as being against public order.

Article 1307. Innominate contracts shall be regulated by the stipulations of the parties, by the provisions of Titles I and II of this Book, by the rules governing the most analogous nominate contracts and by the customs of the place.

Classification of contracts according to its name or designation

- *Nominate contract* or that which has a specific name or designation in law (*e.g.*, commodatum, lease, agent sale, etc.)
- *Innominate contract* or that which has no specific name or designation in law.

Kinds of innominate contract

- *do ut des* (I give that you may give);
- *do ut facias* (I give that you may do);
- *facio ut des* (I do that you may give); and
- *facio ut facias* (I do that you may do).

Do ut des is, however, no longer an innominate contract. It has already been given a name of its own, *i.e.*, *barter* or *exchange*.

Scenario: A, was one of two lawyers who represented B in suit filed by the latter for reinstatement to his position in the Central Bank. The Court ruled in favor of B against the Central Bank. By reason of misunderstanding as to the amount of attorney's fees, A filed a suit against B. B alleged that A was not entitled attorney's fees because there had been no agreement to that effect.

Court Ruling: The Court declared that the payment of attorney's fees to A may also be justified by virtue of innominate contract of *facio ut des* which is based on the principle that no one shall unjustly enrich himself at the expense of another.

Reasons for innominate contracts

The impossibility of anticipating all forms of agreement on one hand, and the progress of man's sociological and economic relationships on the other, justify this provision. A contract will not, therefore, be considered invalid for failure to conform strictly to the standard contracts outlined in the Civil Code. It is sufficient that it has all the elements of a valid contract.

Rules governing innominate contracts

Innominate contracts shall be governed by:

- (1) the agreement of the parties;
- (2) the provisions of the Civil Code on obligations and contracts;
- (3) the rules governing the most analogous contracts; and
- (4) the customs of the place

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

Contract binds both contracting parties.

A contract is an agreement which gives rise to obligations: It must bind both parties in order that it can be enforced against either. Without this equality between the parties, it cannot be said that the contract has the force of law between them.

It is an elementary rule that no party can renounce or violate the law of the contract without the consent of the other. Hence, "its validity or compliance cannot be left to the will of one of them."

Example: Sam agreed to sell his car to Bert for P300,000.00. The contract is binding upon both contracting parties and either of them can enforce the contract against the other.

Will the contract be valid if Sam alone determines the price of the car?

Article 1309. The determination of the performance may be left to a third person, whose decision shall not be binding until it has been made known to both contracting parties.

Determination of performance by a third person

Compliance with a contract cannot be left to the will of one of the contracting parties.

However, under the above provision, the determination of its performance may be left to a third person. In such case, the obligation does not depend upon a potestative condition. The decision, however, shall bind the parties only after it has been made known to both of them.

Example: Sam sold his parcel of land to Bert. It was agreed that Charlie, a real estate appraiser, would be the one to determine the reasonable price of the land. Charlie, then, fixed the price after considering all the circumstances and factors affecting the value of the land.

In this case, Charlie must make known his decision to Sam and Bert who will be bound by the same.

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

Effect where determination inequitable

A contracting party is not bound by the determination if it is evidently inequitable or unjust as when the third person acted in bad faith or by mistake. In such case, the courts shall decide what is equitable under the circumstances.

Scenario: Santos entered into a contract with Reyes whereby Santos agrees to sell Reyes 10 sacks of rice at a reasonable price to be determined by their mutual friend Ledesma. This is freely agreed by both parties. Ledesma then fixes the price at P1750 per cavan, having due regard to all circumstances, the market, etc, and informs both Santos and Reyes of his decision. Santos is then obliged to deliver to Reyes 10 sacks of rice while Reyes is under obligation to pay the reasonable price fixed by the third person Ledesma.

Supposing Ledesma fixes the price of the 10 sacks at P1000 per sack where the current price is P1750. In such case, Santos need not deliver the 10 sacks of rice because the price fixed by Ledesma is highly inequitable, and unjust. He may file a case in court for the court to fix the just price.

Article 1311. Contracts take effect only between the parties, their assigns and heirs, except in case where the rights and obligations arising from the contract are not transmissible by their nature, or by stipulation or by provision of law. The heir is not liable beyond the value of the property he received from the decedent.

If a contract should contain some stipulation in favor of a third person, he may demand its fulfillment provided he communicated his acceptance to the obligor before its revocation. A mere incidental benefit or interest of a person is not sufficient. The contracting parties must have clearly and deliberately conferred a favor upon a third person.

Persons affected by a contract

(1) *General rule.* — Contract takes effect only between the parties, their assigns (*i.e.*, transferees), and heirs. This means that only the parties, their assigns and heirs can have rights and obligations under the contract. As a rule, the act of declaration, or omission of a person cannot affect or prejudice another without the latter's authorization or ratification.

(2) *Exceptions.* — The cases when a contract are effective only between the *parties* are when the rights and obligations arising from the contract are not transmissible:

- (a) by their nature (like a contract involving personal qualifications, as painting, singing, etc.); or
- (b) by stipulation (in accordance with the principle of freedom to contract); or
- (c) by provision of law (as in agency, partnership, and *commodatum*, when death extinguishes the legal relationships).

Examples:

1. Don is indebted to Matt in the amount of P80,000. On the due date of the obligation, Matt dies leaving his son Chad as his sole heir. Is the right of Matt transmissible to his heir, Chad?
2. Art engages the services of Ben, a lawyer, to defend him on a case. If Ben dies before the case is heard, is the obligation of B to defend Art transmissible to his son?
3. Cory entered into a contract with Lupita whereby Cory agreed to sell her bungalow to Lupita for P800,000 on June 30, 2002. They stipulated that in case either one of them dies before that date, the right or obligation of the deceased shall not pass to her heirs. Cory died before June 30, 2002. Could their heirs be compelled to sell the bungalow to Lupita?
4. Martin, Fred and Carlos are partners in a duly organized partnership contributing P1M each to the common fund. In case, Martin dies, the partnership shall be dissolved. Can the heirs become partners in the stead?
5. Barrera is indebted to Padilla in the amount of P1,000,000. Upon Barrera's death, he leaves properties valued at P600,000 to his son Ricardo. Is Ricardo liable to pay Padilla the amount of P600,000, the value of the property which he inherits from his father Barrera? Can Padilla compel Ricardo to pay the balance of P400,000?

Cases when strangers or third persons affected by a contract

A *third person* is one who has not taken part in a contract and is, therefore, a stranger to the contract. As a general rule, a third person has no rights and obligations under a contract to which he is a stranger. He has no standing in law to demand the enforcement of a contract or question its validity.

There are cases, however, when third persons may be affected by a contract. Among such cases are the following:

- (a) In contracts containing a stipulation in favor of a third person (*stipulation pour autrui*);
- (b) In contracts creating real rights;
- (c) In contracts entered into to defraud creditors; and
- (d) In contracts which have been violated at the inducement of a third person.

Stipulation pour autrui - It is a stipulation in a contract clearly and deliberately conferring a favor upon a third person who has a right to demand its fulfillment provided he communicates *his* acceptance to the obligor before its revocation.

Example: Tom leased his house to Abel for 2 years at an agreed rental of P10,000 a month. They stipulated that the P10000 monthly rental should be given to Mar, a godson of Tom, as his monthly allowance. Mar communicated his acceptance of the benefit to Abel, the debtor, before Tom could revoke the same.

The stipulation in the contract between Tom and Abel expressly granting a benefit to Mar who accepts the same is known as stipulation pour autrui.

Article 1312. In contracts creating real rights, third persons who come into possession of the object of the contract are bound thereby, subject to the provisions of the Mortgage Law and the Land Registration Laws.

Article 1313. Creditors are protected in cases of contracts intended to defraud them.

Article 1313 is another qualification to the rule that contracts take effect only between the parties. The creditor is given the right to impugn the contracts of his debtor intended to defraud him.

Example: Dina is indebted to Cita in the amount of P800,000.00. Dina sells a parcel of land to Tom in order that Cita may not attach the land in payment of his debt and Dina has no other property.

Cita, who is a stranger to the contract between Dina and Tom, is given by law the right to ask for the rescission or cancellation of the sale in order that he may be paid his claim.

Article 1314. Any third person who induces another to violate his contract shall be liable for damages to the other contracting party.

Example: Sam agreed to sell his parcel of land to Bert for P900,000.00. Sam sells the land to Charlie instead because of the inducement of Dina.

In this case, Bert can sue Dina for damages. However, the liability of Dina for damages cannot be more than that of Sam for the latter's violation of his contract. To hold Dina liable for damages in excess of those that can be recovered against Sam "would lead to a result at once grotesque and unjust."

Article 1315. Contracts are perfected by mere consent, and from that moment the parties are bound not only to the fulfillment of what has been expressly stipulated but also to all the consequences which, according to their nature, may be keeping with good faith, usage and law.

Article 1316. Real contracts, such as deposit, pledge and commodatum, are not perfected until the delivery of the object of the obligation.

Classification of contracts according to perfection

Consensual contract or that which is perfected by mere consent (*e.g.*, sale, lease, agency)

Real contract or that which is perfected by the delivery of the thing subject matter of the contract (*e.g.*, deposit, pledge, commodatum, etc.)

Solemn contract or that which requires compliance with certain formalities prescribed by law, such prescribed form being thereby an essential element thereof (*e.g.*, donation of real property which must be in a public instrument)

Examples:

1. Today Sam and Bert enter into a contract whereby Sam binds himself to sell his car to Bert for P300,000.00. Is the contract deemed perfected although there has yet no delivery of the car and payment of the price made?
2. Dina borrowed from Cita P200,000.00. As security for the debt, Dina promised to pledge his diamond ring to Cita. Before the delivery of the ring to Cita, is the contract of pledge perfected? If Dina later on refuses to pledge the ring, can Cita demand the payment of the obligation although it is with a period? Can Cita require Dina to deliver the ring as security?

Effect of perfection of the contract

From the moment the parties come to an agreement on, a definite subject matter and valid consideration, they are bound not only —

(1) to the fulfillment of what has been expressly stipulated but also

(2) to all the consequences which according to their nature, may be in keeping with good faith, usage, and law.

Example: Sam agreed to sell his horse to Bert. It was stipulated that Sam should deliver the horse to Bert the next day. What is Sam's obligation then?

Article 1317. No one may contract in the name of another without being authorized by the latter, or unless he has by law a right to represent him.

A contract entered into in the name of another by one who has no authority or legal representation, or who has acted beyond his powers, shall be unenforceable, unless it is ratified, expressly or impliedly, by the person on whose behalf it has been executed, before it is revoked by the other contracting party.

Unauthorized contracts are unenforceable.

As a general rule, a person is not bound by the **contract** of another of *which* he has no knowledge or to which he has not given his consent. A contract involves the free will of the parties and only he who enters into the contract can be bound thereby (see Art. 1311, par. 1.)

Thus, a contract entered into in the name of another **by** one who has no authority is unenforceable against the former unless it is ratified by him before it is revoked by the other contracting party.

An unauthorized contract is not to be confused with a contract for the benefit of a third person who may demand its fulfillment provided the requisites mentioned are present.

Unauthorized contracts can be cured only by ratification

The mere lapse of time cannot give efficacy to such a contract. The defect is such that it cannot be cured except by the subsequent ratification of the person *in whose name* the contract was entered into or by his duly authorized agent and not by any other person not so empowered.

The ratification must be clear and express so as not to admit of any doubt or vagueness.

Example: Jim owns a motor boat. His friend, Archie, without the knowledge and consent of Jim, enters into a contract of sale of the motor boat with Ben for P800,000. After the perfection of the contract, Ben goes to Jim to pay P800,000 for the motor boat and demand its delivery. Jim refuses to accept the payment and to deliver the motor boat to Ben. Under the circumstances, can Ben juridically compel Jim to accept the payment and deliver the boat? Supposing Jim knowing all the facts regarding the transaction accepts the payment for the motor boat, can Ben enforce the contract against him so as to compel him to deliver the boat?

When a person is bound by the contract of another.

In order that a person may **be** bound by the contract of another, there are two requisites:

1. The person entering into the contract must be duly authorized, expressly or impliedly, by the person in whose name he contracts *or* he must have, by law, a right to represent him (like a guardian or an administrator); *and*
2. He must act within his power. A contract entered into by an agent in excess of his authority is unenforceable against the principal, but the agent is personally liable to the party with whom he contracted where such party was not given sufficient notice of the limits of the powers granted by the principal.

Example: Pat authorized Ann to sell his car for P400,000.00 cash. Ann sold the car to Che for P400,000.00 payable in ten (10) monthly installments. Can Che compel Pat to accept the monthly installments and to deliver the car?