OBLIGATIONS AND CONTRACTS 1A

2S, 24-25

Consolidated codal, case law, and commentary

Codal | Commentary | Case law

Title I
Obligations

Chapter 1
General Provisions

Definition;
3 prestations

Art. 1156

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

Why is the definition of an obligation, under the law, incomplete?

- It does not tell the actors.
- It just gives the object or prestation of an obligation (to give, to do, or not to do).
- The NCC just tells you that it's a juridical necessity plus the prestation.

Prestations:

1. To give (+)
2. To do (+)
3. Not to do (-)

Definition

An obligation is a juridical relation whereby a person (creditor) may demand from another (debtor) the observation of a determinative conduct (the prestation), and in case of breach, may demand satisfaction from the assets of the latter (*MKSE v. Campos*).

- *"Juridical"* – legal.
  - This gives rise to the compulsory aspect to the obligation.

Elements of a civil obligation

Elements of a civil obligation ♥

1. Creditor or obligee who can demand the performance of the prestation
2. Debtor or obligor who is bound to perform the prestation
3. Object of prestation (to give, to do, or not to do)
4. *Vinculum juris* or the juridical tie between the creditor and the debtor

⚠ *A civil obligation exists upon the concurrence of the elements. Always check: Is there an obligation? If there's a missing requisite, then, there's no obligation.*

De Leon v. Manulife, G.R. 243733, January 12, 2021

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The cause is the *vinculum juris* or juridical tie that essentially binds the parties to the obligation.

- In insurance, the *vinculum juris* is the insurance policy, which shall constitute the *entire* contract between the parties (§227, Insurance Code).
- What's not included in the policy is not a binding obligation or rule.

Elements 1-2: the parties

Parties

1. Creditor/obligee
2. Debtor/obligor

⚠ ***The parties must either be determinate or determinable.***

1. Determinate – The identity is specified in the source of obligation.
2. Determinable – The identity can be specified upon performance (e.g. the bearer of this promissory note)

Case 1: A promissory note

- An obligation based on a contract.
- The obligation is to pay the principal and the interest.
- **Determinate creditor and debtor.**
- "Without need of any notice or demand" – To trigger default in case of delay.

Case 2: Deed of sale

- A **reciprocal obligation**.
- Seller sells the property, buyer pays the price.
  - Identify the prestation to identify the parties.

Case 3: Payment of income tax

- **Determinable debtor** – Whoever will pay tax by the end of the year

at certain brackets.

Element 3: prestation

Prestation

To give, to do, or not to do – somehow this enumeration contains all the prestation

1. To give
    a. Sale (convey land and pay)
    b. Lease (to allow use of property and to pay rent)
    c. Donate (to give a property for free by the donor)
2. To do
    a. Performance of a positive undertaking
    b. Rendition of professional service
3. Not to do
    a. A negative pledge in a contract
        i. *E.g.,:* The borrower agrees not to encumber the property, or an undertaking not to dispose of a property within a certain period (bawal isangla o ibenta)

Element 4: juridical tie

Juridical tie

An efficient cause provided by the various sources of obligation (Art. 1157).

- An element of the obligation that compels the debtor to perform
- Entitles the creditor to exact performance from the debtor

Sources of juridical tie:

1. Law
2. Contracts
3. Quasi-contracts
4. Delicts (crimes/felonies)
5. Quasi-delict

Remedies

Creditor's basic remedies ♥

1. Specific performance – The debtor's fulfillment of the prestation under the obligation.
2. Resolution or rescission under Art. 1191 – Completely setting aside of a reciprocal obligation based on substantial breach.
3. Damages – It can be:
    a. A remedy itself (damages alone), or
    b. Combined with specific performance or resolution

Other remedies

1. Subsidiary – May only be done once the basic remedies have been exhausted but unavailing
    a. *Accion subrogatoria* (Art. 1177) – Creditor exercises certain rights of action of the debtor.
        i. *Ex.:* If the debtor has pending receivables, the creditor may step in and collect that on behalf of the debtor.
    b. *Accion pauliana* – Rescission based on fraud (Arts. 1177, 1381).
        i. *Ex.:* If a debtor disposes of assets to avoid paying debts—such as selling property to a relative for a low price or gifting assets—the creditor can file an acción pauliana to annul the transaction and recover what is due.
2. Ancillary
    a. Attachments
    b. Replevin
    c. Garnishments
    d. Receivership

Buenviaje v. Sps. Salonga, G.R. 216023, October 5, 2016

Specific performance – The remedy of requiring exact performance of a contract in the specific form in which it was made, or according to the precise terms agreed upon.

Resolution – The unmaking of a contract for a legally sufficient reason.

- It restores the parties to their original positions as if no contract has been made.
- Resolution will not be permitted for a slight or casual breach, but only for substantial and fundamental violations.

Rescission – A remedy granted by law to the contracting parties and even to third persons, to secure the reparation of damages caused to them by a contract, even if this should be valid, by restoration of things to their condition at the moment prior to the celebration of the contract.

- It implies a contract that produces *pecuniary* damage to someone.
- Where the defendant makes good the damages caused, the action cannot be maintained.
    - Hence, once Jebson delivers Unit 5 to Buenviaje, the latter can no longer claim rescission (i.e,. to return the payment),

because the obligation has already been fulfilled.

Art. 1157 ⭐

Obligations arise from:
(1) Law;
(2) Contracts;
(3) Quasi-contracts;
(4) Acts or omissions punished by law; and
(5) Quasi-delicts

JSP: Law and contracts lang daw talaga 'to.

Similar obligations may arise from, or be based on, different sources.

In such cases, it is necessary to identify the source or basis of the obligation to determine what law or contract will govern the obligation.

- The party asserting an obligation must identify the source of obligation in Art. 1157 (which is an exclusive list).

An act or omission of a person can create two or more obligations arising from different sources.

- *Example:* An owner-driver of a Grab has a condition of carriage with the passenger. If the owner-driver negligently drove the vehicle and figured in an accident resulting injuries to the passenger, the owner-driver will have obligations arising from:
  - Contract (breach of the conditions of carriage)
  - Felony (reckless imprudence)
  - Tort liability or quasi-delict (negligence)

Practice or customs

Makati Stock Exchange Corp. v. Campos, G.R. 138814, April 16, 2009

A practice or custom is, as a general rule, not a source of a legally demandable or enforceable right.

- The items in Art. 1157 is exclusive.

Bicol Medical Center v. Botor, G.R. 214073, October 4, 2017

Customary use is not one of the sources of legal obligation; hence, it does not ripen into a right.

- Hence, an injunction may not be issued based on a custom.

Exception: In labor law, an employee benefit arising from a longstanding employer practice is an obligation.

- Art. 100 of the Labor Code prohibits the elimination or diminution of benefits.
- Hence, the practice becomes an obligation based on law (Labor Code).

Costs–not an obligation!

Norsk v. Premier, G.R. 226771, September 16, 2020

The costs of a suit do not partake the nature of a loan or forbearance of money, or even an obligation, which is demandable by a party against another under Art. 1156 in relation to Art. 1157.

- But when the courts award costs, it becomes an obligation to pay it because judicial decisions, upon finality, are laws.
  - Costs are discretionary upon the court.

Law

Art. 1158

Obligations derived from law are not presumed. Only those expressly determined in this Code or in special laws are demandable, and shall be regulated by the precepts of the law which establishes them; and as to what has not been foreseen, by the provisions of this Book.

Absolute rule: Only obligations expressly provided in the law are demandable.

For an obligation derived from law to arise, the law should expressly recognize or impose the obligation. The obligation will not be presumed from the law.

Illustrative example: Taxation

- The obligation to pay taxes must be explicitly provided therein because tax laws are strictly construed against the government.
- In the case of tax exemption, a taxpayer cannot claim exemption from whatever that's not in the law. Corollarily, exemptions are construed against the taxpayer.

OSG v. ALI, G.R. 177056, September 18, 2009

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There is nothing in the NBC or its IRR pertaining to collection (or noncollection) of parking fees by the respondents. In fact, "parking fees" cannot be found in the NBC and IRR.

- Hence, the total prohibition against the collection by respondents of parking fees from persons who use the mall parking facilities has no basis in the National Building Code or its IRR.

Art. 1159

Obligations arising from contracts have the force of law between the contracting parties and should be complied with in good faith.

Contracts – Two parties (at least) agree on an exchange of prestation.

- 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 (Art. 1305, NCC).

Requisites of a contract:

1. Consent of the parties
2. Object
3. Cause

What does the obligatory force of a contract mean?

- Consent! Once parties consent, they cannot renege. That makes it obligatory on each party.
- Art. 1159 gives contracts a binding effect.
  - "Have the force of law"

How must parties fulfill their obligations under a contract?

- In good faith.
- The law is a set of default/background rules. If parties enter a specific act/omission, there are specific rules to apply. They can opt-out by contract, or they are mandatory. This obligation of a contracting party to act in good faith is part and parcel of a contract.
  - There's no need to stipulate good faith.

What is good faith performance of an obligation?

- Absence of malice and the absence of design to defraud or to seek an unconscionable advantage
- An honest belief
- Honesty of intention, and freedom from knowledge of circumstances which ought to put the holder upon inquiry

In the instance where contract > law

Benson v. Benson, G.R. 200746, August 6, 2014

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Obligations arising from contracts have the force of law between the contracting parties and thus should be complied with in good faith.

- Hence, the parties are bound by the stipulations, clauses, terms and conditions they have agreed to.
- The only limitation is that these stipulations are not contrary to law, morals, public order, or public policy.
  - Hence, if the CBA provides better benefits than the minimum provided by law, the CBA prevails!

Consent

PCSO v. Mendoza, G.R. 257849, March 13, 2023

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Crucial in the law of contracts is the consent of the parties, which is manifested by the (1) meeting of the offer and the (2) acceptance upon the thing and the (3) cause which are to constitute the contract. The offer must be certain and the acceptance absolute.

Construction of contracts – When a contract is ambiguous, then the interpretation of the contract is left to the court. A contract provision is ambiguous if it is susceptible to two reasonable alternative interpretations.

'Good faith'

Torres v. GSIS, G.R. 225920, April 3, 2024

The Civil Code is replete with references to good faith, with the constant caution of the particularly corrosive effect of bad faith and malice in the ways that we relate to each other's rights and duties.

The Civil Code requires that every contract be complied with in good faith, and for every party to exert all efforts to that end.

May a court modify the contractual stipulations of the parties?

- No. Except:
  - Unconscionable interest (3% per month interest is unconscionable), unreasonable penalty, or excessive legal fees.
    - The court does not completely void the stipulation but only modify it by reducing the stipulated rates or amounts.
  - Public interest (police power)

- The court must respect the stipulation of the parties because the contract is the law between the parties.

Quasi-contracts

Art. 1160

Obligations derived from quasi-contracts shall be subject to the provisions of Chapter 1, Title XVII, of this Book.

Quasi-contract – Is a juridical relation that the law creates, on the basis of voluntary (vs. quasi-delict), unilateral (vs. contracts), and lawful acts (vs. delicts), to prevent unjust enrichment.

(Some) types of quasi-contracts:
1. Negotiorum gestio
2. Solutio indebiti

The enumeration in the NCC is *nonexhaustive*. So long as something fits the definition, it can be a quasi-contract.

Negotiorum gestio (officious management)– A person without contractual relation with the owner manages the property of that owner (Art. 2144, NCC).
- The manager does this without power from the owner.
- To prevent unjust enrichment, the manager must be compensated.

Requisites of negotiorum gestio:
1. The property or business has been abandoned
2. The manager should not have been tacitly authorized by the owner

Solutio indebiti

Metrobank v. Absolute, G.R. 170498, January 9, 2013

A quasi-contract involves a juridical relation that the law creates on the basis of certain voluntary, unilateral and lawful acts of a person, to avoid unjust enrichment.

Solutio indebiti – This arises when something is delivered through mistake to a person who has no right to demand it. It obligates the latter to return what has been received through mistake.

Requisites of solutio indebiti:
1. Something has been unduly delivered through mistake; and
2. Something was received when there was no right to demand it

JSP: It's actually negligence (why Chua was able to encash the checks). The bank fell short of the diligence required by law.

Domestic v. MIAA, G.R. 210641, March 27, 2019 ♥

In order to establish the application of *solutio indebiti* in a given situation, two conditions must concur:
1. a payment is made when there exists no binding relation between the payor who has no duty to pay, and the person who received the payment, and
2. the payment is made through mistake, and not through liberality or some other cause.

Hence, because MIAA and DPRC have a contract of lease, the first requisite falls. Moreover, payment in protest and with the belief that the price escalation is valid is not payment by mistake (second requisite fails).

Illustrative example (*solutio indebiti*): Somebody was supposed to get a check for a few hundred dollars. The bank made a mistake and made it millions. That's a classic case of *solutio indebiti*. There was a contract, but the bank made excessive payments.

Delicts

Art. 1161

Civil obligations arising from criminal offenses shall be governed by the penal laws, subject to the provisions of article 2177, and of the pertinent provisions of Chapter 2, Preliminary Title, on Human Relations, and of Title XVIII of this Book, regulating damages.

Death of an accused;
Effect on liability ex-delicto

Republic v. Desierto, G.R. 136506, January 16, 2023

Death of the accused pending appeal of his conviction extinguishes his criminal liability and the civil liability based thereon.

The claim for civil liability survives notwithstanding the death of the accused, if the same may also be predicated on a source of obligation other than delict.
- When the civil liability survives, an action for recovery therefor may

be pursued but only by way of filing a separate civil action.
- This separate civil action may be enforced either against the executor/administrator of the estate of the accused, depending on the source of obligation upon which the same is based.

Quantum of proof required:
1. Civil cases – Preponderance of evidence
    a. Fraud – Clear and convincing evidence
2. Criminal cases – Proof beyond reasonable doubt

You have to choose what will suit your objective, if you have different sources of obligations (Grabcar example).

Multiple sources of obligations;
Civil liability ex-delicto;
Effect of acquittal

De Leon v. Roqson, G.R. 234329, November 23, 2021

An acquittal on reasonable doubt does not necessarily extinguish civil liability, it also does not mean that the civil liability of the acquitted nonetheless automatically survives.

Instead, care must still be taken in determining whether a civil liability persists as traced back to another source of obligation under Arti. 1157, NCC.
- Hence, an accused who was acquitted from a BP 22 violation may still face civil liability if he acted as an accommodation party of a corporate debt. In this case, the obligation's source is now the law (Negotiable Instruments Law).
- Contractual, criminal, or civil obligations may arise from bounced checks

JSP: Contractual, criminal, and civil obligations may arise from bounced checks (BP 22).

Quasi-delicts

Art. 1162

Obligations derived from quasi-delicts shall be governed by the provisions of Chapter 2, Title XVII of this Book, and by special laws.

An act or omission of a person can create two or more obligations arising from different sources.

Examples:
1. Vehicular accident of a public transport system (contractual, delict, and quasi-delict)
2. Bouncing checks (contractual, delict)

Liability quasi-delicto;
Prohibition on double recovery

Fegarido v. Alcantara, G.R. 240066, June 13, 2022

A single act or omission causing injury to another creates two kinds of liability:
1. Civil liability ex-delicto
2. Civil liability quasi-delicto

The aggrieved party may choose to enforce either liability against the erring party, subject only to the prohibition against double recovery of damages.

An independent civil action, such as that based on quasi-delict under Art. 2176, NCC, no longer requires a prior reservation to be made before it can proceed independently and be tried simultaneously with its concomitant criminal action.

Environmental tort

Sanggacala v. NAPOCOR, G.R. 209538, July 7, 2021
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Tort law can be used to address environmental harms to a well-defined area or specific person, or a class of persons, when readily supported by general and specific causation and closely fits the traditional elements of a tort cause of action.

Quasi-delict or culpa aquiliana – The wrongful or negligent act or omission which creates a vinculum juris and gives rise to an obligation between two persons not formally bound by any other obligation.

Elements of a quasi-delict:
1. Damages suffered by the plaintiff
2. Fault or negligence of the defendant
3. The connection of cause and effect between the fault or negligence of the defendant and the damages incurred by the plaintiff.

Damnum absque injuria – Damage without injury.

- Arises when the loss or harm was not the result of a violation of a legal duty.
- When this occurs, the consequences must be borne by the injured person alone, since there is no remedy for damages resulting from an act which does not amount to a legal injury or wrong.

Chapter 2
Nature and Effect of Obligations

Art. 1163

Every person obliged to give something is also obliged to take care of it with the proper diligence of a good father of a family, unless the law or the stipulation of the parties requires another standard of care.

Determinate/specific vs. generic/indeterminate thing

Determinate/specific – Particularly designated or physically segregated from all others of the same class.
- Identified by its individuality.
- The debtor cannot substitute it with another although the latter is of the same kind and quality *without the consent of the creditor*.

Generic/indeterminate – The thing refers only to a class or genus to which it pertains and cannot be pointed out with particularity.
- Identified by its specie.
- The debtor can give anything of the same class as long as it is of the same kind.

Duties of a debtor in obligation to give a determinate thing
1. To preserve or take care of the thing due
2. To deliver the fruits of the thing
3. To deliver its accessions and accessories
    a. Accessions – Improvements
    b. Accessories – Embellishments for better use or completion
4. To deliver the thing itself
5. To answer for damages in case of nonfulfillment or breach

Duties of debtor in obligation to deliver a generic thing
1. To deliver a thing which is of the quality intended by the parties taking into consideration the purpose of the obligation and other circumstances.
2. To be liable for damages in case of fraud, negligence, or delay in the performance of his obligation, or contravention of the tenor thereof.

"Obliged to take care of it"
1. **Diligence of a good father of a family** – Ordinary care or that diligence which an average, reasonably prudent person, exercises over his own property.
2. **Other standards of care**:
    a. *Common carriers* – Utmost (extraordinary) diligence of very cautious persons, with a due regard for all the circumstances.
    b. *Banks* – Highest degree of care when the fiduciary relationship is involved.
        i. *Banks exercising commercial transactions* → The highest degree of care is not expected because the fiduciary relationship is not involved.

Debtor's* obligations in an obligation *to give
1. Perform the mandated prestation in good faith by delivering the property subject of the obligation to give.
2. Deliver the fruits of the property to be delivered from the time the obligation to deliver it arises.
3. Prior to the delivery, the debtor must take care of the thing using ordinary diligence.
4. If the object of the obligation to give is a determinate property, the debtor should also deliver its accessions and accessories.

Creditor's* rights in an obligation *to give
1. To demand–
    a. Specific performance
    b. Substitute performance, if indeterminate thing, at the cost of the debtor
        i. The prestation may be performed by another party.
2. Personal right [1] to the fruits of the property on the mandated date of delivery
3. Right to accessions and accessories of the thing
4. In case of substantial breach and as an alternative to SP, to resolve (resolution) the obligation
5. In case of breach, claim damages vs. the debtor, whether with a demand for SP, or resolution (if the breach is substantial)

[1] Two rights:
1. **Personal right** (jus in personam or jus ad rem) – The right or power of a person (obligee) to demand from another (obligor), as a definite and passive subject, the fulfillment of the latter's obligation to give, to do, or not to do.

2. **Real right** (jus in re) – The right or interest of a person over a specific thing (e.g., ownership, possession, mortgage, lease) without a definite passive subject against whom the right may be personally enforced.

Class example 1:
Buyer → D1: P10 million
Buyer → D3: P10 million
Seller → D3: Orchard (consideration of P20 million) defaults

- On D3, the seller sells the fruits of the orchard to X.

In this case, the right of the buyer to the fruits will be enforceable against the seller only, not to X. Buyer cannot reclaim the fruits from X!

Class example 2:
Seller planned to sell a BMW with plate number AAA0000. However, a day before the scheduled delivery to the buyer, the seller removed the carpets and stereo system of the car.

- Seller is obligated to deliver all the accessions and accessories of the thing in good faith.

To give

Art. 1164

The creditor has a right to the fruits of the thing from the time the obligation to deliver it arises. However, he shall acquire no real right over it until the same has been delivered to him.

Kinds of fruits

1. **Natural** – The spontaneous products of the soil, and the young and other products of animals (e.g., grass).
2. **Industrial** – Those produced by lands of any kind through cultivation of labor (e.g., vegetable, rice).
3. **Civil** – Those derived by virtue of a juridical relation (e.g., rents of buildings, price of leases of lands)

When the obligation to deliver arises

1. General rule: It arises from the perfection of the contract
    a. Perfection – Birth of the contract or to the meeting of the minds between parties
2. If subject to a suspensive condition or period → upon fulfillment of the condition or arrival of the period
3. In contract of sale → upon the perfection of the contract, notwithstanding a suspensive condition/period
4. When based on law, quasi-contracts, delicts, and quasi-delicts → upon the specific provision of the law

"He shall acquire no right over it until the same has been delivered to him" – The creditor does not become the owner until the specific thing has been delivered.

- Hence, if there is no delivery yet, the remedy should be SP, and not recovery of possession and ownership.

Remedies of creditors;
To give

Art. 1165

When what is to be delivered is a determinate thing, the creditor, in addition to the right granted him by Article 1170, may compel the debtor to make the delivery.

If the thing is indeterminate or generic, he may ask that the obligation be complied with at the expense of the debtor.

If the obligor delays, or has promised to deliver the same thing to two or more persons who do not have the same interest, he shall be responsible for any fortuitous event until he has effected the delivery.

Pars. 1-2

Remedies of creditor in real obligations

1. For specific real obligation:
    a. SP or fulfillment with a right to indemnity for damages
    b. Resolution or cancellation with a right to recover damages
    c. Demand payment of damages only

    In any case, only the debtor can comply with the obligation.
2. Generic real obligation:
    a. Can be performed by a third person
    b. It's not necessary for the creditor to compel the debtor to make the delivery though he may ask for the performance of the obligation
    c. Nevertheless, the creditor can still recover damages

Par. 3 – Exceptions to a fortuitous event

Two instances when a fortuitous event does not exempt the debtor from responsibility:

1. The obligor has delayed delivery
2. The obligor has promised to deliver the same thing to 2 or more

persons who do not have the same interest

Correlate this with Art. 1174 (on fortuitous events).

To give

Art. 1166

The obligation to give a determinate thing includes that of delivering all its accessions and accessories, even though they may not have been mentioned.

1. **Accessions** – The fruits of, or additions to, improvements upon, a thing (e.g. house or trees on a land).
2. **Accessories** – Things joined to, or included with, the principal thing for the latter's embellishment, better use, or completion (e.g. key of a house, bracelet of a watch).

While accessions are not *necessary* to the principal thing, the accessory and the principal thing must go together but both accessions and accessories can exist only in relation to the principal.

Right of creditor to accessions and accessories

- General rule: All accessions and accessories are considered included in the obligation to deliver a determinate thing.
    - An obligation to deliver the accessions or accessories of a thing does not include the latter
    - Hence, a sale of a house does not cover title or any right over the land.

To do

Art. 1167

If a person obliged to do something fails to do it, the same shall be executed at his cost.

This same rule shall be observed if he does it in contravention of the tenor of the obligation. Furthermore, it may be decreed that what has been poorly done be undone.

Situations contemplated in Art. 1167:

1. The debtor fails to perform an obligation to do
2. The debtor performs an obligation to do, but contrary to the tenor thereof
3. The debtor performs an obligation to do, but in a poor manner

Remedies of creditor in positive personal obligation

1. If the debtor fails to comply with his obligation to do, the creditor may:
    a. To have the obligation performed by himself, or by another, at the debtor's expense; and
    b. Recover damages.
2. In case the obligation is done in contravention of the terms of the contract or poorly done, it may be ordered by the court that it be undone, if possible.

Performance by a third person

A personal obligation *to do* can be performed by a third person.

1. SP is prohibited in a personal obligation to do, because this can be involuntary servitude.
2. Where the personal qualifications of the debtor are the determining motive for the obligation contracted, the performance of the same by another is impossible. Hence, damages may be recovered.

Debtor's obligations in an obligation to do

1. Perform the mandated prestation in good faith.

Creditor's rights in an obligation to do

1. Compel specific performance (unless involuntary servitude in which case, damages only), or substitute performance if the service is not strictly personal
2. Demand rectification of faulty or defective service by the debtor or by another party at the cost of the debtor
3. In case of substantial breach and as an alternative to specific/substitute performance, resolve the obligation
4. Claim damages only

Not to do

Art. 1168

When the obligation consists in not doing, and the obligor does what has been forbidden him, it shall also be undone at his expense.

Debtor's obligations in an obligation not to do

1. To refrain from doing the prohibited act.

Creditor's rights in an obligation not to do

1. Enjoin the prohibited act
2. Obtain a reversal, if possible
3. In case of breach, claim damages

Hirakawa v. Lopzcom, G.R. 213230, December 5, 2019

Breach of contract may arise to an action for specific performance, rescission of contract, or a complaint for damages.

1. **Specific performance** – The remedy of requiring exact performance of a contract in the specific form in which it was made, or according to the precise terms agreed upon. It is the actual accomplishment of a contract by a party bound to fulfill it.
2. **Rescission** – A remedy available to the obligee when the obligor cannot comply with what is incumbent upon him. It is predicated on a breach of faith by the other party who violates the reciprocity between them. Rescission may also refer to a remedy to secure reparation of damages caused by a valid contract; by means of restoration of things to their condition in which they were prior to the celebration of the contract.

Resolution vs. rescission

Basis of comparison	**Resolution**	**Rescission**
Who may avail	Only a party to the obligation	A third person (creditor) may avail
Grounds	Nonperformance by the other party	Fraud, lesion, or other grounds
Court's discretion	May be refused on valid grounds	Cannot be refused if all requisites are present
Nature of remedy	Primary	Subsidiary
Basis	Mutuality of the parties	Prejudice or damage suffered

Nuñez v. Moises-Palma, G.R. 224466, March 27, 2019

The remedies of the unpaid seller, after ownership of the real property has been vested to the buyer are:

1. Compel specific performance
2. To rescind or resolve the contract of sale either judicially or by a notarial act
3. Recover damages for the breach of contract

When resolution is sought, the obligation to return the things which were the object of the contract, together with their fruits, and the price with interests is created per Art. 1385, NCC.

In this case, resolution was proper because of substantial breach–the respondent did not pay the obligation at all.

Substantial breach vis-a-vis resolution

Substantial breach – When the debtor violates an essential cause for the other party (e.g., fulfillment of the price).

- **JSP:** Substantial payment is 80-85% of the principal. Anything less, there would not be a substantial breach, only a slight or casual breach.
    - This means, resolution isn't proper, but just SP.

Lara's Gift v. Midtown, G.R. 225433, September 20, 2022 ♥

When an obligation, regardless of source, is breached, the contravenor can be held liable for damages.

Two kinds of interests:

1. **Conventional** – The interest agreed to by the parties themselves. It is allowed only if the following conditions concur:
    a. There is an express stipulation for the payment of interest, and
    b. The stipulation for the payment of interest is in writing.
2. **Compensatory** – (a.k.a. penalty interest, indemnity, or moratory interest) The indemnity for damages arising from delay on the part of the debtor in an obligation consisting in the payment of a sum of money.
    a. It need not be expressly stipulated in writing.
    b. It can be stipulated through a penalty or penal clause.

The **applicable compensatory interest** in contracts consisting in the payment of a sum of money should be determined as follows:

1. If there is a penal clause that stipulates the penalty or indemnity, follow that stipulation
2. If there is no penal clause, but there is a stipulation on conventional or monetary interest, then the said interest applies
3. If there is no stipulation on the penalty or on the conventional interest, then the legal interest rate shall be applicable (6% p.a. for a

simple loan of money)

Stipulated interest rates–whether conventional or compensatory–are subject to the **"unconscionability" standard**.

- The maximum interest rate that will not cross the line of conscionability is not more than twice the prevailing legal rate of interest.
- If the stipulated interest exceeds this standard, the creditor must show that the rate is necessary under current market conditions.
- The creditor must also show that the parties were on an equal footing when they stipulated on the interest rate.

Skipping Art. 1169, we'll come back to it later!

Damages

Art. 1170 ⭐

Those who in the performance of their obligations are guilty of fraud, negligence, or delay, and those who in any manner contravene the tenor thereof, are liable for damages.

Four grounds for liability which may entitle the injured party to **damages for whatever source of obligation**:

1. Fraud
2. Negligence
3. Delay
4. Contravention of the terms of the obligation

These apply whether the obligations are real or personal.

It contemplates that the obligation was eventually performed, but the obligor is guilty of breach thereof.

Fraud (deceit or dolo)

- The deliberate or intentional evasion of the normal fulfillment of an obligation.
- **JSP:** The conscious and intentional design to evade the normal fulfillment of existing obligations and is, thus, incompatible with good faith.

Negligence (fault or culpa)

- It is any voluntary act or omission, there being no bad faith or malice, which prevents the normal fulfillment of an obligation.
- It is the failure to exercise that degree of care required by the circumstances.
- It may result in *culpa aquiliana* or *culpa contractual*.

Delay (mora)

- The delay must either be malicious or negligent.

Contravention of the terms of the obligation

- Violation of the terms and conditions stipulated in the obligation
- The contravention must not be due to a fortuitous event or force majeure

Poole-Blunden v. Union Bank, G.R. 205838, November 29, 2017

There is fraud when, through insidious words or machinations of one of the contracting parties, the other is induced to enter into a contract which, without them, he would not have agreed to.

The fraud must be the determining cause of the contract, or must have caused the consent to be given (vitiation of consent).

JSP: When there is fraud, there is disparity in the information between the parties.

Classification of fraud

1. Civil fraud
    a. Fraud in the performance of an obligation. It entitles the creditor to remedies or damages.
    b. Fraud as a tort. It entitles the creditor to damages (Arts. 28, 33, NCC).
    c. Causal fraud, which vitiates consent. It renders the contract voidable (Art. 1390, NCC).
    d. Contract undertaken in fraud of a creditor. It renders the contract rescissible.
    e. Fraud that causes the failure of the written contract to express the true agreement of the parties. The contract will be subject to reformation.
2. Criminal fraud
    a. e.g., estafa

Proof of fraud

1. A question of fact
2. Circumstances constituting fraud must be alleged and proved by the creditor in an appropriate case or proceeding

3. Proven by clear and convincing evidence

JSP: Being a mental state of the debtor, fraud is more difficult to prove than the debtor's negligence, default or other contravention of the obligation. The creditor may establish fraud by showing facts from which may be inferred deceit, dishonesty, malice or bad faith.

Fraud vs. negligence

Basis of comparison	**Fraud** [1]	**Negligence**
With intention to cause damage/injury?	Yes	No
Voluntarily?	Yes	Yes
Waiver of the liability for future fraud void?	Yes	Allowed [2]
Presumed?	No, must be clearly proved by clear and convincing evidence	Yes, from the breach of a contractual obligation
Can courts mitigate liability?	No	Yes, according to the circumstances

[1] Being a state of mind, fraud may be inferred from the circumstances of the case.
[2] But not allowed for future gross negligence.

Breach of contract – The failure without justifiable excuse or reason to comply with the terms of a contract.
- It can be willful or unintentional.

Fraud;
Future fraud waivers

Art. 1171

Responsibility arising from fraud is demandable in all obligations. Any waiver of an action for future fraud is void.

Q: Why is a waiver for future fraud void?
A: Because it removes the obligatory force of a contract. There's no compulsion.

Q: May a creditor waive in advance an action based on the debtor's future negligence?
A: For simple negligence, **yes**. For gross negligence, **no**—it's tantamount to fraud and the law doesn't allow a waiver of action for future fraud.
- Gross negligence is equivalent to bad faith, and bad faith is fraud. Therefore, a waiver of an action based on future gross negligence is not allowed.

Infotech v. COMELEC, G.R. 159139, June 6, 2017


Based on its nature, actionable fraud may be criminal or civil.

Civil fraud – Can either be
- Fraud that gives rise to an action for damages (*e.g.* tort), or
- Fraud that creates a vice in the intent of one or more parties in juridical transactions
  - **Causal fraud** – Deceptions or misrepresentations of a serious character employed by one party and without which the other party would not have entered into the contract.

Criminal fraud – May pertain to the means of committing a crime, or the classes of crimes under Rev. Pen. Code, bk. 2, tit. IV & VII, ch. 3.

Poole-Blunden (*supra* art. 1170)


Two types of fraud in the performance of contracts:
1. Dolo incidente or **incidental** fraud
2. Dolo causante or **causal** fraud
   a. Here, there is vitiation of consent.
   b. The party to a contract whose consent was vitiated is entitled to have the contract rescinded.

Dumaran v. Llamedo, G.R. 217583, August 4, 2021 ♥

The nonpayment of a debt per se does not automatically equate to a fraudulent act.
- Being a state of mind, fraud cannot be merely inferred from a bare allegation of nonpayment of debt or nonperformance of obligation.

Negligence

Art. 1172

Responsibility arising from negligence in the performance of every kind of obligation is also demandable, but such liability may be regulated by the courts, according to the circumstances.

Art. 1173

The fault of negligence of the obligor consists in the omission of that diligence which is required by the nature of the obligation and corresponds with the circumstances of the persons, of the time and of the place. When negligence shows bad faith, the provisions of Articles 1171 and 2201, paragraph 2 shall apply.

If the law or contract does not state the diligence which is to be observed in the performance, that which is expected of a good father of a family shall be required.

Note that in fraud, responsibility is demandable in all obligations. However, when the case is negligence, the "liability may be regulated by the courts, according to the circumstances."

Kim v. Slimmers World International, G.R. 206306, April 3, 2024 ♥

Negligence – The failure to observe for the protection of the interests of another person, that degree of care, precaution and vigilance which the circumstances justly demand, whereby such other person suffers injury.

- It is the omission to do something which a reasonable man, guided by those considerations which ordinarily regulate the conduct of human affairs, would do, or the doing of something which a prudent and reasonable man would not do.

Negligence may either result in *culpa aquiliana* or *culpa contractual*. They generally cannot co-exist.

- Culpa aquiliana – Wrongful or negligent act or omission which creates a vinculum juris and gives rise to an obligation between two persons not formally bound by any other obligation.
- Culpa contractual – The fault or negligence incident in the performance of an obligation which already existed, and which increases the liability from such already existing obligation.

Burden of proof: Once a breach of contract is proved, the defendant is presumed negligent and must prove not being at fault. In a quasi-delict, the complaining party has the burden of proving the other party's negligence.

Ona v. Northstar International, G.R. 209581, January 15, 2020

🇪🇺✈️

To be exculpated from liability arising from contractual negligence, the person claiming moral damages must show that he was not negligent in carrying out the obligation.

- **Test:** Did the defendant in doing the alleged negligent act use that reasonable care and caution which an ordinarily prudent person would have used in the same situation?

Abrogar v. Cosmos, G.R. 164749, March 15, 2017

🏃🚗

Negligence as a source of obligation has the following requisites:

1. Damages to the plaintiff
2. Negligence by act or omission of which defendant personally or some person for whose acts it must respond, was guilty
3. The connection of the cause and effect between the negligence and the damage

Proximate cause – Is that which, in natural and continuous sequence, unbroken by any new cause (efficient intervening cause), produces an event, and without which the event would not have occurred.

- **Efficient intervening cause** – One not produced by a wrongful act or omission, but (1) independent of it, and (2) adequate to bring the injurious results.
    - Any cause intervening between the 1st wrongful cause and the final injury which might have been foreseen or anticipated by the wrongdoer is not such an efficient intervening cause.

Delay;
Default

Art. 1169 ⭐

Those obliged to deliver or to do something incur in delay from the time the obligee judicially or extrajudicially demands from them the fulfillment of their obligation.

However, the demand by the creditor shall not be necessary in order that delay may exist:

(1) When the obligation or the law expressly so declares; or
(2) When from the nature and the circumstances of the obligation it appears that the designation of time when the thing is to delivered or the service is to be rendered was a controlling motive for the establishment of the contract; or
(3) When demand would be useless, as when the obligor has rendered it

beyond his power to perform.

In reciprocal obligations, neither party incurs in delay if the other does not comply or is not ready to comply in a proper manner with what is incumbent upon him. From the moment one of the parties fulfills his obligation, delay by the other begins.

Default – The debtor's delay in the performance of the obligation on the due date upon:
a. Extrajudicial or judicial demand by the creditor, or
b. When demand is not necessary to place the debtor in default

In what obligations may a debtor default?
a. To give
b. To do

Default only occurs in positive obligations. When an obligation not to do is violated, that's a breach and not legal delay.

Requisites of default ♥
1. The debtor has a positive obligation (*see* Art. 1156)
2. The obligation is demandable and liquidated
3. The creditor judicially or extrajudicially demands
    a. This does not apply when demand is not necessary (see nos. 1-3, Art. 1169)
4. The debtor does not pay the obligation after receipt of the demand, or if demand is legally unnecessary, on the due date.

Default, requisites

Aclado v. GSIS, G.R. 260428, March 1, 2023

Requisites for debtor to be considered in default:
1. The obligation be demandable and already liquidated
2. The debtor delays performance
3. The creditor requires the performance, judicially or extra-judicially.

Default only begins from the moment the creditor demands the performance of the obligation.

Foreclosure only available when mortgagor-creditor in default

Sps. Rodriguez v. EIB, G.R. 214520, June 14, 2021

There are three elements before a creditor may proceed with extrajudicial foreclosure of a mortgage:
1. Failure to pay the loan
2. Loan obligation secured by a REM
3. The mortgagee-creditor has the right to foreclose the REM, either judicially or extrajudicially.

Subsumed in the first and third elements is the requirement that the mortgagor-creditor be in default.
- They can only be deemed in default when the latter fails to pay despite a valid demand by the mortgagee-creditor.

Judicial demand

Pineda v. De Vega, G.R. 233774, April 10, 2019

The obligor/debtor incurs delay from the time the obligee/creditor demands from him the fulfillment of the obligation.

The filing of a complaint (*e.g.* for collection) constituted the judicial demand upon the debtor to pay her principal obligation and the interest.

What are **instances when demand is not necessary** to place the debtor in default?
1. The parties stipulate to dispense with the necessity of demand
2. The law so provides
3. Time is of the essence
4. Demand is unnecessary

Illustrative examples

(1.1) Stipulation
- "Without need of notice of demand" must be written in the contract.
- They may also stipulate that the due date will trigger the debtor's default, i.e., interest will accrue from maturity date (*see Southstar v. PHES*).
- The stipulation of the due date alone does not dispense with the need for a demand!

(1.2) Law
- NIRC provides deadlines for filing of tax returns and payment of taxes
- Corporation Code's deadline for audited financial statements and general information sheet
- Social Security Act's deadline for employers' remittance of employee contributions
- Failure to fulfill the obligations to the due dates will automatically

give rise to penalties

(2) Time is of the essence

- A stipulation of a due date does not mean that time is of the essence in the performance of an obligation.
- The creditor must inform the debtor that the prestation must be done on a particular time, and the debtor must agree/accept it.
    - There must be an "actual flow of information"

(3) Demand is unnecessary

- The creditor's demand is not necessary if the debtor is in no position to fulfill the obligation on the due date.
- Demand is unnecessary if the debtor will not be able to fulfill his prestation on the due date.

Demand not required

Southstar v. PHES, G.R. 218966, August 1, 2022

There are four instances when demand is not necessary to constitute the debtor in default:

1. There's an express stipulation to that effect
2. When the law so provides
3. When the period is the controlling motive or the principal inducement for the creation of the obligation
4. When demand would be useless

In the first two instances, it must expressly state that after the period lapses, default will commence.

- Hence, the inclusion of a clause for payment of liquidated damages in the contract implies the waiver of a demand to put the debtor in default.

Default in reciprocal obligations ♥

Reciprocal obligation – The obligation of one is dependent upon the obligation of the other.

- The parties are mutual debtors and creditors of each other and they exchange prestations.
- For example, in a COS, there is simultaneous delivery of the object and payment of the price (*kaliwaan*).

What is the **timing of the performance** by the parties of the reciprocal obligations?

a. *Generally,* to be performed **simultaneously**, so that the performance of one is conditioned upon the simultaneous fulfillment of the other.
    i. Exception: If the parties agree on (or the law so provides) **successive performance** of their prestations (i.e., prestation 1, then, prestation 2).

Neither party incurs in delay if the other does not comply or is not ready to comply in a proper manner with what is incumbent upon him.

- The delay of each other cancels out.
- **Compensatio morae** – The liability of a party for damages is offset or, at least, tempered by the liability for damages of the other party (*see* Art. 1192).
    - It can *sometimes* be a complete extinction of the liabilities.
    - What you offset are the damages based on default—only damages on account of default will be offset.

Rule on simultaneous performance

1. If one party performs, and the other does not, the other party is automatically in default.
2. If one party is never ready, willing and able (RWA) to perform, the other party can never be in default.

Rules on successive performance

1. General rule: Demand is necessary (see Art. 1191).
2. The party entitled to the fulfillment of the prestation on the due date should demand fulfillment to place the other in default.

Why is it necessary to **reckon the time of default**?

1. It may give rise to additional obligations
2. Entitlement of compensatory damages/interests (*Lara's Gift*)
3. Acceleration of the payment of the entire obligation
4. Marks the accrual of the creditor's cause of action and the corresponding commencement of the prescriptive period of said action

Delay of the creditor

Mora accipiendi – Creditor rejects/refuses to accept a proper performance by the debtor of the prestation.

- Default caused by an act or omission of the creditor
- Default not in the performance of the obligation, but in the acceptance of a valid fulfillment of the debtor's prestation
- Does not extinguish the obligation.

Consequences of mora accipiendi:

1. Creditor shall bear the risk of damage to, or loss of, the object of the obligation.
2. The debtor shall remain liable for fraud or gross negligence.

   a. *Mora accipiendi* does not negate the juridical tie and does not entitle the debtor to act contrary to the mandate of the obligation
3. The creditor shall be liable for the debtor's cost of preserving the object of the obligation
4. The debtor can complete payment by judicial consignation of the object of the obligation
   a. Without consignation, the debtor remains liable for payment of interest even after he offered to pay and the creditor did not accept payment. This is because the debtor remained in use of the money he would've paid (conventional interest).

***No* mora accipiendi in:**

1. Borrower had the payment, but the lender did not collect. Lender continues to fail to collect.
   a. No delay because the lender's failure to demand only prevents the borrower's default (if demand is necessary).
2. Lender assigned his rights to the assignee. Borrower paid, but the lender refused. Lender informed the borrower of the assignment.
   a. No delay because the lender is no longer the correct payee–the assignee is.

Reciprocal obligations

Solar Harvest v. Davao Corrugated, G.R. 176868, July 26, 2010

In a reciprocal obligations (e.g., contract of sale), the fulfillment of the parties' respective obligations should be simultaneous.

- *Simultaneous:* No demand is necessary because once a party fulfills his obligation and the other does not, the latter automatically incurs delay.
- *Successive:* But if the period for the fulfillment of the obligation is fixed, demand upon the obligee is still necessary before the obligor can be considered in default and before a cause of action for rescission will accrue.

Richardson Steel v. UBP, G.R. 224235, June 28, 2021

With the refusal of UBP to release the loan proceeds under the CLA to the petitioners, it can be deemed that UBP reneged on its obligation under the CLA and failed to comply in the proper manner with what is incumbent upon it under contemplation of Article 1169 of the Civil Code.

Lara's Gift (*supra* art. 1168) ♥

1. In obligations consisting of loans or forbearances of money, goods or credit:
   a. The compensatory interest due shall be that which is stipulated by the parties in writing as the penalty or compensatory interest rate, provided it is not unconscionable. In the absence of a stipulated penalty or compensatory interest rate, the compensatory interest due shall be that which is stipulated by the parties in writing as the conventional interest rate, provided it is not unconscionable. In the absence of a stipulated penalty or a stipulated conventional interest rate, or if these rates are unconscionable, the compensatory interest shall be the prevailing legal interest rate prescribed by the Bangko Sentral ng Pilipinas. Compensatory interest, in the absence of a stipulated reckoning date, shall be computed from default, i.e., from extrajudicial or judicial demand, until full payment.
   b. Interest on conventional/monetary interest and stipulated compensatory interest shall accrue at the stipulated interest rate (compounded interest) from the stipulated reckoning point or, in the absence thereof, from extrajudicial or judicial demand until full payment, provided it is not unconscionable. In the absence of a stipulated compounded interest rate or if this rate is unconscionable, the prevailing legal interest rate prescribed by the Bangko Sentral ng Pilipinas shall apply from the time of judicial demand until full payment.

2. In obligations not consisting of loans or forbearances of money, goods or credit:
   a. For liquidated claims:
      The compensatory interest due shall be that which is stipulated by the parties in writing as the penalty or compensatory interest rate, provided it is not unconscionable. In the absence of a stipulated penalty or compensatory interest rate, or if these rates are unconscionable, the compensatory interest shall be at the rate of 6%. Compensatory interest, in the absence of a stipulated reckoning date, shall be computed from default, i.e., from extrajudicial or judicial demand, until full payment.
      - Interest on stipulated compensatory interest shall accrue at the stipulated interest rate (compounded interest) from the stipulated reckoning point or, in the absence thereof, from extrajudicial or judicial demand until full payment, provided it is not unconscionable. In the absence of a stipulated compounded interest rate or if this rate is

unconscionable, legal interest at the rate of 6% shall apply from the time of judicial demand until full payment.

b. For unliquidated claims:
Compensatory interest on the amount of damages awarded may be imposed in the discretion of the court at the rate of 6% per annum. No compensatory interest, however, shall be adjudged on unliquidated claims or damages until the demand can be established with reasonable certainty. Thus, when such certainty cannot be so reasonably established at the time the demand is made, the interest shall begin to run only from the date of the judgment of the trial court (at which time the quantification of damages may be deemed to have been reasonably ascertained) until full payment. The actual base for the computation of the interest shall, in any case, be on the principal amount finally adjudged.

In applying *Lara's Gift*, there's a **two-level analysis** involved:
1. Did the parties stipulate a compensatory interest?
2. Did the parties stipulate a conventional interest?

Any other contravention of the tenor of the obligation

Cathay Pacific Airways v. Sps. Vazquez, G.R. 150843, March 14, 2003

Failure to perform the exact prestation required is a breach of contract, despite the absence of bad faith or fraud.
- Hence, the plaintiffs are entitled only to nominal damages when the airline bumped them to business class, when they were only booked for economy.

Example of another contravention: Insurer erroneously canceled the policy due to nonpayment of premium but reinstated it upon learning of its mistake. Insurer also extended the term of the policy by a period corresponding to the duration of the cancellation.

Q: Is the insurer liable to the insured?
A: Yes. The insurance was interrupted, though no fault of the insurer. There was still a breach, notwithstanding the extension. Insurer failed to provide continuous insurance cover for 1 year.

Fortuitous event

Art. 1174 ⭐

Except in cases expressly specified by law, or when it is otherwise declared by stipulation, or when the nature of the obligation requires the assumption of risk, no person shall be responsible for those events which could not be foreseen, or which, though foreseen, were inevitable.

Fortuitous event ♥

Definition: An event that cannot be foreseen, or although foreseen, cannot be avoided by the obligor, and thus, exempts the obligor from any liability for the nonperformance caused by said event.

Requisites of a fortuitous event (FE)
1. Independent of the will of the debtor
   a. FE must be the sole and proximate cause of the nonperformance of the obligation
   b. The debtor must not cause nonfulfillment
2. Unforeseeable and unavoidable
   a. Impossible to foresee the event which constitutes the *caso fortuito*.
   b. The debtor should be in no position to anticipate or avoid the event.
3. Event renders it impossible for the debtor to perform
4. Debtor did not aggravate to the injury (no concurring fault or negligence)

Q: Does a fortuitous event exempt from paying a monetary obligation?
A: No. Money is a generic thing, therefore it is not excused by fortuitous loss of any specific property of the debtor.

Requisites of a fortuitous event

Sulpicio Lines v. Sesante, G.R. 172682, July 27, 2016 ♥

Requisites to be considered a fortuitous event:
1. The cause of the unforeseen and unexpected occurrence, or failure of the debtor to comply with his obligation must be independent of the human will.
2. It must be impossible to foresee the event, or impossible to avoid.
3. The occurrence must be such as to render it impossible for the debtor to fulfill his obligation in any manner.
4. The obligor must be free from any participation in the aggravation of the injury resulting to the creditor.

Not a fortuitous event

Awayan v. Sulu Resources, G.R. 200474, November 9, 2020

When the event is found to be partly the result of a party's participation–whether by active intervention, neglect, or failure to act–the incident is humanized and removed from the ambit of force majeure. Hence, there must be no human intervention that caused or aggravated the event, or at the very least, it must be beyond the obligor's will.

Does a fortuitous event suspend an obligation? If yes, does it automatically extend a contract between parties?

Ace-agro Development Corp. v. CA, G.R. 119729, January 21, 1997

Force majeure only relieves the parties from the fulfillment of their respective obligations during that time. However, it did not stop the running of the period of their contract.

Nielson v. Lepanto, G.R. L-21601, December 28, 1968

The operation of the contract is suspended for as long as the adverse effects of the fortuitous event are present.

The contract between the parties may be extended if it was the intent of the parties that the suspension of the contract meant also an extension of the same period after the resolutory period.

When may a debtor not claim the benefits of a fortuitous event?

1. In cases expressly specified by law
2. When the parties so stipulate
3. When the nature of the obligation requires the assumption of risk

Usury

Art. 1175

Usurious transactions shall be governed by special laws.

Advocates for Truth in Lending Inc. v. BSP, G.R. 192986, January 15, 2013

CB Circular 905 did not repeal nor in any way amend the Usury Law but simply suspended the latter's effectivity. By virtue of the circular, the Usury Law has been rendered ineffective, and usury has been legally nonexistent in our jurisdiction. **Interest can now be charged as the lender and borrower may agree upon.**

When will conventional or monetary interest be due an obligation?

- When the parties agreed to it in writing (Art. 1956).

May the contracting parties agree on any interest rate?

- Yes, but it may be reduced by the court in a proper case should it find it unconscionable.

When is an interest rate deemed reasonable?

- The maximum interest rate that will not cross the line of unconscionability is not more than twice the prevailing legal rate of interest.

If the rate exceeds double the legal rate, is it automatically unconscionable?

- No. The creditor has the burden of proving the reasonableness of the rate under current market conditions and that the parties were on an equal footing when they stipulated the interest rate.

Presumptions

Art. 1176

The receipt of the principal by the creditor, without reservation with respect to the interest, shall give rise to the presumption that said interest has been paid.

The receipt of a later installment of a debt without reservation as to prior installments, shall likewise raise the presumption that such installments have been paid.

Presumption – The inference of the existence or nonexistence of a fact not actually known arising from its usual connection with another fact or group of facts which is known or otherwise established.

- **Conclusive presumption** – One which cannot be contradicted or overturned by evidence
- **Disputable presumption** – One which is satisfactory if uncontradicted, but may be rebutted or overcome by presenting proof to the contrary.

What are the presumptions?

1. Payment of interest is presumed if the creditor receives payment of the principal without any reservation as to interest
2. Payment of an earlier installment of a debt is presumed if the creditor receives payment of a later installment without any reservation as to the prior installment

Cf. Art. 1253.

- Art. 1176 is general, while Art. 1253 is specifically pertinent on questions involving application of payments and extinguishment of obligations.
  - In Art. 1176, the creditor "receives."
  - In Art. 1253, the creditor "accepts" an incomplete payment fully aware of the incompleteness thereof.
    - In this case, the creditor is deemed to have waived the incomplete or irregular performance.

⚠️ *Correlate this with the requisites of a valid payment in Arts. 1232, et. seq.*

Art. 1176 vis-a-vis Art. 1253

Marquez v. Elisan Credit Corporation, G.R. 194642, April 6, 2015

The presumption under Art. 1176 does not resolve the question of whether the amount received by the creditor is a payment for the principal or interest. Under this article the amount received by the creditor is the payment for the principal, but a doubt arises on whether or not the interest is waived because the creditor accepts the payment for the principal without reservation with respect to the interest. Art. 1176 resolves this doubt by presuming that the creditor waives the payment of interest because he accepts payment for the principal without any reservation.

Acción subrogatoria;
Acción pauliana

Art. 1177

The creditors, after having pursued the property in possession of the debtor to satisfy their claims, may exercise all the rights and bring all the actions of the latter for the same purpose [1], save those which are inherent in his person; they may also impugn the acts which the debtor may have done to defraud them [2].

[1] Accion subrogatoria
[2] Accion pauliana

Remedies available to creditors for the satisfaction of their claims:

1. Specific performance (with a right to damages)
2. Pursue the leviable property of the debtor
3. Acción subrogatoria (Art. 1177)
4. Acción pauliana – To ask the court to rescind or impugn acts or contracts which the debtor may have done to defraud him when he cannot in any other manner recover his claim (Arts. 1380-1389, NCC)

Acción subrogatoria ♥

- "The debtor of my debtor is my debtor"
- The creditor may exercise the rights or bring actions for and on behalf of the debtor for the purpose of obtaining payment
  - These "rights" are assets or receivables by the debtor
  - However, the creditor cannot exercise rights and actions that are personal to the debtor (*e.g.,* an action for support)

Acción pauliana ♥

- The law protects the creditor against acts of the debtor to defraud the creditor and entitles the creditor to file the appropriate action to assail the debtor's fraudulent acts and seek redress
- The legal remedy of the creditor to impugn fraudulent acts of the debtor is called acción pauliana
  - Example: Rescission of a conveyance of a property by the debtor in fraud of the creditor.
- *Requirements:*
  1. Plaintiff asking for rescission has credit prior to the alienation although demandable later
  2. The debtor has made a subsequent contract conveying a patrimonial benefit to a 3rd person
  3. The creditor has no other legal remedy to satisfy his claim, but would benefit by rescission of the conveyance to the third person (you cannot go directly to rescission)
  4. The act being impugned is fraudulent
  5. The 3rd person should be an accomplice in the fraud (an innocent purchaser will be protected)
- *Prescriptive period:* Four years from the accrual of the right of action (*e.g.,* exhaustion of all the primary remedies)

Transmissibility

Art. 1178

Subject to the laws, all rights acquired in virtue of an obligation are transmissible, if there has been no stipulation to the contrary.

General rule: Creditor may transmit or transfer her rights acquired by virtue of an obligation

Exceptions:
1. The law provides otherwise
2. Agreement of the parties provide otherwise
3. Nature of the rights provide otherwise (*e.g.*, strictly personal rights)

Chapter 2
Different Kinds of Obligations

Pure obligations

Art. 1179

Every obligation whose performance does not depend upon a future or uncertain event, or upon a past event unknown to the parties, is demandable at once.

Every obligation which contains a resolutory condition shall also be demandable, without prejudice to the effects of the happening of the event.

Pure obligations – An obligation whose performance the creditor may immediately demand from the debtor
- Not subject to a suspensive condition or a suspensive term

Condition – A future and uncertain event upon which an obligation depends.
- **Suspensive** – The obligation arises and the creditor acquires the corresponding right upon the fulfillment of the suspensive condition (condition precedent)
- **Resolutory** – The debtor's obligation and the creditor's right are extinguished upon the fulfillment of the resolutory condition (condition subsequent)

Term or period – A term is a future event that is certain to happen (a day certain)
- Suspensive – The debtor has an obligation and the creditor has a corresponding right but the creditor may demand fulfillment of the obligation only upon arrival of the term
- Resolutory – The debtor's obligation and the creditor's right are extinguished upon arrival of the term.

An obligation subject to a resolutory condition/term is immediately demandable by the creditor upon the happening of the condition or arrival of the term.
- The obligation will be extinguished upon fulfillment of the resolutory condition.

Conditional obligations
- A contingency that determines the existence or extinction of an obligation.
- It's either suspensive/condition precedent (existence), or a resolutory condition/condition subsequent (extinction)

Kinds of conditions based on who determines their fulfillment

1. **Potestative** – Depends on the sole will of the debtor *or* the creditor.
   a. Dependent on the *debtor's will* – As a suspensive condition for the effectivity of an employment contract between a shipping company and a seaman, the issuance by the shipping company's agent of a boarding confirmation to the seaman is a potestative condition dependent on the will of the shipping company as employer
   b. Dependent on the *creditor's will* – In an obligation payable by the debtor upon demand by the creditor, the demand is a potestative condition dependent on the will of the creditor
2. **Casual** – Depends exclusively upon chance *or other factors* not depending upon the will of the parties to an obligation.
   a. In a contract of insurance of a building vs. an earthquake. The loss or damage caused by an earthquake is a casual condition that neither the insured nor the insurer controls.
3. **Mixed** – Depends on the will of a party and *other circumstances* or factors, including the will of a *third person*.
   a. As a suspensive condition of the buyer's obligation to pay the balance of the purchase price of the land sold by a seller, (i) if the seller removes the squatters, and the (ii) buyer acquires a road ROW. These conditions are mixed.

Suspensive vs. resolutory conditions in a sale

	Contract to sell	**Contract of sale**	**Contract of conditional sale (CCS)**
Who has ownership?	Seller	Buyer, *upon delivery*	If there was prior delivery, title to the property passes to the buyer upon fulfillment of the

			suspensive condition. Seller consented to the sale but subject to the suspensive condition.
Payment or nonpayment of the price as a condition	Full payment is a suspensive condition of the seller's obligation to convey ownership Nonpayment: Art. 1184	Nonpayment is a negative resolutory condition, the happening of which will extinguish the obligation or the sale Nonpayment: basic remedies	If the suspensive condition is not fulfilled, the perfection of the contract of sale is completely abated Nonpayment: Art. 1184

Donation subject to a condition

Clemente v. Republic, G.R. 220008, February 20, 2019

Upon nonfulfillment of the condition, a donation may be revoked and all the rights already acquired by the donee shall be deemed lost and extinguished.

This is a resolutory condition because it is demandable at once by the donee, but the nonfulfillment of the condition gives the donor the right to revoke it.

- Because the deed of donation is a resolutory condition, until the donation is revoked, the donation is valid.
- However, for it to remain valid, the donee must comply with the condition.
- The failure to comply gives the donor the right to revoke, per Art. 764, NCC.

Pay once means permit to do so → with a period

Art. 1180

When the debtor binds himself to pay when his means permit him to do so, the obligation shall be deemed to be one with a period, subject to the provisions of Article 1197.

Example: A promissory note with a clause "when I have earned or otherwise raised the necessary funds therefor"

Q: Is the obligation to pay conditional?
A: No. It's an obligation to a period dependent on her sole will (Art. 1180). The debtor or creditor may file an action to ask the court to fix the period for her to pay (Art. 1197).

Art. 1181

In conditional obligations, the acquisition of rights, as well as extinguishment or loss of those already acquired, shall depend upon the happening of the event which constitutes the condition.

Estipona v. Estate of Aquino, G.R. 207407, September 29, 2021

Art. 1181 classifies conditions into suspensive and resolutory conditions.

- **Suspensive** – The happening thereof gives rise to the obligation; and the obligation is not demandable until the happening of the event which constitutes the obligation.
- **Resolutory** – Conditions subsequent; conditions on which depend the extinction of the obligation.

CTS vs. COS

- Contract of sale (COS) – The title to the property passes to the vendee upon delivery of the thing sold.
- Conditional sale/Contract to sell (CTS) – Ownership remains with the vendor and does not pass to the vendee until full payment of the purchase price.
    - The full payment of the purchase price is the positive suspensive condition, the failure of which is not a breach of contract, but simply an event that prevented the obligation of the vendor to convey title from acquiring binding force.

Heirs of Gonzales v. Basas, G.R. 206847, June 15, 2022

In a COS, the nonpayment of the price is a negative resolutory condition because it can extinguish the seller's obligation to deliver the thing sold.

- If the buyer fails to pay, the seller has the right to rescind (resolve) the contract.
- The nonpayment triggers the seller's right to undo the contract and recover the item.

Potestative conditions

Art. 1182 ⭐

When the fulfillment of the condition depends upon the sole will of the debtor, the conditional obligation shall be void. If it depends upon chance or upon the will of a third person, the obligation shall take effect in conformity with the provisions of this Code.

Yupangco v. OJ Development and Trading Corp., G.R. 242074, November 10, 2021 ♥

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Potestative condition – A condition the fulfillment of which depends exclusively upon the will of the debtor, in which case, the conditional obligation is void.

Two kinds of potestative condition:

1. Potestative condition **imposed on the birth of the obligation**
    a. Here, the entire obligation is void.
    b. This is a purely potestative suspensive condition dependent on the will of the debtor (PPSC-D).
        i. **JSP:** In case of a contract, the proper justification of the nullification only of the condition is the principle of mutuality of contracts, *i.e.*, the contract's validity or compliance cannot be left to the will of one of them. (Art. 1308)
2. Potestative condition **imposed on the obligation's fulfillment**
    - Here, only the condition is void, leaving unaffected the obligation itself.

In this case, the "best efforts" clause is a purely potestative condition, dependent on the sole will or discretion of OJDTC and Oscar.

- As the condition is imposed on the performance or fulfillment of the obligation to reimburse/pay petitioners, only the condition is treated as void.

JSP: It's a mixed condition, because the best efforts to pay may also depend on OJDT's creditors, lenders, etc.

Catungal v. Rodriguez, G.R. 146839, March 23, 2011

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Mixed condition – A condition dependent not on the will of the vendor alone, but also of third persons.

- It is not a purely potestative condition, hence it is valid.

PPSC-D vs. PPSC-C

While a PPSC-D destroys the juridical tie, a purely potestative suspensive condition dependent on the sole will of the creditor does not affect the validity of the conditional obligation.

- In this case, the obligation is immediately effective and the lender controls only when the borrower shall pay, i.e., upon demand.

A PPSC-D, however, will not nullify the obligation if the debtor's decision will be externalized through certain acts and trigger the obligation.

- Example: *Right of first refusal*. This time, you have an objective measure. The decision of the lessor is manifested by accepting the offer or making an offer. In which case, the lessor is obliged to make the offer first to the lessee.
    - This time around, the relevant parties can determine if an action has been made by the lessor.

Impossible condition

Art. 1183

Impossible conditions, those contrary to good customs or public policy and those prohibited by law shall annul the obligation which depends upon them. If the obligation is divisible, that part thereof which is not affected by the impossible or unlawful condition shall be valid.

The condition not to do an impossible thing shall be considered as not having been agreed upon.

What will be the consequence of an obligation subject to an impossible condition?

1. In a positive obligation (to give, to do) – The obligation depending on it shall be void.
    a. Both the condition and the obligation shall be void
    b. Exception: This rule does not apply to donations and wills.
2. In a negative obligation (not to do) – The obligation is valid.
    a. The condition is deemed not imposed or agreed upon by the parties.

⚠️ *If the obligation is divisible, the rule on severability shall apply.*

Fulfillment of conditions

Art. 1184

The condition that some event happen at a determinate time shall extinguish the obligation as soon as the time expires or if it has become indubitable that the event will not take place.

Art. 1185

The condition that some event will not happen at a determinate time shall render the obligation effective from the moment the time indicated has elapsed, or if it has become evident that the event cannot occur.

If no time has been fixed, the condition shall be deemed fulfilled at such time as may have probably been contemplated, bearing in mind the condition of the obligation.

Art. 1184 and CTS

Ayala Land v. Burton, G.R. 163075, January 23, 2006 ♥

The non-fulfillment by the buyer of his obligation to pay, which is a suspensive condition to the obligation of the seller to sell and deliver the title to the property, rendered the **contract to sell** ineffective and without force and effect.

- The parties stand as if the conditional obligation had never existed. Article 1191 of the New Civil Code will not apply because it presupposes an obligation already extant
- There can be no rescission of an obligation that is still non-existing, the suspensive condition not having happened.

When is an obligation subject to a **positive suspensive condition** that should occur within a fixed period extinguished?

1. The period expires without the event taking place
2. The event indubitably will not happen (Art. 1184)

Illustrative example: In a noncompete clause, the ex-worker's obligation not to work in a competitor company expires after:
1. The period stipulated (*e.g.*, five years after resignation), or
2. The competitor company closes down (it becomes impossible to be hired in the competitor)

When is an obligation subject to a negative suspensive condition that should occur within a fixed period extinguished?

1. The period expires without the occurrence
2. Even before the expiration the condition indubitably cannot occur

(Art. 1185)

Illustrative example: The ex-worker will be paid a certain sum if he will not work in a competitor company within two years from termination. The obligation not to work expires:
1. After two years (period expires), or
2. The competitor closes down.

In either case, the ex-worker can collect the sum immediately thereafter.

Art. 1184 is the **remedy** for an unpaid seller in a **contract to sell**. The payment of the full price is the suspensive condition, which gives rise to the seller's obligation to convey ownership of the property to the buyer.

- Nonpayment, therefore, is the negative resolutory condition that extinguishes the obligation (Art. 1185).

Constructive fulfillment

Art. 1186 ⭐

The condition shall be deemed fulfilled when the obligor voluntarily prevents its fulfillment.

Constructive fulfillment – A suspensive condition of an obligation is constructively fulfilled if the debtor intended to preclude and actually precluded the fulfillment of the condition.

Art. 1186 applies when:
1. There is an intent of the obligor to prevent, and
2. There is actual prevention.

Q: Is malice required?
A: No. Art. 1186 requires only that the act be voluntary and thus constructive fulfillment may arise from the debtor's negligence.

DBP v. Sta Ines, G.R. 196068, February 1, 2017

A condition shall be deemed fulfilled when the obligor voluntarily prevents its fulfillment and a debtor loses the right to make use of the period when a condition is violated, making the obligation immediately demandable.

Retroactivity of condition

Art. 1187

The effects of a conditional obligation to give, once the condition has been fulfilled, shall retroact to the day of the constitution of the obligation. Nevertheless, when the obligation imposes reciprocal prestations upon the parties, the fruits and interests during the pendency of the condition shall be deemed to have been mutually compensated. If the obligation is unilateral, the debtor shall appropriate the fruits and interests received, unless from the nature and circumstances of the obligation it should be inferred that the intention of the person constituting the same was different.

In obligations to do and not to do, the courts shall determine, in each case, the retroactive effect of the condition that has been complied with.

Illustrative example: Here is a contract of conditional sale for an unregistered parcel of land. Upon signing, the seller transferred possession of the land to the buyer and the buyer paid P1M to the seller. Buyer shall acquire ownership of the land only upon full payment of the price. Buyer fully paid the price on Day 5. When did the buyer own the land?

Buyer owns the land as of Day 1, because the fulfillment of the suspensive condition retroacts on the constitution of the obligation (D1). This is by fiction of law.

- The effects of the obligation to give subject to a suspensive condition retroact to the time of its constitution or creation (Art. 1187).

The retroactive effect does not apply to the fruits and interests accruing during the pendency of the condition.

1. In reciprocal obligations, the fruits and interests accruing are mutually compensated
2. In a unilateral obligation, the debtor appropriates the fruits and interests
3. In obligations to do and not to do the courts determine the retroactive effect of the fulfillment of the condition

Art. 1188

The creditor may, before the fulfillment of the condition, bring the appropriate actions for the preservation of his right.

The debtor may recover what during the same time he has paid by mistake in case of a suspensive condition.

- Before the fulfillment of the suspensive/resolutory condition of an obligation, the creditor has a mere expectancy or inchoate rights but may take judicial or extrajudicial actions to preserve/protect his rights.
- If the obligation is subject to a suspensive condition and the debtor pays by mistake before the fulfillment thereof, the debtor may recover the payment before such fulfillment
    - The debtor should pay by mistake if she pays fully aware that the condition has yet to happen, she implicitly waives the condition.
    - If the debtor does not pay by mistake but the condition later is not fulfilled, she may recover the payment if it was made on the expectancy that the condition will be fulfilled.

Suspensive condition;
Rules during pendency

Art. 1189

When the conditions have been imposed with the intention of suspending the efficacy of an obligation to give, the following rules shall be observed in case of the improvement, loss or deterioration of the thing during the pendency of the condition.

(1) If the thing is lost without the fault of the debtor, the obligation shall be extinguished;
(2) If the thing is lost through the fault of the debtor, he shall be obliged to pay damages; it is understood that the thing is lost when it perishes, or goes out of commerce, or disappears in such a way that its existence is unknown or it cannot be recovered;
(3) When the thing deteriorates without the fault of the debtor, the impairment is to be borne by the creditor;
(4) If it deteriorates through fault of the debtor, the creditor may choose between the rescission of the obligation and its fulfillment, with indemnity for damages in either case.
(5) If the thing is improved by its nature, or by time, the improvement shall inure to the benefit of the creditor;
(6) If it is improved at the expense of the debtor, he shall have no other right than that granted to the usufructuary.

Rules for the application of Art. 1189

1. Obligation is to give a determinate thing
2. Obligation is subject to a suspensive condition which is fulfilled
3. There is a loss, deterioration, or improvement of the thing prior to the fulfillment of the condition.

Situation	Effect on obligation	Rights and obligations
Lost + debtor's fault	Remains	Debtor must pay damages
Lost + no fault	Extinguished	-
Deterioration + debtor's fault fault	Remains	Creditor may choose: 1. Rescission + damages 2. Fulfillment + damages
Deterioration + no fault	Remains	Creditor bears the impairment
Improved by nature or time	Remains	Improvement benefits the creditor
Improved by debtor	Remains	Debtor has only usufructuary rights

Resolutory condition;
Rules during pendency

Art. 1190

When the conditions have for their purpose the extinguishment of an obligation to give, the parties, upon the fulfillment of said conditions, shall return to each other what they have received.

In case of the loss, deterioration or improvement of the thing, the provisions which, with respect to the debtor, are laid down in the preceding article shall be applied to the party who is bound to return.

As for the obligations to do and not to do, the provisions of the second paragraph of article 1187 shall be observed as regards the effect of the extinguishment of the obligation.

Resolutory condition of an obligation to give:

1. When the condition extinguishes an obligation to give, both parties must return what they have received upon fulfillment of the condition.
    a. *See Sps. Macasaet v. Sps. Macaset.*
2. The party bound to return the thing is subject to the same rules as the debtor in the preceding article (Art. 1189)
3. For obligations to do or not to do, the effects of the extinguishment of the obligation shall follow the rules stated in Article 1187, second paragraph (court's determination).

Resolution

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 [1] 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 court shall decree the rescission claimed [2], unless there be just cause authorizing the fixing of a period [3].

This is understood to be without prejudice to the rights of third persons who have acquired the thing, in accordance with articles 1385 and 1388 and the Mortgage Law.

[1] Specific performance.
[2] Implies the availability of both judicial and extrajudicial resolution
[3] *See* Art. 1197.

Preliminarily, Art. 1191 gives the injured party two options:
1. Fulfillment (specific performance) or
2. Resolution

And resolution may also be opted, if SP is impossible.

Rescission only for substantial;
Fundamental breach

CASTEA v. Province of Camarines Sur, G.R. 199666, October 7, 2019

Rescission will not be permitted for a slight or casual breach of the contract, but only for such breaches as are so substantial and fundamental as to defeat the object of the parties in making the agreement.

Substantial breach – A substantial and fundamental violation that defeats the very object of the parties in making or entering into the agreement.

- It does not solely depend on the percentage of the amount not paid.

Other examples of substantial breach:

1. The lessee failed to insure the leased premises with the lessor as the beneficiary as mandated by the lease contract
2. A party to a JV contract unilaterally reduced his committed cash contribution from P32.5M to P5M.
3. Buyer sold the property contrary to the provision in the DOS prohibiting the alienation/encumbrance of the property within a certain period without the prior written consent of the seller
4. Corporation did not issue and deliver to the stockholder the stock certificate covering the common share subscribed and fully paid by the stockholder

Substantial breach need not refer to a monetary obligation of the debtor.

General rule: Resolution is not allowed on mere casual/slight breach.
Exceptions:

1. The parties stipulated it (any violation shall be a material breach of the contract, which shall warrant resolution)
2. Time is the essence of the agreement

What should the court do if it finds only a **casual or slight breach** by the debtor?

1. Fix a period for the debtor to rectify the breach and fulfill the obligation
2. Award damages to the creditor based on said breach

Who may resolve?

- Only the injured party who:
  - Fulfilled his prestation (if simultaneous), or
  - Ready, willing and able to fulfill (if successive).

Q: Is fraud a requirement of resolution under Art. 1191?
A: No. It's predicated on substantial breach.

Grounds for rescission;
Breach of faith

De Luna v. Swire Realty, G.R. 226912, November 24, 2021

The right of rescission of a party to an obligation under Art. 1191 is predicated on a breach of faith by the other party who violates the reciprocity between them.

- The breach contemplated in the said provision is the obligor's failure to comply with an existing obligation.

Rescission vs. specific performance

Chanelay Development Corp. v. GSIS, G.R. 210423, July 5, 2021

Rescission and specific performance (SP) are alternative remedies.

While persons prejudiced may choose either SP and resolution, they are not entitled to pursue both.

Art. 1191 vis-a-vis Art. 1197 (fixing a period)

Camp John Hay v. Charter Chemical, G.R. 198849, August 7, 2019

Rescission under Art. 1191 is the proper remedy when a party breaches a reciprocal obligation. The court's power to fix a period of an obligation under Art. 1197 is discretionary and should be exercised only if there is just cause.

Rescission vs. foreclosure

Suria v. IAC, G.R. 73893, June 30, 1987 ♥

The remedy of rescission is not a principal action retaliatory in character but becomes a subsidiary one which by law is available only in the absence of any other legal remedy. Foreclosure is not a remedy accorded by law, but a specific provision found in the contract between the parties.

Hence, the debtor could have foreclosed the mortgage immediately when it fell due instead of waiting for all these years while trying to enforce the wrong remedy (rescission).

Extrajudicial rescission;
Duty of courts

Nissan v. Lica Management Inc., G.R. 176986, January 13, 2016

An aggrieved party is not prevented from extrajudicially rescinding a contract to protect its interests, even in the absence of any provision expressly providing for such right.

The only practical effect of a contractual stipulation allowing extrajudicial rescission is to merely transfer to the defaulter the initiative of instituting suit, instead of the rescinder.

Sps. Co v. CA, G.R. 112330, August 17, 1999 ♥

In the absence of an express stipulation authorizing the sellers to extrajudicially rescind the contract of sale, Sps. Co–who is the injured party–cannot unilaterally and extrajudicially rescind the contract of sale.

Extrajudicial resolution

General rule: The power to rescind must be invoked judicially and cannot be exercised solely on a party's own judgment that the other has committed a breach of obligation.
Exceptions:
1. Expressly stipulated by the party
2. Authorized by law

Q: If the parties agree on extrajudicial resolution, what should the injured party do?
A: The injured party must invoke the remedy and notify the other party of the intended resolution. The notice is meant to give the party in breach an opportunity to decide whether to accept or reject the resolution.

There is an attempt in recent jurisprudence to adopt extrajudicial resolution as the default rule *(see* UP v. De Los Angeles below*)*.

Q: What step should a party take to protect herself from the vagary of SC decisions?
A: Require the stipulation of extrajudicial resolution or better yet extrajudicial termination or cancelation in case of breach by the debtor of the reciprocal obligation.

Q: Regardless of the default rule on how to resolve a reciprocal obligation, when is the injured party required to file an action to resolve a reciprocal obligation?
A: Judicial resolution will be essential if the party resolving the reciprocal obligation seeks to recover property from the other party who rejects the resolution.

The weight of jurisprudence suggests that extrajudicial resolution is only available upon the parties' stipulation, However, the cases of *UP* and *Nissan* provide otherwise.
- A party who resolves without judicial action may act accordingly (as if resolved), but proceeds at its own risk.

Extrajudicial resolution; Origin story

UP v. De Los Angeles, G.R. L-28602, September 29, 1970 ♥

Effects of extrajudicial resolution
1. Takes effect upon notice of the resolution served by the aggrieved party on the offending party.
2. Offending party can challenge the resolution by filing an appropriate court action
    a. Hence, the extrajudicial resolution is "provisional"
3. If the court finds the resolution proper, the obligation shall be considered resolved at the time of service (see no. 1)
4. If the court finds the resolution improper, the obligation subsists.

No automatic rescission

Chua v. Victorio, G.R. 157568, May 18, 2004

The mere failure by the obligee to comply with an obligation did not *ipso jure* produce the rescission of the contract of lease.

The right of rescission is statutorily recognized in reciprocal obligations, such as a contract of lease.

'Cause' of resolution

Uy v. CA, G.R. 120465, September 9, 1999 ♥

Ordinarily, a party's motives for entering into the contract do not affect the contract. However, when the motive predetermines the cause, the motive may be regarded as the cause.
- **Cause** – Essential reason which moves the contracting parties to enter into it.
    - It is the immediate, direct and proximate reason which justifies the creation of an obligation through the will of the contracting parties.
- **Motive** – The particular reason of a contracting party which does not affect the other party.

This is because *cause* is an essential requisite (the others are consent and object) of a contract. The absence of which voids the obligation.

Termination vs. rescission

Pryce Corp. v. PAGCOR, G.R. 157480, May 6, 2005 ♥

In termination, the parties are not restored to their original situation; neither

is the contract treated as if it never existed.
- Only after the contract has been canceled will the parties be released from their obligations.

Termination	Resolution
Ends the contract but acknowledges its existence and effects up to the termination	Declares the contract void from its inception, as if it never existed
Does not require restoration; obligations performed before termination remain valid	Requires mutual restitution, restoring parties to their original situation

Effects of rescission

Heirs of Kim v. Quicho, G.R. 249247, March 15, 2021

Although rescission repeals the contract from its inception, it does not disregard all the consequences that the contract has created, such as the validity of the forfeiture/penalty clauses.
- Hence, forfeiture and penalty clauses subsist despite a resolution.

Nuñez-Palma (*supra* art. 1168)

When resolution is sought, the obligation to return the things which were the object of the contract, together with their fruits, and the price with interests is created per Art. 1385, NCC.

No mutual restitution in:
1. When there is an express stipulation to the contrary by way of a forfeiture or penalty clause in recognition of the parties' autonomy to contract
2. The buyer was given possession or was able to use the property prior to transfer of title, where in such case, partial payments may be retained and considered as rentals by the seller to avoid unjust enrichment (*Heirs of Kim v. Quicho*)

Interests and market value;
Return of the things

Solid Homes Inc. v. Tan, G.R. 145156, July 29, 2005

In an obligation to give, the current market value–not the purchase price–of the property must be paid in case of rescission under Art. 1385 due to breach of obligation under Art. 1191.
- To hold otherwise will allow unjust enrichment on the part of the debtor.

JSP: The basis here of the court in awarding the FMV is its equity jurisdiction. An alternative that is more consistent with the mutual restitution rule is to award the purchase price, plus the appreciation value of the land as damages because there was bad faith on the part of the developer.

Other remedies apart from resolution

In lieu of the default remedy of resolution, the parties may stipulate or the law may provide a different remedy or course of action of a party should the other party commit a breach of an obligation.

1. The parties may grant the injured or aggrieved party the right to cancel or terminate the contract upon breach thereof by the other party (*Pryce v. PACGOR*).
2. The parties can stipulate an arbitration clause as a mode of settling their contractual dispute and thus preempt a party's exercise of the remedy of resolution in case of contractual breach by the other party (*CJH v. Charter Chemical*).
3. Foreclosure, like in case of a sale of a parcel of land on installments with the payment of the price secured by a REM on the same land (*Suria v. IAC*).
    a. Here, resolution is not available because SP and foreclosure are available.
    b. The COS was consummated as the installment payments secured by the REM took the place of cash payment.
4. Instead of resolution, the injured party can cancel the contract in case of the negation of its cause.
    a. A motive will be deemed to have predetermined the cause and will be considered the cause of the contract only if a party makes known her motive in entering into a contract to the other party, who recognizes it as an essential consideration of the former (like "time is of the essence").
    b. Both parties should know and agree that the motive is an essential consideration of one or both of them for the motive to predetermine the cause and be deemed the cause of the contract.
        i. This may be gleaned from the "whereas" clauses of the contract.

When Art. 1191 is not applicable

1. Sales of residential real property on installment since they are governed by RA 6552 or Maceda Law
2. A party's violation of a compromise agreement approved as the judgment in a case
    a. Remedy is found in the Rules of Court (i.e., contempt)
3. When a third party will be prejudiced (par. 4, Art. 1191).

Compensatio morae

Art. 1192

In case both parties have committed a breach of the obligation, the liability of the first infractor shall be equitably tempered by the courts. If it cannot be determined which of the parties first violated the contract, the same shall be deemed extinguished, and each shall bear his own damages.

Illustrative example: VEDC and Cortes signed a COS whereby Cortes would sell three lots to VEDC for P3.7M. Upon payment of downpayment, Cortes must deliver the property. However, VEDC only paid partial of the P2.2-M downpayment, and Cortes did not deliver the lots. VEDC sued Cortes for specific performance and damages. It wanted Cortes to deliver the TCTs covering the three lots and notarized DOAS (*Cortes v. CA, G.R 126083, July 12, 2006*).

Who was in default?

- Both parties were in default in the performance of the reciprocal obligation (*compensatio morae*). Cortes did not transfer ownership of the lots, while VEDC did not fully pay the P2.2M.

What is the consequence?

- The mutual delay canceled out the effects as if no one was in default.

Application of Art. 1192 ♥

General rule: The court shall equitably offset their individual liabilities, provided that the court can establish the first infractor.

- The sequence of the default must be presented/shown and proven.
- Whoever claims an offsetting has the burden of proving that the other party also committed a violation of the obligation.
- Art. 1192, cl. 1 is premised on successive performance of prestations and corresponding default.

⚠️ *In all cases where an offsetting will be decreed, any obligation to pay whatever is not affected. Only the damages will be offset.*

In applying Art. 1192, the court may do two things:

1. Equitably temper the liability of the first infractor, or
    a. Hence, if the court cannot identify the first infractor, this will not apply.
2. Totally offset the damages.
    a. This will apply if the court cannot distinguish the first infractor. Hence, the contract shall be deemed extinguished and each shall bear his own damage.
        i. In this case, resolution will not be proper because the obligation has been extinguished *ipso facto* by the mere fact of the mutual breach.

Obligations with a period

Art. 1193 ⭐

Obligations for whose fulfillment a day certain has been fixed, shall be demandable only when that day comes.

Obligations with a resolutory period take effect at once, but terminate upon arrival of the day certain.

A day certain is understood to be that which must necessarily come, although it may not be known when.

If the uncertainty consists in whether the day will come or not, the obligation is conditional, and it shall be regulated by the rules of the preceding Section (Arts. 1179-1192).

Outline of the codal:

Par. 1 – Suspensive period
Par. 2 – Resolutory period
Par. 3 – Definition of a period
Par. 4 – Condition vs. period

Period or term – A future and *certain* event that either suspends the demandability or extinguishes an obligation.

- *Cf.* condition: It is a future and *uncertain* event, or a past event that is unknown to the parties.

Two kinds of periods:

1. Suspensive

   a. A loan payable on a certain *due date*
   b. A price payable by a buyer to a seller *within 30 days* from signing of the COS
   c. A survivorship agreement relating to a bank account
2. Resolutory
   a. A lease or option expiring *after one year* from the commencement date
   b. A usufruct expiring *upon the death* of the usufructuary (to one given the right to enjoy the property)

	Term	Condition
Certainty	A term is certain—it will definitely happen	A condition is a contingency—it may or may not happen
Effect on demandability	A suspensive term only suspends the demandability of an already existing obligation	A suspensive condition determine whether the obligation will exist
When purely potestative (i.e., dependent on the sole will of the debtor)	A suspensive term dependent on the debtor's will does not nullify the obligation. Instead, the creditor may ask the court to fix the period for performance (Art. 1197; *see also* Art. 1180)	A suspensive condition dependent on the sole will of the debtor voids the obligation (PPSC-D)

Art. 1194

In case of loss, deterioration or improvement of the thing before the arrival of the day certain, the rules in Article 1189 shall be observed.

Reproducing here the rules for Art. 1189, which also applies to conditions as per Art. 1194.

Rules for the application of Art. 1189

1. Obligation is to give a determinate thing
2. Obligation is subject to a suspensive [term] which is fulfilled
3. There is a loss, deterioration, or improvement of the thing prior to the fulfillment of the condition.

Situation	Effect on obligation	Rights and obligations
Lost + debtor's fault	Remains	Debtor must pay damages
Lost + no fault	Extinguished	-
Deterioration + debtor's fault fault	Remains	Creditor may choose: 1. Rescission + damages 2. Fulfillment + damages
Deterioration + no fault	Remains	Creditor bears the impairment
Improved by nature or time	Remains	Improvement benefits the creditor
Improved by debtor	Remains	Debtor has only usufructuary rights

Prepayment

Art. 1195

Anything paid or delivered before the arrival of the period, the obligor being unaware of the period or believing that the obligation has become due and demandable, may be recovered, with the fruits and interests.

Requisites for recovery of payment under Art. 1195:

1. There is an obligation to give subject to a suspensive term
2. The debtor is either unaware of the period or believes the obligation to be due and demandable
3. The debtor pays the obligation prior to the arrival of the period
4. The creditor accepts the payment
5. The debtor asks for recovery with fruits and interests

⚠️ *If the debtor knowingly prepays before the period expires, he forfeits the benefit of said period.*

Benefit of a period

Art. 1196

Whenever in an obligation a period is designated, it is presumed to have been established for the benefit of both the creditor and the debtor, unless from the tenor of the same or other circumstances it should appear that the period has been established in favor of one or of the other.

General rule: The period benefits both the creditor and debtor.
Exception: A period may benefit one party based on:

1. Stipulation
2. Law
3. Nature of obligation

Illustrative examples:

1. A lease contract will expire one year after the turnover of the leased premises by the lessor to the lessee on Mar. 1, 2022. Who has the benefit of the period? *Both*.
2. A PN provides that "the borrower shall pay the lender P10 million plus 6% interest per annum on Aug. 25, 2025." How should the clause be amended to have the term benefit only one party?
    a. Borrower: the borrower shall pay the lender P10 million plus 6% interest per annum *at the borrower's option*, or before Aug. 25, 2025.
        i. Here, the borrower can pay anytime before Aug. 25, 2025.
    b. Lender: the borrower shall pay the lender P10 million plus 6% interest per annum on Aug. 25, 2025, or upon the lender's demand.
        i. Here, the lender can demand payment anytime up until Aug. 25, 2025.

Fixing a period

Art. 1197 ⭐

If the obligation does not fix a period, but from its nature and the circumstances it can be inferred that a period was intended, the courts may fix the duration thereof.

The courts shall also fix the duration of the period when it depends upon the will of the debtor.

In every case, the courts shall determine such period as may under the circumstances have been probably contemplated by the parties. Once fixed by the courts, the period cannot be changed by them.

When will Art. 1197 apply?
When will courts fix the period? [1]

1. The nature and circumstances of the obligation indicate an intention of the parties to fix a period, but the parties omitted it.
2. The period depends on the will of the debtor, including a debtor's undertaking to pay when able or when his means permit him to do so.
    a. A reasonable term will be set.
3. Setting a period cannot be coupled with specific performance.
    a. Except: When SP is dilatory.

By fixing the period, the court will only implement the intent of the parties to allow the creditor to demand the debtor's performance of the obligation.

⚠️ *Be careful in distinguishing pure obligation (not subject to suspensive condition), and an inadvertence of omitting a period.*

- Regardless of the absence of the period, if the obligation is pure, it is demandable immediately, without the need to resort to action to fix the period under Art. 1197.

⚠️ *The application of Art. 1197 implies that there is still an existing obligation. If the obligation has already been extinguished, this finds no application.*

Illustrative example: Upon expiration of the term of their lease contract, the lessor and the lessee were unable to agree on the renewal of the lease, specifically, the monthly rent and the additional term. The lessee sued the lessor and asked the court to fix the term of the rend payable under the contract. May the court grant the reliefs asked by the lessee?

No, the parties do not have an obligation. The previous contract already expired. There is no more period to be fixed.

[1] As a general rule, the court cannot provide a term or condition of an obligation. An exception to this is the reduction of an unconscionable interest—but the court does not nullify the obligation. As an exception to the parties' freedom of contract, the court may fix the term of an obligation.

Omission of date in a contract;
Contemporaneous acts, important in determining intent

Radiowealth v. Sps. Del Rosario, G.R. 138789, July 6, 2000

The act of leaving blank the due date of the first installment did not

necessarily mean that the debtors were allowed to pay as and when they could. If this was the intention of the parties, they should have so indicated in the Promissory Note. However, it did not reflect any such intention.

- The contemporaneous and subsequent acts of the parties manifest their intention and knowledge that the monthly installments would be due and demandable each month.
    - Basically, the court was saying that there was a period, notwithstanding the inadvertent omission of when the first installment's due date, because the debtor paid the installments.

Here, the court did not fix a period.

Q: How can a party make a proper Art. 1197 case?
A: By using the special circumstances of the loan transaction that will show an intent of the parties that it intended a period.

May the court decline to fix the period of an obligation?

Yes. The court has discretion whether to fix the period. The court may refrain from fixing a period if it will be an exercise in futility, for example:

a. when the debtor does not intend to fulfill the obligation or,
b. like in *Camp John Hay* and *Clemente* cases, when the obligation was to be performed within a reasonable period that had already lapsed.

Sps. Macasaet v. Sps. Macasaet, G.R. 154391, September 30, 2004

Art. 1197 allows the courts to fix the duration or the period. It, however, only applies to a situation in which the party intended a period. The parties' mere failure to fix the duration of their agreement does not necessarily justify or authorize the courts to do so.

Camp John Hay (*surpa* art. 1191)

The court's power to fix a period of an obligation under Art. 1197 is discretionary and should be exercised only if there is just cause.

- The discretion to fix an obligation's period is addressed to this court's judgment and is tempered by equitable considerations.

In fixing said period, the court merely ascertains the will of the parties and gives effect thereto.

Hence, lacking any reasonable explanation and just cause for the fixing of the period for the obligee's noncompliance, the rescission of the obligation is justified (Art. 1191 in relation to Art. 1197).

Clemente (*supra* art. 1179)

In the absence of any just cause for the court to determine the period of the compliance, there is no more obstacle for the court to decree the rescission claimed.

- If period is not intended, then, rescission/resolution may be granted.

Loss of the period

Art. 1198

The debtor shall lose every right to make use of the period:

1. When after the obligation has been contracted, he becomes insolvent, unless he gives a guaranty or security for the debt;
2. When he does not furnish to the creditor the guaranties or securities which he has promised;
3. When by his own acts he has impaired said guaranties or securities after their establishment, and when through a fortuitous event they disappear, unless he immediately gives new ones equally satisfactory;
4. When the debtor violates any undertaking, in consideration of which the creditor agreed to the period;
5. When the debtor attempts to abscond.

Art. 1198 is similar to an acceleration clause in a contract.

- If installment, everything will now become due at once because the debtor lost the benefit of the term.

In par. 1, what is contemplated is **practical insolvency**, which means that the debtor's debt is now greater than his assets.

In par. 5, a mere attempt is enough to extinguish the period.

Alternative obligations

Art. 1199

A person alternatively bound by different prestations shall completely perform one of them.

The creditor cannot be compelled to receive part of one and part of the other undertaking.

Art. 1200

The right of choice belongs to the debtor, unless it has been expressly granted to the creditor.

The debtor shall have no right to choose those prestations which are impossible, unlawful or which could not have been the object of the obligation.

Art. 1201

The choice shall produce no effect except from the time it has been communicated.

Art. 1202

The debtor shall lose the right of choice when among the prestations whereby he is alternatively bound, only one is practicable.

Art. 1203

If through the creditor's acts the debtor cannot make a choice according to the terms of the obligation, the latter may rescind the contract with damages.

Kinds of obligations with multiple prestations:

1. **Conjunctive** – The debtor has to perform several prestations
2. **Alternative** – The debtor has to perform only one of several prestations
3. **Facultative** – The debtor has to perform a single principal prestation but may opt for a substitute prestation

General rule: The debtor has the right to choose.
Exception: Parties may stipulate to give the creditor the right to choose (Art. 1200)

Limitations on debtor's right to choose in an alternative obligation

1. The debtor should choose and perform:
    a. A single complete prestation (integrity of payment) (Art. 1199)
    b. A prestation as agreed upon by the parties (identity of payment) (Art. 1201)
    c. A physically and juridically possible prestation (Art. 1183)
2. The debtor loses the right to choose if only one prestation is practicable (Art. 1201)
3. Debtor has to choose a prestation

Arco v. Lim, G.R. 206806, Jun. 25, 2014

The choice of the debtor must also be communicated to the creditor who must receive notice of it since the object of this notice is to give the creditor opportunity to express his consent, or to impugn the election made by the debtor.

- Only after said notice shall the election take legal effect when consented by the creditor, or if impugned by the latter, when declared proper by a competent court.

Loss of some/all prestations

Art. 1204

The creditor shall have a right to indemnity for damages [1] when, through the fault of the debtor, all the things which are alternatively the object of the obligation have been lost, or the compliance of the obligation has become impossible.

The indemnity shall be fixed taking as a basis the value of the last thing which disappeared, or that of the service which last became impossible.

Damages other than the value of the last thing or service may also be awarded.

Art. 1205

When the choice has been expressly given to the creditor, the obligation shall cease to be alternative from the day when the selection has been communicated to the debtor.

Until then the responsibility of the debtor shall be governed by the following rules:

(1) If one of the things is lost through a fortuitous event, he shall perform the obligation by delivering that which the creditor should choose from among the remainder, or that which remains, if only one subsists.
(2) If the lost of one of the things occurs through the fault of the debtor, the creditor may claim any of those subsisting, or the price of that which, through the fault of the former, has disappeared, with a right to damages;
(3) If all the things are lost through the fault of the debtor, the choice by

the creditor shall fall upon the price of any one of them, also with indemnity for damages.

The same rules shall be applied to obligations to do or not to do in case, one some or all of the prestations should become impossible.

[1] Obligation becomes that for damages.

When debtor has the choice:
The nullity of one prestation does not invalidate the obligation.
- The obligation remains valid as long as there is one valid prestation.
- Only the impossibility of all prestations without the fault of the debtor extinguishes the obligation (Art. 1204).
- But if everything is lost → action for damages

When the creditor has the choice (Art. 1205)**:**

Case	Effect
If **one** object is lost due to a **fortuitous event**	Debtor must deliver what remains or what the creditor chooses
If **all** objects are lost due to a **fortuitous event**	Exempts the obligor from nonperformance (Art. 1174)
If **one** object is lost due to **debtor's fault**	Creditor may claim any remaining object or the price of the lost object, plus damages
If **all** objects are lost due to **debtor's fault**	Creditor may claim the price of any one of them, plus damages

Facultative obligation

Art. 1206 ⭐

When only one prestation has been agreed upon, but the obligor may render another in substitution, the obligation is called facultative.

The loss or deterioration of the thing intended as a substitute, through the negligence of the obligor, does not render him liable. But once the substitution has been made, the obligor is liable for the loss of the substitute on account of his delay, negligence or fraud.

	Alternative	**Facultative**
Principal prestation	Several principal but alternative prestations (a, b, or c)	A principal and an accessory/substitute prestation (tiered) (a, or *in the absence thereof*, b)
Effect of nullity of prestation	The nullity of one prestation does not invalidate the obligation. The obligation remains valid as long as there is one valid prestation. Only the impossibility of all prestations without the fault of the debtor extinguishes the obligation (Art. 1204).	The **nullity of the principal** prestation **invalidates** the obligation even if the substitute prestation is valid. The **impossibility** of the principal prestation **extinguishes** the obligation. If the **substitute prestation is void**, the obligation remains **valid** as long as the principal prestation is valid.
Right to elect/choose	Debtor (but creditor, upon stipulation)	Debtor alone

Joint obligations

Art. 1207

The concurrence of two or more creditors or of two or more debtors in one and the same obligation does not imply that each one of the former has a right to demand, or that each one of the latter is bound to render, entire compliance with the prestation. There is a solidary liability only when the obligation expressly so states, or when the law or the nature of the obligation requires solidarity.

Art. 1208

If from the law, or the nature or the wording of the obligations to which the preceding article refers the contrary does not appear, the credit or debt shall be presumed to be divided into as many shares as there are creditors or

debtors, the credits or debts being considered distinct from one another, subject to the Rules of Court governing the multiplicity of suits.

General rule: Joint obligation
- The debt/credit is divided into as many debtors/creditors.

Exception: It becomes solidary only if the law, nature, or the wording (stipulation) of the obligation says so.

Kinds of joint/solidary obligations

	No. of creditors	No. of debtors
Active joint or active solidary	Multiple	One
Passive joint or passive solidary *(most common)*	One	Multiple
Mixed joint or mixed solidary	Multiple	Multiple

Illustrative examples:

1. Nico lent P40 million to Job and Ahmed, who will pay the principal plus interest. On the due date, Nico demanded payment from Job. How much should he Job?
    a. They are joint debtors, who are presumed to pay half. Hence, Job must pay 50% of the P+I.
2. Assume that Ahmed mortgaged his land (REM) to secure payment of the loan. On the due date, Nico demanded payment from Job. How much should Job pay?
    a. Still the same, 50% of P+I.
3. Job did not pay despite demand. Ahmed paid his share. May Nico completely foreclose the REM?
    a. Yes, because the REM secures the entire loan obligation despite the joint liability.
4. Nico and Icon (lenders) lent P40 million to Job and Ahmed, who will pay the principal plus interest. On the due date, Nico demanded payment from Job. Assuming the total amount due is P50 million, how much should Job pay?
    a. Nico is only entitled to P25 million. Of it, Nico can collect half from Job, which is P12.5 million.
5. If Ahmed will pay his half share of the P50 million, to whom he should pay and how much?
    a. He must pay P12.5 million to Nico, and P12.5 million to Icon. This is because the credit or debt shall be presumed to be divided into as many shares as there are creditors or debtors (Art. 1208).
6. Assuming the contract provided a default penalty equal to the 10% of the total amount due. Nico demanded payment from Job, and the latter did not pay. Is Job in default, and what should he pay Nico?
    a. Yes, and Job must pay P+I plus penalty.
7. Is Job in default with respect to Icon? What is his liability to Icon?
    a. No, because Icon, a joint creditor, did not make a demand. Icon's credit is distinct from Nico's. Job is liable to pay P+I only to Icon.
        i. A demand by one is not a demand by the other creditor.
8. Is Ahmed in default?
    a. No, because Ahmed, a joint debtor, did not receive any demand. Ahmed's debt is distinct from Job's.
9. Job did not pay because he is insolvent. Is Ahmed obliged to pay Job's share?
    a. No. Job's insolvency does not increase Ahmed's obligation. Neither does it grant any additional entitlement to Nico and Icon against each other.

Divisibility of joint obligations

Art. 1209

If the division is impossible, the right of the creditors may be prejudiced only by their collective acts, and the debt can be enforced only by proceeding against all the debtors. If one of the latter should be insolvent, the other's shall not be liable for his share.

Art. 1210 ⭐

The indivisibility of an obligation does not necessarily give rise to solidarity. Nor does solidarity of itself imply indivisibility.

Divisibility of joint obligations

1. Joint indivisible obligations – The indivisibility of the prestation does not *ipso facto* import solidarity.
    a. Example: An undertaking by several co-owners of a car to deliver it to one creditor.

2. Performance/breach – Since the obligation is joint, performance must be by all the debtors in favor of all the creditors.
    a. Delay – The liability for damages will be apportioned among the debtors or creditors.
        i. Hence, the prestation becomes divisible among the several parties, without prejudice to the liability of the culpable party to reimburse his co-debtors/creditors for the liability that these latter had to assume.

⚠️ *Indivisibility has to do with the prestation and its performance. Solidarity has to do with the number of parties to an obligation.*

- A joint obligation may be divisible or indivisible. Likewise, a divisible obligation may be joint or solidary.

Illustrative examples:

Nico, and Job and Ahmed entered into a contract of sale of a car worth P5 million. On day 1, Nico will pay P2.5 million. On day 3, Job and Ahmed must deliver the car, and Nico will pay the balance of P2.5 million on day 4. Job did not deliver the car on day 3.

1. Did they default?
    a. No, because there was no demand.
2. What is the nature of Job and Ahmed's obligation to deliver the car?
    a. Joint, despite the car's indivisibility (Art. 1210).
3. On whom should Nico demand?
    a. As the obligation is joint, Nico should demand delivery of the car from both Job and Ahmed (Art. 1209).
4. Upon demand, Job defaulted and preempted the delivery. What happens to the obligation?
    a. It becomes an obligation to pay for damages.
5. What will be the liability of each debtor?
    a. Job will pay for half-share and damages. Ahmed will pay half-share.
        i. The nondefaulting debtor does not answer for the liability of the defaulting debtor.

Nico and Icon, and Job entered into a contract of sale of a car worth P5 million. On day 1, Nico and Icon will pay P2.5 million, and Job will deliver the car on day 3. Nico and Icon will pay the balance of P2.5 million on day 4.

1. Prior to day 3, Icon told Job that he was waiving his right in favor of Job. Does Job still have an obligation?
    a. Yes, because the joint obligation remains despite Icon's waiver. In a divisible obligation, only the collective acts of the creditors can prejudice their rights. Here, only Icon waived.
2. Assuming Icon did not waive. On day 3, Job did not deliver despite Icon's demand. Is Job in default?
    a. The obligation is joint. Hence, Icon's demand does not benefit Nico. Nico and Icon should both demand delivery to place Job in default.
        i. In a joint obligation, any act or omission of a creditor or debtor will only affect the debtor and creditor privy to such act or omission.
3. Job did not deliver on day 3 despite Nico's demand. Is he in default?
    a. Yes. Although both joint creditors should demand, Nico's demand should suffice as Job is creditor and debtor with respect to the other half (reciprocal obligation).

Marsman v. PGI, G.R. 183374, June 29, 2010

In a joint venture (JV) agreement, the joint venture partners are jointly and equally liable to their creditors.

- JVs are governed by the law on partnerships.

Solidary obligation

Art. 1211

Solidarity may exist although the creditors and the debtors may not be bound in the same manner and by the same periods and conditions.

Art. 1212

Each one of the solidary creditors may do whatever may be useful to the others, but not anything which may be prejudicial to the latter.

Art. 1213

A solidary creditor cannot assign his rights without the consent of the others.

Art. 1214

The debtor may pay any one of the solidary creditors; but if any demand, judicial or extrajudicial, has been made by one of them, payment should be made to him. [1]

Art. 1215

Novation, compensation, confusion or remission of the debt, made by any of the solidary creditors or with any of the solidary debtors, shall extinguish the obligation, without prejudice to the provisions of Article 1219.

The creditor who may have executed [2] any of these acts, as well as he who collects the debt, shall be liable to the others for the share in the obligation corresponding to them.

Art. 1216 ⭐

The creditor may proceed against any one of the solidary creditors or some or all of them simultaneously. The demand made against one of them shall not be an obstacle to those which may subsequently be directed against the others, so long as the debt has not been fully collected. [3]

Art. 1217 ⭐

Payment made by one of the solidary debtors extinguishes the obligation. If two or more solidary debtors offer to pay, the creditor may choose which offer to accept.

He who made the payment may claim from his co-debtors only the share which corresponds to each, with the interest for the payment already made. If the payment is made before the debt is due, no interest for the intervening period may be demanded.

When one of the solidary debtors cannot, because of his insolvency, reimburse his share to the debtors paying the obligation, such share shall be borne by all his co-debtors, in proportion to the debt of each.

Art. 1218

Payment by a solidary debtor shall not entitle him to reimbursement from his co-debtors if such payment is made after the obligation has prescribed or become illegal.

[1] Applies to active solidarity. The creditor who demanded must be paid.
[2] The creditor who was able to collect must account and distribute payment to his co-creditors.
[3] Applies to passive solidarity.

Nature of solidary liability

Chiquita Brands v. Omelio, G.R. 189102, June 7, 2017
🍌

Solidary liability is not to be inferred lightly, but must be clearly expressed.

- This, if a judicially approved compromise agreement did not impose solidary liability on the parties' subsidiaries, affiliates, controlled and related entities, successors and assignees, but merely allowed them to benefit from its effects.

AFP-RSBS v. Sanvictores, G.R. 207586, August 17, 2016

Though there are multiple parties in an obligation, if they are denominated only as a singular entity (i.e., “seller” not “sellers”), they are deemed solidary.

Liability of corporations;
When joint, when solidary

BDO v. Seastres, G.R. 257151, February 13, 2023

When the basis of the obligation is contract and there has been a breach, the liability will only affect the party who breached. The liability does not extend to the latter’s agents or agents, and they cannot be held jointly and severally liable to the injured party.

Virata v. Ng Wee, G.R. 220926, July 5, 2017

Basic is the rule that a corporation is invested by law with a personality separate and distinct from that of the persons composing it as well as from that of any other legal entity to which it may be related.

By way of exception, a corporate director, a trustee or an officer, may be held solidarily liable with the corporation under Sec. 31 of the Corporation Code, which provides:

> Section 31. *Liability of directors, trustees or officers*. - Directors or trustees who willfully and knowingly vote for or assent to patently unlawful acts of the corporation or who are guilty of gross negligence or bad faith in directing the affairs of the corporation or acquire any personal or pecuniary interest in conflict with their duty as such directors or trustees shall be liable jointly and severally for all damages resulting therefrom suffered by the corporation, its stockholders or members and other persons.

Right of reimbursement (*cf.* Art. 1217)

- The paying debtor is entitled to reimbursement from his co-debtors in an amount representing the share for each.
  - **Illustrative example:** A, B, C, D, and E are five solidary debtors of X for a loan worth P120,000. A pays the debt in full. Hence, A acquires the right to collect P24,000 each from B, C,

D, and E.

- Nature of obligation of reimbursement – The obligation of the co-debtors to reimburse the paying debtor is *joint*.
- This rule, however, does not apply when the obligation is extinguished, has prescribed or became illegal (Art. 1218).
    - If the prescription or loss is partial, Art. 1218 will only apply to the portion that has been extinguished.
    - Whether the debtor who pays has the right to recover from the creditor will depend on whether or not the rules on *solutio indebiti* (mistake in payment) apply.

Effect of insolvency

- The noninsolvent co-debtors will have to bear proportionately the insolvent debtor's share.
    - Thus, in the example above, if E is insolvent, E's share of P24,000 will be divided among A, B, C, and D. Hence, each noninsolvent co-debtor incurs an additional obligation of P6,000, increasing their payment to P30,000 each.

Right of reimbursement

Lozada v. COA, G.R. 230383, July 13, 2021

There is nothing illegal when a creditor opts to collect from one solidary debtor ahead of any other, as he is expected to do so at his convenience.

- *Remedy of the paying debtor:* The debtor who pays the solidary debt has the right to demand reimbursement from his co-debtors in proportion to each one's share therein. While there is but a single debt in a solidary obligation, this proration establishes that the liability among the debtors is fundamentally joint or equal.

Art. 1219

The remission made by the creditor of the share which affects one of the solidary debtors does not release the latter from his responsibility towards the co-debtors, in case the debt had been totally paid by anyone of them before the remission was effected.

Art. 1220

The remission of the whole obligation, obtained by one of the solidary debtors, does not entitle him to reimburse from his co-debtors.

Remission by creditor

- Art. 1219 applies to cases of remission by the creditor of a co-debtor's share after another co-debtor has made full payment.
    - This remission does not excuse the debtor whose share has been remitted from contributing his share.
    - Balane: A *sensu contrario*, the rule implied in Art. 1219 is that if the remission is made before payment, the share that has been remitted and extinguished and the paying debtor cannot collect from the co-debtor whose share has been remitted.
- If the entire obligation is remitted by the creditor to any of the debtors, no reimbursement will be made to the debtor who received the remission (Art. 1220).
    - This is because no payment was made by the solidary debtor concerned.

Q: What is the juridical effect of the remission of the share of one of the debtors?
A: Such remission extinguishes the obligation in part, i.e, to the extent of the share remitted.

Art. 1221

If the thing has been lost or if the prestation has become impossible without the fault of the solidary debtors, the obligation shall be extinguished.

If there was fault on the part of any one of them, all shall be responsible to the creditor, for the price and the payment of damages and interest, without prejudice to their action against the guilty or negligent debtor.

If through a fortuitous event, the thing is lost or the performance has become impossible after one of the solidary debtors has incurred in delay through the judicial or extrajudicial demand upon him by the creditor, the provisions of the preceding paragraph shall apply.

Loss/impossibility in passive solidary obligations

- Fortuitous loss/impossibility of performance → Obligation extinguished.
    - Loss/impossibility after delay → Debtor will not be excused from liability (*see* Art. 1165, par. 3).
- Culpable loss/impossibility
    - Loss or impossibility caused by the fault or negligence of any of the solidary debtors is the solidary liability of all (*see* Art. 2194).
    - The debtor guilty of fault/negligence will be liable for any

damage or liability suffered by his co-creditors because of his fault/negligence.

Art. 1222

A solidary debtor may, in actions filed by the creditor, avail himself of all defenses which are derived from the nature of the obligation and of those which are personal to him, or pertain to his own share. With respect to those which personally belong to the others, he may avail himself only as regards that part of the debt for which the latter are responsible.

In a suit by the creditor against the solidary debtor, the latter may present three possible defenses:

1. One arising from the nature of the obligation itself, e.g., the illegality of the object, or prescription of the entire obligation
    a. This is a **real** defense. The defendant-debtor is free of liability.
2. One personal to the defendant-debtor
    a. If the defense consists of vitiation of consent, this is a **total** defense → obligation is voidable
    b. If the defense involves some special terms/stipulations, this is a **partial** defense → valid only as far as the defendant's share is concerned
3. One personal to the other debtors
    a. This is a **partial** defense, covering only the co-debtor's share

Summarizing

	Joint	**Solidary**
Nature	Several obligations (there are as many obligations as the no. of debtors multiplied by the no. of creditors)	Single obligation even if there are multiple parties
Who can be sued and how much can be recovered	Creditor can sue each of the debtors only to their proportionate amount (sum/debtors). To recover entire amount, creditor has to sue all debtors.	*Active*: Any of the creditors may demand the whole amount from the creditor • Mutual agency *Passive*: Creditor may demand the whole amount from any of the debtors. • Mutual guaranty
Failure/refusal of a debtor	The failure or refusal of one debtor to pay his share does not give rise to any additional liability on the part of the co-debtors	-
Effect of demand	Only affects the debtor who received the demand. Such demand on a debtor does not affect the other debtors	*Creditor*: Demand by one is demand by all *Debtor*: Demand on one is demand on all
Insolvency of one debtor	The insolvency of one debtor does not increase the liability of other co-debtors	Any of the other debtors can still be made to pay the whole amount (Art. 1217)
Payment	-	The payment of one solidary co-debtor is extinguished in whole, or to the extent of the payment, with the right on the part of the debtor to recover from the co-debtors their shares (Art. 1217)

Divisible obligations

Art. 1223

The divisibility or indivisibility of the things that are the object of obligations in which there is only one debtor and only one creditor does not alter or modify the provisions of Chapter 2 of this Title.

Divisible – One which is susceptible of partial performance.

- The debtor can legally perform the obligation by parts and the creditor cannot demand a single performance of the entire obligation.

Indivisible – The obligation is indivisible when it cannot be validly performed in parts.

⚠️ *The divisibility refers to the performance of the obligation, not its object.*

General rule: Obligations are indivisible, whether the object of the prestation is divisible or indivisible. Therefore, the performance cannot be effected in parts, but in one act.
Exceptions:

1. The parties provide otherwise
    a. E.g., Art. 1248, a loan agreement which provides for payment in installments.
2. When the nature of the obligation necessarily entails performance in parts
    a. E.g., Art. 1225, par. 2, a contract for the furnishing of security guard services for a certain number of hours a day over a certain specified period
3. When the law provides otherwise:
    a. When the debt is liquidated in part and unliquidated in part (Art. 1248, par. 2)
    b. Joint divisible obligations (Art. 1208)
    c. Solidary obligations in which the debtors are bound under different terms or conditions (Art. 1211)
    d. In cases of compensation, when a balance is left (Art. 1290)
    e. If a piece of work is to be delivered partially, the price for each part having been fixed, the price is also payable (Art. 1720)
    f. Debts guaranteed by several guarantors who are entitled to the benefit of division (Art. 2065)
    g. Impossibility or extreme difficulty of a single performance

Joint indivisible obligation

Art. 1224

A joint indivisible obligation gives rise to indemnity for damages from the time anyone of the debtors does not comply with his undertaking. The debtors who may have been ready to fulfill their promises shall not contribute to the indemnity beyond the corresponding portion of the thing or of the value of the services in which the obligation consists.

Joint indivisible obligation – Performance by the debtors must be done by all of them together.

Effect of noncompliance by one debtor – The obligation, at the creditor's option, converts into one for damages.

- The prestation becomes divisible, and each debtor becomes individually liable only for his proportionate part of the amount.

Damages from the contravening debtor – The debtor whose contravention caused the breach shall be liable to his co-debtors for damages occasioned by said breach.

- Those not liable from the breach, however, shall not contribute to the indemnity in excess of his share in the obligation.

Divisible obligation

Art. 1225 ⭐

For the purposes of the preceding articles, obligations to give definite things and those which are not susceptible of partial performance shall be deemed to be indivisible.

When the obligation has for its object the execution of a certain number of days of work, the accomplishment of work by metrical units, or analogous things which by their nature are susceptible of partial performance, it shall be divisible.

However, even though the object or service may be physically divisible, an obligation is divisible if so provided by law or intended by the parties.

In obligations not to do, divisibility or indivisibility shall be determined by the character of the prestation in each particular case.

Partial nonperformance

In **indivisible** obligations: Partial nonperformance is total nonperformance, under the rule of indivisibility, except:

1. Substantial performance in good faith (Art. 1234)
2. Waiver by the creditor (Art. 1235)

In **divisible** obligation: The problem in these cases is the determination of the effect of partial breach and the extent of the damages recoverable (*see* Art. 1191).

UCPB v. E. Ganzon Inc., G.R. 244247, November 10, 2021

In determining the divisibility of an obligation, the following factors may be

considered:
1. Intent of the parties
2. Objective or purpose of the stipulated prestation
3. Nature of the thing
4. Provisions of law affecting the prestation

However, while the obligation to give in the MOA is indivisible and not susceptible of partial performance, the fact that the parties entered into several dacion en pago transactions now precludes them from denying the divisible nature with respect to the securities to be assigned.
- Here, the contemporaneous and subsequent acts of the parties were considered.

Penal clauses

Art. 1226 ⭐

In obligations with a penal clause, the penalty shall substitute the indemnity for damages and the payment of interests in case of noncompliance, if there is no stipulation to the contrary. Nevertheless, damages shall be paid if the obligor refuses to pay the penalty or is guilty of fraud in the fulfillment of the obligation.

The penalty may be enforced only when it is demandable in accordance with the provisions of this Code.

Art. 1227 ⭐

The debtor cannot exempt himself from the performance of the obligation by paying the penalty, save in the case where this right has been expressly reserved for him. Neither can the creditor demand the fulfilment of the obligation and the satisfaction of the penalty at the same time, unless this right has been clearly granted him. However, if after the creditor has decided to require the fulfillment of the obligation, the performance thereof should become impossible without his fault, the penalty may be enforced.

Penal clause – An accessory undertaking to assume greater liability on the part of an obligor in case of breach of an obligation.

Two functions of penal clauses:
1. Provide for liquidated damages
    a. The parties determine in advance the damages payable in case of breach. Such a stipulation facilitates future litigation and spares the parties the often difficult and protracted process of having to prove the extent and amount of damages.
2. Strengthen the coercive force of obligations
    a. To make the indemnity for breach more burdensome.
        i. However, the stipulation must at least be more burdensome than the legal rate (>6%).

Tan v. First Malayan Leasing and Finance Corp., G.R. 254510, June 16, 2021

The nature of a penalty charge and liquidated damages are similar, and they may not be simultaneously imposed without violating the fundamental concepts of iniquity and excessiveness, and notwithstanding the contractual autonomy of the parties herein.

1. Penalty as reparation/compensation – The stipulated indemnity represents a legitimate estimate made by the parties caused by the breach of the obligation.
    a. No need to prove actual damages.
2. Penalty as punishment – The question of damages is not yet resolved inasmuch as the right to damages, besides the penalty, still subsists.
    a. The injured party must prove actual damages if he desires to recover damages.

Reduction if iniquitous or unconscionable
- Courts may equitably reduce a stipulated penalty in the contract if it is iniquitous or unconscionable, or if the principal obligation has been partly or irregularly complied with.

Factors in determining if penalty is iniquitous or unconscionable
1. Type
2. Extent
3. Purpose of the penalty
4. Nature of the obligation
5. Mode of breach and its consequences
6. Supervening realities
7. Standing relationship of the parties

Classification of penal clause
General rule: A penal clause is subsidiary (Art. 1227) and exclusive (Art. 1226).
1. Subsidiary/alternative – Upon breach, only the penalty is demandable.
    a. Exception: Joint/cumulative – Both the principal undertaking and the penalty are demandable; applies when there is a clear grant.
2. Exclusive/reparative – The penalty takes the place of damages (Art.

1226).
   a. Exception: Inclusive/punitive – Damages in addition to the penalty may be demanded. Damages can be demanded in addition to the penalty:
      i. When so stipulated
      ii. When the debtor refuses to pay the penalty
      iii. When the debtor is guilty of fraud in the fulfillment of the obligation

Art. 1228

Proof of actual damages suffered by the creditor is not necessary in order that the penalty may be demanded.

Proof of actual damages is dispensed with the very nature of a penal clause/liquidated damages.
- The clause makes proof of damages actually suffered irrelevant and superfluous.
- The penal clause constitutes predetermined damages.

Art. 1229

The judge shall equitably reduce the penalty when the principal obligation has been partly or irregularly complied with by the debtor. Even if there has been no performance, the penalty may also be reduced by the courts if it is iniquitous or unconscionable.

Penalty may be reduced when:
1. The principal obligation has been partly or irregularly complied with
2. There is no performance, but the penalty is iniquitous or unconscionable

Art. 1230

The nullity of the penalty clause does not carry with it that of the principal obligation.

The nullity of the principal obligation carries with it that of the penal clause.

There may be instances where the penalty is enforceable despite the defective nature of the principal obligation:
1. When the penalty is undertaken by a third person precisely for an obligation which is unenforceable, voidable or natural, in which case it assumes the form of a guaranty which is valid (Art. 2052)
2. When the nullity of the principal obligation itself gives rise to liability of the debtor for damages, such as when the vendor knew that the thing was nonexistent at the time of the contract
   a. In this case, the vendor becomes liable for damages, although the contract itself is avoided; and since the penalty is merely a substitute for damages, it can be enforced.

Chapter 4
Extinguishment of Obligations

Art. 1231 ⭐

Obligations are extinguished:
(1) By payment or performance;
(2) By the loss of the thing due;
(3) By the condonation or remission of the debt;
(4) By the confusion or merger of the rights of creditor and debtor;
(5) By compensation;
(6) By novation.

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

Other causes of extinguishment:
1. Death of a party
   a. Applicable to obligations *intuitu personae*
2. Rebus sic stantibus (*see* Art. 1267)
3. Mutual dissent (mutuo disenso)
   a. This will operate when the parties, before full performance, agree to cancel or discontinue the contract.
4. Judicially declared insolvency
5. Waiver by the creditor (*see* Art. 6)
6. Compromise (Arts. 2028-2041)
7. Arrival of resolutory term (Art. 1193, par. 2)
8. Change of civil status
   a. Example: When a marriage is annulled, the mutual obligation of support is also extinguished.

9. Withdrawal by one of the parties
    a. Example: Withdrawal of a partner from a partnership (*see generally* Art. 1830, par. b)
10. Disappearance or cessation of the creditor's interest

Art. 1232

Payment means not only the delivery of money but also the performance, in any other manner, of an obligation

Payment/performance – Normal, perfect mode of extinguishment of obligations.

- All the other modes are abnormal.

Payment – To give
Performance – To do/not to do

Rules on payment/performance ♥

The prestation (objective)

A. Identity
    a. If specific – The very thing or service must be delivered or performed (Art. 1244)
    b. If generic – The prestation must be neither inferior nor superior in quality (Art. 1246)
    Special rules for money debts:
        1. Payment must be in the currency stipulated. In the absence of stipulation, PhP (Art. 1249)
        2. Payment in negotiable paper:
            a. May be refused by creditor,
            b. In any case, provisional only until encashed or impaired through creditor's fault
            c. Revaluation in case of extraordinary inflation or deflation (Art. 1250)
    Exceptions to requirement of identity:
        1. Dacion en pago (Art. 1245)
        2. Novation

B. Integrity – The entire prestation must be performed.
    Exceptions:
        1. Substantial performance in good faith (Art. 1234)
        2. Waiver by creditor/obligee (Art. 1235)
        3. In application of payments, if the several debts are equally onerous (Art. 1254, par. 2): rule of *pro rata* application

C. Indivisibility – Performance in a single act
    Exceptions:
        1. Express stipulation (Art. 1248)
        2. Prestations which necessarily entail partial performance (Art. 1225)
        3. If debt is liquidated in part and unliquidated in part (Art. 1248)
        4. Joint divisible obligations (Art. 1208)
        5. Solidary obligations in which debtors are bound under different terms or conditions (Art. 1211)
        6. In compensation, when a balance is left (Art. 1290)
        7. If the work is to be delivered partially, the price for each part having been fixed, price also payable partially (Art. 1720)
        8. Several guarantors who demand division (Art. 2065)
        9. Impossibility or extreme difficulty of single performance

The parties (subjective)

A. The payor
    1. Without need of creditor's consent (as a matter of right)
        a. Debtor/obligor himself
        b. Heir or assignee
        c. Agent
        d. Anyone interested in fulfillment of obligation (guarantor)
    2. With creditor's consent
        a. Anyone
    Effect of payment by third person:
        1. If with debtor's consent – subrogation (Arts. 1236-1237)
            a. Exception: Third person intended it as a donation (Art. 1238)
        2. If without the debtor's consent – reimbursement to the extent of the benefit (Art. 1236, par. 2)

B. The payee
    1. The creditor/obligee himself (Art. 1240)
    2. Successor or transferee (Art. 1240)
    3. Agent (Art. 1240)
    4. A third person:
        a. Provided it redounded to the creditor's benefit and only to the extent of such benefit (Art. 1241, par. 2)
        b. Benefit deemed to be total if under Art. 1241 (1-3).
    5. Anyone in possession of the credit (Art. 1242)

    In all these cases, the payment is effective provided the debt has not been garnished (Art. 1243)

Time and place

1. Time – when due (Art. 1269)

2. Place:
    a. Primary rule: stipulation
    b. Secondary rule: place where thing was at time of constitution of obligation (if obligation is to deliver a determinate thing)
    c. Tertiary rule: debtor's domicile

Special forms of payment
1. Dacion en pago (Art. 1245)
2. Application of payments (Arts. 1252-1254)
3. Payment by cession (Art. 1255)
4. Consignation (Art. 1256-1261)

Integrity of payment

Art. 1233 ⭐

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.

General rule: Partial performance is no performance →breach
Exceptions:
1. Substantial performance in good faith
2. Waiver by creditor/obligee
3. *Pro rata* rule in case of several debts of the same nature and burden

Art. 1234 ⭐

If the obligation has been substantially performed in good faith, the obligor may recover as though there had been a strict and complete fulfillment, less damages suffered by the obligee.

Juxtaposed with Art. 1191: The operation of Art. 1234 prevents the application of Art. 1191 (resolution).
- If there's breach but also substantial performance, resolution is not available.

Waiver for integrity of payment

Art. 1235

When the obligee accepts the performance, knowing its incompleteness or irregularity, and without expressing any protest or objection, the obligation is deemed fully complied with.

The debtor/obligee has the right to waive or renounce integrity, in accordance with Art. 6.

International Hotel Corp. v. Joaquin, G.R. 158361, April 10, 2013 ♥

Art. 1234 applies only when an obligor admits breaching the contract after honestly and faithfully performing all the material elements thereof except for some technical aspects that cause no serious harm to the obligee.

By reason of the inconsequential nature of the breach or omission, the law deems the performance as substantial, making it the obligee's duty to pay.

Conversely, the principle of substantial performance is inappropriate when the incomplete performance constitutes a material breach of the contract.

Southstar (*supra* art. 1169)

The acceptance of the contractor's work implies a waiver of the irregularities, if any, in such a work. Hence, the obligation will be deemed complete, and the contractor is entitled to payment.

HSBC-SRP v. Galang, G.R. 199565, June 30, 2021

Accepting payment without objection complies with an obligation.
- Hence, the creditor is estopped from placing the debtors in default when the latter have paid consistently following several "installment due reminders."

Rules on payor;
Payment by a third person

Art. 1236

The creditor is not bound to accept payment or performance by a third person who has no interest in the fulfillment of the obligation, unless there is a stipulation to the contrary.

Whoever pays for another may demand from the debtor what he has paid, except that if he paid without the knowledge or against the will of the debtor, he can recover only insofar as the payment has been beneficial to the debtor.

Art. 1237

Whoever pays on behalf of the debtor without the knowledge or against the will of the latter, cannot compel the debtor to subrogate him in his rights, such as those arising from a mortgage, guaranty, or penalty.

Art. 1238

Payment made by a third person who does not intend to be reimbursed by the debtor is deemed to be a donation, which requires the debtor's consent. But the payment is in any case valid as to the creditor who has accepted it.

Rule: Strangers cannot validly perform the obligation unless so stipulated or consented by the creditor.

Effects of payment by a third person
General rule: Anyone may pay if the creditor is willing to accept performance

1. If with consent and knowledge of the debtor, there will be subrogation of the third person in the creditor's rights.
    a. The third person-payor becomes the creditor, and acquires the right to demand payment from the debtor.
        i. Exception: If the third person intended payment as a donation.
2. If a third person paid without consent, he can only recover from the debtor only to the extent that the debtor has benefited.
    a. Illustrative example: Creditor lent P100,000 to debtor payable in a year. By the 6th month, the debtor only paid P30,000, with a balance of P70,000. At the same time, a third person paid the obligation, giving P100,000 to the creditor.
        i. Here, the third person can only recover P70,000.
        ii. This is without prejudice to the application of *solutio indebiti* between the third party and the debtor.

Payment by incapacitated person

Art. 1239

In obligations to give, payment made by one who does not have the free disposal of the thing due and capacity to alienate it shall not be valid, without prejudice to the provisions of Article 1427 under the Title on "Natural Obligations."

Incapacitated person – One who does not have the free disposal of the thing due and capacity to alienate it.

Case 1: Creditor is aware of incapacity – He accepts the thing at his own risk.
Case 2: Creditor is unaware of incapacity – The debtor or the person who has a better right to the property may recover the same.

Balane: The only exception in this article is Art. 1427 (payment of a minor). However, this codal is now dead letter. Hence, there is no more exception.

Payee

Art. 1240

Payment shall be made to the person in whose favor the obligation has been constituted, or his successor in interest, or any person authorized to receive it.

Art. 1241

Payment to a person who is incapacitated to administer his property shall be valid if he has kept the thing delivered, or insofar as the payment has been beneficial to him.

Payment to a third person shall also be valid insofar as it has redounded to the benefit of the creditor. Such benefit to the creditor need not be proved in the following cases:

(1) If after the payment, the third person acquires the creditor's rights;
(2) If the creditor ratifies the payment to the third person;
(3) If by the creditor's conduct, the debtor has been led to believe that the third person had authority to receive the payment.

Art. 1242

Payment made in good faith to any person in possession of the credit shall release the debtor.

To whom payment shall be made
General rule: Payment should be made to the creditor himself

- Payment to an incapacitated creditors are only valid to the extent:
    - Of what the creditor has kept
    - That the creditor has benefited

Exceptions:

1. The creditor's transferee or representative
    a. Transferees – Successors-in-interest (donees, vendees, heirs,

devisees, legatees, subrogees or assignees)
   b. Representatives – Those who stand in the place of the creditor
2. Anyone in possession of the credit
   a. Example: Bearer of a promissory note who may have come into possession of the paper through theft.
3. Third persons – Only to the extent of the benefit of the creditor. Benefit need not be proven in:
   1. Third person acquires creditor's rights (third person becomes creditor)
   2. Creditor ratifies payment of the third person
   3. Debtor has been led to believe that the third person had authority to receive the payment
      a. Basis: Estoppel

Art. 1243

Payment made to the creditor by the debtor after the latter has been judicially ordered to retain the debt shall not be valid.

Identity in specific thing

Art. 1244 ⭐

The debtor of a thing cannot compel the creditor to receive a different one, although the latter may be of same value as, or more valuable than that which is due.

In obligations to do or not to do, an act or forbearance cannot be substituted by another act or forbearance against the obligee's will.

Identity – The very prestation must be performed.

Applicable to specific obligations. For generic obligations, see *Art. 1246*.

Exceptions to the rule of identity:
1. Dacion en pago
2. Novation

Identity in generic thing

Art. 1246

When the obligation consists in the delivery of an indeterminate or generic thing, whose quality and circumstances have not been stated, the creditor cannot demand a thing of superior quality. Neither can the debtor deliver a thing of inferior quality. The purpose of the obligation and other circumstances shall be taken into consideration.

Rule of identity in generic obligations:
1. The creditor cannot require the delivery of something that is superior in quality.
2. The debtor cannot insist on delivering an inferior thing.

In case of dispute between the creditor and debtor on a thing's quality, the courts will have to decide.

Costs

Art. 1247

Unless it is otherwise stipulated, the extrajudicial expenses required by the payment shall be for the account of the debtor. With regard to judicial costs, the Rules of Court shall govern.

Extrajudicial costs
- In reciprocal obligations, each party bears the costs of the performance of his own prestation.
  - This is because in a reciprocal obligation, each party is a debtor.
- Nevertheless, parties may stipulate to the contrary.

Indivisibility of payment

Art. 1248 ⭐

Unless there is an express stipulation to that effect, the creditor cannot be compelled partially to receive the prestations in which the obligation consists. Neither may the debtor be required to make partial payments.

However, when the debt is in part liquidated and in part unliquidated, the creditor may demand and the debtor may effect the payment of the former without waiting for the liquidation of the latter.

General rule: The performance of an obligation cannot be broken up into parts.

- Obligations in general are indivisible, regardless of the (in)divisibility of the object of the prestation (*see Arts. 1223-1225*).
- Therefore, partial performance is a breach of the entire obligation and may be refused by the creditor.
    - But, the debtor may also refuse partial performance should the creditor request it!
- The rule of indivisibility may be invoked by both parties.

Exceptions:

1. Express stipulation
2. Liquidated in part, unliquidated in part
    a. In this case, only the liquidated debt may be paid

We'll skip legal tender (Art. 1249) and come back to it later.

Location of payment

Art. 1251

📍

Payment shall be made in the place designated in the obligation.

There being no express stipulation and if the undertaking is to deliver a determinate thing, the payment shall be made wherever the thing might be at the moment the obligation was constituted.

In any other case the place of payment shall be the domicile of the debtors.

If the debtor changes his domicile in bad faith or after he has incurred in delay, the additional expenses shall be borne by him.

These provisions are without prejudice to venue under the Rules of Court.

Time and place

1. Time – when due; default (Art. 1169)
2. Place:
    d. Primary rule: stipulation
    e. Secondary rule: place where thing was at time of constitution of obligation (if obligation is to deliver a determinate thing)
    f. Tertiary rule: debtor's domicile

End of midterm coverage.