



Republic of the Philippines
Supreme Court
Manila

THIRD DIVISION

ELISEO N. HAO,
 Petitioner,

G.R. No. 247472

Present:

LEONEN, *J.*,
Chairperson,
 CARANDANG,
 ZALAMEDA,
 ROSARIO, and
 DIMAAMPAO, *JJ.*

- versus -

EMERLINDA* S. GALANG,
 Respondent.

Promulgated:

October 6, 2021

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D E C I S I O N

CARANDANG, J.:

This Court resolves the instant petition for review on *certiorari* under Rule 45 of the Rules of Court that assails the Decision¹ dated May 10, 2019 of the Court of Appeals (CA) in CA-G.R. SP No. 157869 affirming the Decision of the Regional Trial Court that petitioner Eliseo N. Hao (Hao) is primarily liable to pay rental arrears in an unlawful detainer case filed by respondent Ermelinda S. Galang (Galang).

Factual Antecedents

On February 25, 2011, Hao signed a lease contract² over a property owned by respondent Galang. The lease over the property was for a period five years beginning April 1, 2011 with monthly rentals amounting to ₱100,000.00. Hao leased the property for the establishment of a diagnostic

* Ermelinda in some parts of the *rollo*.

¹ Penned by Associate Justice Ma. Luisa C. Quijano-Padilla, with the concurrence of Associate Justices Elihu A. Ybañez, and Gabriel T. Robeniol; *rollo*, pp. 29-36.

² *Id.* at 45-51.

center. In March 2011, Hao, together with other individuals organized under Philippine Corporate laws Suremed Diagnostic Center Corp. (SUREMED). Upon incorporation, Hao was the company president. Eventually, SUREMED began operating its business at the property subject of the contract of lease.³

In 2012, Dr. Ramon Ragos (Dr. Ragos) replaced Hao as president of SUREMED. Due to the change in the corporate presidency, Galang sent a revised lease contract replacing Hao as the signing lessee to SUREMED because the company continued to occupy Galang's property. However, SUREMED refused to execute a new lease contract. Nonetheless, the company continued occupancy of the property in 2013.⁴

SUREMED incurred delays in paying rent by 2013, but it was in 2014 that the company failed to make payments to Galang. In April 2014, Galang sent a letter to Dr. Ragos as president of SUREMED, demanding payment of the rental arrears.⁵ However, SUREMED did not respond to the letter and failed to issue checks and post-dated checks to cover the rent for the property. In May 2014, Galang again sent a demand letter for payment of rental arrears with notice to vacate to Dr. Ramon Ragos, in his capacity as President of SUREMED.⁶ As of June 2014, SUREMED's rental arrears amounted to ₱540,655.75. For this reason, Galang sent to Hao and Dr. Ramon Ragos a demand letter dated June 5, 2014 with notice to vacate for failure to pay rent in February, March, April, May and June 2014.⁷ As neither Hao nor SUREMED responded to the letter, Galang filed, on June 13, 2014, an unlawful detainer suit against Hao and SUREMED.⁸

Hao and SUREMED both argued that Galang has no cause of action against them. As to SUREMED, the company denied liability because it is not a party to the lease contract. Hao signed the lease contract as lessee and even failed to present proof that he was authorized by the company to execute the lease contract. There was also no proof of replacement of Hao as lessee to the contract.⁹ Moreover, the complaint for unlawful detainer should be dismissed because SUREMED is no longer in possession of the property in July 2014.¹⁰ SUREMED filed a counterclaim against Galang praying for payment of damages and attorney's fees.¹¹

Hao, on the other hand, argued that Galang is estopped from ascribing liability to him under the lease contract. Galang is aware that the leased property was for the use of SUREMED in running its business. In fact, she initially sent several demand letters for payment of rental arrears to Dr.

³ Id. at 38-39.

⁴ Id. at 39.

⁵ Id. at 53-54.

⁶ Id. at 55-56.

⁷ Id. at 57-60.

⁸ Id. at 40.

⁹ Id. at 66-72.

¹⁰ Id. at 64.

¹¹ Id. at 72-73

Ragos, president of SUREMED. Hao also argued that he could not have had any knowledge or participation of SUREMED's refusal to execute a new contract or failure to pay lease in 2014 as he was no longer the corporate president at such time.¹²

Hao filed a cross-claim against SUREMED in the same unlawful detainer suit. He argued that the company is the actual lessee of the Galang's property. He asserted that should he be made liable to pay whatever amount from the unlawful detainer suit, SUREMED must pay the same directly to Galang.¹³

Ruling of the Metropolitan Trial Court

In a Decision¹⁴ dated July 25, 2017, the Metropolitan Trial Court (MTC) held that ordering Hao and SUREMED to vacate the property is moot and academic as SUREMED no longer occupied the property. The obligation to pay belongs to Hao as he is the lessee-signatory in the lease contract. While the lease contract specifies that the premises shall be used for diagnostic center purposes, the MTC held that there was no mention if the same was for the exclusive use of SUREMED. Even assuming that the lease was for SUREMED, there was no evidence showing that Hao was given authority by the company to enter into a lease contract with Galang. The MTC dismissed the complaint for unlawful detainer against SUREMED because the company is not a privy to the lease contract. The MTC found Hao liable for payment of the rental arrears, ₱20,000.00 attorney's fees and the cost of suit. Corollary, the MTC dismissed the cross-claim of Hao against SUREMED. The counterclaim filed by SUREMED against Galang was also dismissed.

Ruling of the Regional Trial Court

Hao appealed the MTC Decision with the Regional Trial Court (RTC) of Quezon City, Branch 98. In a Resolution dated April 27, 2018,¹⁵ the RTC affirmed the ruling of the MTC holding that SUREMED is not privy to the lease contract with Galang because Hao signed the same as lessee. The RTC held that there is no substitution of the lessee in the contract because novation of the contract had not taken place. There is no record showing that a new contract unequivocally declares the old and new obligations to be on every point incompatible with each other. Notably, SUREMED even refused to execute a revised contract and issue post-dated checks for the reason that it does not want to be bound as lessee of Galang. The RTC held that Hao was not released from liability under the lease contract he signed. The RTC held that "not too uncommon is when a stranger to a contract agrees to assume an obligation; and while this may have the effect of adding to the number of persons liable, it does not necessarily imply extinguishment of the

¹² Id. at 80-81.

¹³ Id. at 82-83.

¹⁴ Penned by Presiding Judge Josephus Joannes H. Asis; id. at 149-159.

¹⁵ Id. at 204-211.

liability of the first debtor.” In fact, Galang sent her demand letters for payment of arrears, not only to SUREMED but also to Hao. Anent the issue of dismissal of Hao’s cross-claim, the RTC held that he may file a separate action for collection of sum of money against SUREMED.

Ruling of the Court of Appeals

Hao filed a petition for review under Rule 42 of the Rules of Court with the CA. In a Decision¹⁶ dated May 10, 2019 the CA upheld the ruling of the RTC finding Hao liable for the unpaid rentals. There was no evidence showing that SUREMED acceded to a “new” lease contract. In fact, SUREMED refused to execute a new one. Hence, there could not have been a valid substitution of a debtor as claimed by Hao. In the same vein, novation of the original lease contract could not have taken place. Anent the dismissal of Hao’s cross-claim against SUREMED, the CA held that the unlawful detainer case against SUREMED was dismissed for lack of cause of action. In view of the dismissal of the case against SUREMED, the cross-claim of Hao against said company can no longer subsist.

Proceedings before this Court

Unsatisfied with the CA decision, Hao filed the instant petition.¹⁷ Hao reiterated that there was subjective novation wherein his obligation with Galang was extinguished and a new one was created between Galang and SUREMED. Moreover, SUREMED is the actual occupant over the property. Galang does not dispute this because she even sent demand letters with notice to vacate to the company. Hao also claimed that checks were issued by SUREMED in favor of Galang. Galang’s knowledge and acceptance of checks from the company clearly show that she intended to dissolve the old contract with Hao and recognizes the lease of SUREMED. Accordingly, SUREMED is liable for the rental arrears subject of the unlawful detainer suit. The suit against SUREMED should not have been dismissed and the cross-claim of Hao against said company should be allowed.

In her Comment,¹⁸ Galang argued that by the lease contract alone, it can be indubitably established that Hao is the lessee of her property. While the contract is explicit that the lease was for purposes of the establishment and set-up of a diagnostic center, SUREMED was not yet incorporated at the time of the execution of the contract. Moreover, SUREMED never consented or acceded to the execution of a new lease contract. Therefore, there can be no change in the person of the debtor and there is no novation of the contract, express or implied. Galang argued that whatever agreement Hao had with SUREMED as to the lease of the property is beyond her. In so far as Galang is concerned, Hao is obliged to pay the rent per the lease contract.

¹⁶ Supra note 1.

¹⁷ *Rollo*, pp. 9-22.

¹⁸ *Id.* at 269-281.

Ruling of the Court

The crux of controversy is whether or not Hao is personally liable for the rental arrears over SUREMED's use of the property owned by Galang. Galang mainly argued that, on the face of the lease agreement, Hao is liable for the arrears because he signed the agreement as lessee. We, however, find it necessary to review the surrounding circumstances of Hao and Galang's execution of the lease contract in order to properly resolve the issue.

From the facts, it is undisputed that Hao, in February 2011, executed a lease contract with a period of five years for the purpose of establishing and setting-up a diagnostic center. After the incorporation of SUREMED in March 2011, it was the company that took possession and occupied the leased premises to operate its business. It is also undisputed that Hao was a stockholder and initially the President of SUREMED upon its incorporation and when the company occupied the leased property in April 2011. Based on these circumstances, We find that Hao should not be made liable for the rent because he did not act in his personal capacity in entering the lease agreement but only as an agent of SUREMED.

Indeed, at the time of execution of the contract of lease in February 2011, SUREMED had not come into legal existence. SUREMED had no legal capacity¹⁹ but can act thru an agent, Hao. Under corporate law, contracts entered, prior corporate existence, by its representatives "have binding effects depending on the prevailing circumstances."²⁰ Among which is "where a contract is entered into with the parties knowing fully well that a corporation does not yet legally exist,"²¹ particularly a corporation yet to be registered or still in the process of registration.²² These contracts are entered into in the name of the intended corporation by the "promoters" or

¹⁹ SUREMED only acquires the capacity to enter into a valid contract when it has been created by the law governing it. The principle of a corporation as a juridical person can be found in Articles 44, 45 and 46 of the Civil Code of the Philippines.

Article 44. The following are juridical persons:

- (1) The State and its political subdivisions;
- (2) **Other corporations, institutions and entities for public interest or purpose, created by law; their personality begins as soon as they have been constituted according to law;**
- (3) Corporations, partnerships and associations for private interest or purpose to which the law grants a juridical personality, separate and distinct from that of each shareholder, partner or member.

Article 45. Juridical persons mentioned in Nos. 1 and 2 of the preceding article are governed by the laws creating or recognizing them.

Private corporations are regulated by laws of general application on the subject.

x x x x

Article 46. Juridical persons may acquire and possess property of all kinds, **as well as incur obligations** and bring civil or criminal actions, in conformity with the laws and regulations of their organization. (38a)

²⁰ Cesar L. Villanueva, *Corporate Contract Law: Unifying theme on Theories relating to Promoter's Contracts, De Facto Corporations, Corporation by Estoppel, Articles of Incorporation, By Laws, and Ultra Vires Acts*, Ateneo Law Journal, Vol. 38 No. 2, p. 6. Accessed at <<http://ateneolawjournal.com/Media/uploads?2a44f914b2c4cb34797b321cab841305.pdf>> on September 16, 2021.

²¹ Id.

²² Villanueva, C., *Philippine Corporate Law* 2013 Ed., p. 143.

organizers of the corporation to establish the corporate business enterprise.²³ Contracts of this nature are known as promoter's contracts or pre-incorporation contracts which are governed by the Law on Agency.²⁴ Applying the pertinent provisions of agency in the Civil Code of the Philippines, Article 1897 of the law explicitly provides that "an agent who acts as such is **not personally liable** to the party with whom he contracts, unless he expressly binds himself or exceeds the limits of his authority without giving such party sufficient notice of his powers."

As discussed, Hao's purpose of entering the contract of lease was not a personal affair but in preparation to establish a diagnostic center. Galang is knowledgeable of this purpose²⁵ and even stated in her Judicial Affidavit that SUREMED is not mentioned in the contract of lease at the time of its execution "because Dr. Eliseo N. Hao and his colleagues were still in the process of setting up the corporation."²⁶ Galang is fully aware that Hao was only acting in representation of a corporation in the process of organization and incorporation. Hao's role as an agent of SUREMED is fortified by the undisputed fact that after SUREMED's organization, the company, without Galang's dissent, occupied the leased premises. If indeed Hao was the intended lessee, Galang could have immediately terminated the lease contract for Hao's violation of the provision²⁷ on the prohibition on subletting. If Hao was tenant-lessee, SUREMED's occupancy would in effect be a sublessor. However, Galang made no such termination or at least a warning to Hao. She does not deny collecting rent from SUREMED through checks issued by the company. Galang even demanded solely from SUREMED payment of rental arrears when the latter defaulted. Clearly, SUREMED stands to be the lessee in the contract. The fact that Galang later sent a demand letter to Hao does not change his status as an agent of SUREMED.

The contract of lease between the parties is clearly a pre-incorporation contract, wherein the "representative of a corporation in the process of incorporation binds oneself to ensure that the corporation, once formed, will ratify the contract entered in its name. The representative becomes personally liable for such contract in the event that the corporation does not so ratify it once it comes into existence."²⁸ Article 1898²⁹ and Article 1901³⁰ of the Civil Code of the Philippines demonstrates the effects of the principal's ratification or non-ratification of the acts of the agent. Relatedly, the "principle of ratification is essential in making every pre-incorporation contract valid and binding against the newly created corporation, since the

²³ Id. at 146.

²⁴ Id. at 143.

²⁵ *CA rollo*, p. 117.

²⁶ Id. at 201.

²⁷ *Rollo*, p. 49.

²⁸ Villanueva, C., *supra* note 23 at 143-144.

²⁹ Article 1898. If the agent contracts in the name of the principal, exceeding the scope of his authority, and the principal does not ratify the contract, it shall be void if the party with whom the agent contracted is aware of the limits of the powers granted by the principal. In this case, however, the agent is liable if he undertook to secure the principal's ratification.

³⁰ Article 1901. A third person cannot set up the fact that the agent has exceeded his powers, if the principal has ratified, or has signified his willingness to ratify the agent's acts.

third-party knowingly entered into the contract at the time the corporate party did not yet exist to so authorize a representative.”³¹ As discussed, Galang is fully aware that Hao executed the lease contract in preparation for setting up a diagnostic center, which eventually was organized as SUREMED. The company signified its ratification to the lease agreement executed by Hao and Galang when it occupied and operated its business at the leased premises from 2011 until June 2014. Thus, Hao cannot be held personally liable to SUREMED’s obligations under the lease contract.

Anent Hao’s prayer for payment of moral and exemplary damages, We find no basis to grant the same. We find that no bad faith may be attributed to Galang for instituting the unlawful detainer case she was only protecting her interests.

WHEREFORE, the Decision dated May 10, 2019 of the Court of Appeals in CA-G.R. SP No. 157869 is **REVERSED**. Petitioner Eliseo N. Hao, acting only as an agent of Suremed Diagnostic Center Corp., cannot be held liable for rental arrears or any other costs that may arise pursuant to the contract of lease dated February 25, 2011.

SO ORDERED.

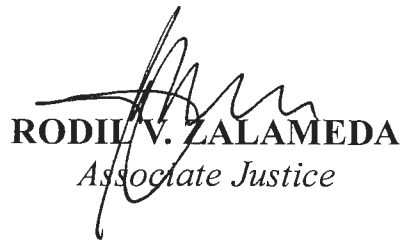

ROS MARI D. CARANDANG
Associate Justice

³¹ Villanueva, C., *supra* note 23 at 144.

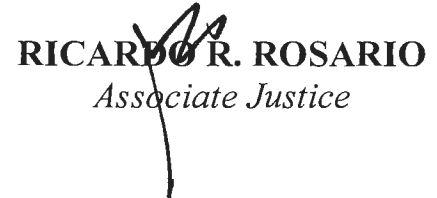
WE CONCUR:



MARVIC MARIO VICTOR F. LEONEN
Associate Justice



RODIL V. ZALAMEDA
Associate Justice



RICARDO R. ROSARIO
Associate Justice



JAPAR B. DIMAAMPAO
Associate Justice

ATTESTATION

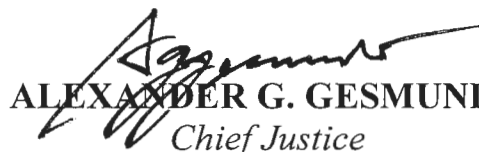
I attest that the conclusions in the above Decision had been reached in consultation before the case was assigned to the writer of the opinion of the Court's Division.



MARVIC MARIO VICTOR F. LEONEN
Associate Justice

CERTIFICATION

Pursuant to Section 13, Article VIII of the Constitution, and the Division Chairperson's Attestation, I certify that the conclusions in the above Decision had been reached in consultation before the case was assigned to the writer of the opinion of the Court's Division.



ALEXANDER G. GESMUNDO
Chief Justice