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FIRST DIVISION

[G.R. No. 124290, January 16, 1998]

ALLIED BANKING CORPORATION, PETITIONER, VS. COURT OF APPEALS, HON. JOSE C. DE GUZMAN, OSCAR D. TANQUECO, LUCIA D. TANQUECO-MATIAS, RUBEN D. TANQUECO AND NESTOR D. TANQUECO, RESPONDENTS

D E C I S I O N

BELLOSILLO, J .:

There are two (2) main issues in this petition for review: namely, (a) whether a stipulation in a contract of lease to the effect that the contract "may be renewed for a like term at the option of the lessee" is void for being potestative or violative of the principle of mutuality of contracts under Art. 1308 of the Civil Code and, corollarily, what is the meaning of the clause "may be renewed for a like term at the option of the lessee;" and, (b) whether a lessee has the legal personality to assail the validity of a deed of donation executed by the lessor over the leased premises.

Spouses Filemon Tanqueco and Lucia Domingo-Tanqueco owned a 512-square meter lot located at No. 2 Sarmiento Street corner Quirino Highway, Novaliches, Quezon City, covered by TCT No. 136779 in their name. On 30 June 1978 they leased the property to petitioner Allied Banking Corporation (ALLIED) for a monthly rental of P1,000.00 for the first three (3) years, adjustable by 25% every three (3) years thereafter.[1] The lease contract specifically states in its Provision No. 1 that "the term of this lease shall be fourteen (14) years commencing from April 1, 1978 and may be renewed for a like term at the option of the lessee."

Pursuant to their lease agreement, ALLIED introduced an improvement on the property consisting of a concrete building with a floor area of 340-square meters which it used as a branch office. As stipulated, the ownership of the building would be transferred to the lessors upon the expiration of the original term of the lease.

Sometime in February 1988 the Tanqueco spouses executed a deed of donation over the subject property in favor of their four (4) children, namely, private respondents herein Oscar D. Tanqueco, Lucia Tanqueco-Matias, Ruben D. Tanqueco and Nestor D. Tanqueco, who accepted the donation in the same public instrument.

On 13 February 1991, a year before the expiration of the contract of lease, the Tanquecos notified petitioner ALLIED that they were no longer interested in renewing the lease.[2] ALLIED replied that it was exercising its option to renew their lease under the same terms with additional proposals.[3] Respondent Ruben D. Tanqueco, acting in behalf of all the donee-lessors, made a counter-proposal.[4] ALLIED however rejected the counter-proposal and insisted on Provision No. 1 of their lease contract.

When the lease contract expired in 1992 private respondents demanded that ALLIED vacate the premises. But the latter asserted its sole option to renew the lease and enclosed in its reply letter a cashier's check in the amount of P68,400.00 representing the advance rental payments for six (6) months taking into account the escalation clause. Private respondents however returned the check to ALLIED, prompting the latter to consign the amount in court.

An action for ejectment was commenced before the Metropolitan Trial Court of Quezon City. After trial, the MeTC-Br. 33 declared Provision No. 1 of the lease contract void for being violative of Art. 1308 of the Civil Code thus -

> x x x but such provision [in the lease contract], to the mind of the Court, does not add luster to defendant's cause nor constitutes as an unbridled or unlimited license or sanctuary of the defendant to perpetuate its occupancy on the subject property. The basic intention of the law in any contract is mutuality and equality. In other words, the validity of a contract cannot be left at (sic) the will of one of the contracting parties. Otherwise, it infringes (upon) Article 1308 of the New Civil Code, which provides: *The contract must bind both contracting parties; its validity or compliance cannot be left to the will of one of them x x x x* Using the principle laid down in the case of Garcia v. Legarda as cornerstone, it is evident that the renewal of the lease in this case cannot be left at the sole option or will of the defendant notwithstanding provision no. 1 of their expired contract. For that would amount to a situation where the continuance and effectivity of a contract will depend only upon the sole will or power of the lessee, which is repugnant to the very spirit envisioned under Article 1308 of the New Civil Code x x x x the theory adopted by this Court in the case at bar finds ample affirmation from the principle echoed by the Supreme Court in the case of *Lao Lim v. CA,* 191 SCRA 150, 154, 155.

On appeal to the Regional Trial Court, and later to the Court of Appeals, the assailed decision was affirmed.[5]

On 20 February 1993, while the case was pending in the Court of Appeals, ALLIED vacated the leased premises by reason of the controversy.[6]

ALLIED insists before us that Provision No. 1 of the lease contract was mutually agreed upon hence valid and binding on both parties, and the exercise by petitioner of its option to renew the contract was part of their agreement and in pursuance thereof.

We agree with petitioner. Article 1308 of the Civil Code expresses what is known in law as the *principle of mutuality of contracts.* It provides that "the contract must bind both the contracting parties; its validity or compliance cannot be left to the will of one of them." This binding effect of a contract on both parties is based on the principle that the obligations arising from contracts have the force of law between the contracting parties, and there must be mutuality between them based essentially on their equality under which it is repugnant to have one party bound by the contract while leaving the other free therefrom. The ultimate purpose is to render void a contract containing a condition which makes its fulfillment dependent solely upon the uncontrolled will of one of the contracting parties.

An express agreement which gives the lessee the sole option to renew the lease is frequent and subject to statutory restrictions, valid and binding on the parties. This option, which is provided in the same lease agreement, is fundamentally part of the consideration in the contract and is no different from any other provision of the lease carrying an undertaking on the part of the lessor to act conditioned on the performance by the lessee. It is a purely executory contract and at most confers a right to obtain a renewal if there is compliance with the conditions on which the right is made to depend. The right of renewal constitutes a part of the lessee's interest in the land and forms a substantial and integral part of the agreement.

The fact that such option is binding only on the lessor and can be exercised only by the lessee does not render it void for lack of mutuality. After all, the lessor is free to give or not to give the option to the lessee. And while the lessee has a right to elect whether to continue with the lease or not, once he exercises his option to continue and the lessor accepts, both parties are thereafter bound by the new lease agreement. Their rights and obligations become mutually fixed, and the lessee is entitled to retain possession of the property for the duration of the new lease, and the lessor may hold him liable for the rent therefor. The lessee cannot thereafter escape liability even if he should subsequently decide to abandon the premises. Mutuality obtains in such a contract and equality exists between the lessor and the lessee since they remain with the same faculties in respect to fulfillment.[7]

The case of *Lao Lim v. Court of Appeals*[8] relied upon by the trial court is not applicable here. In that case, the stipulation in the disputed compromise agreement was to the effect that the lessee would be allowed to stay in the premises "as long as he needs it and can pay the rents." In the present case, the questioned provision states that the lease "may be renewed for a like term at the option of the lessee." The lessor is bound by the option he has conceded to the lessee. The lessee likewise becomes bound only when he exercises his option and the lessor cannot thereafter be excused from performing his part of the agreement.

Likewise, reliance by the trial court on the 1967 case of *Garcia v. Rita Legarda, Inc.*, [9] is misplaced. In that case, what was involved was a contract to sell involving residential lots, which gave the vendor the right to declare the contract cancelled and of no effect upon the failure of the vendee to fulfill any of the conditions therein set forth. In the instant case, we are dealing with a contract of lease which gives the lessee the right to renew the same.

With respect to the meaning of the clause "may be renewed for a like term at the option of the lessee," we sustain petitioner's contention that its exercise of the option resulted in the automatic extension of the contract of lease under the same terms and conditions. The subject contract simply provides that "the term of this lease shall be fourteen (14) years and may be renewed for a like term at the option of the lessee." As we see it, the only term on which there has been a clear agreement is the period of the new contract, i.e., fourteen (14) years, which is evident from the clause "may be renewed for a like term at the option of the lessee," the phrase "*for a like term*" referring to the period. It is silent as to what the specific terms and conditions of the renewed lease shall be. Shall it be the same terms and conditions as in the original contract, or shall it be under the terms and conditions as may be mutually agreed upon by the parties after the expiration of the