

**ROSENCOR DEVELOPMENT CORPORATION AND RENE JOAQUIN,
PETITIONERS, VS. PATERNO INQUING, IRENE GUILLERMO,
FEDERICO BANTUGAN, FERNANDO MAGBANUA AND LIZZA
TIANGCO, RESPONDENTS.**

G.R. No. 140479. March 08, 2001

Ponente: GONZAGA-REYES, J.

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GONZAGA-REYES, J.:

This is a petition for review on certiorari under Rule 45 of the Rules of Court seeking reversal of the Decision^[1] of the Court of Appeals dated June 25, 1999 in CA-G.R. CV No. 53963. The Court of Appeals decision reversed and set aside the Decision^[2] dated May 13, 1996 of Branch 217 of the Regional Trial Court of Quezon City in Civil Case No. Q-93-18582.

The case was originally filed on December 10, 1993 by Paterno Inquing, Irene Guillermo and Federico Bantugan, herein respondents, against Rosencor Development Corporation (hereinafter "Rosencor"), Rene Joaquin, and Eufrocina de Leon. Originally, the complaint was one for annulment of absolute deed of sale but was later amended to one for rescission of absolute deed of sale. A complaint-for intervention was thereafter filed by respondents Fernando Magbanua and Danna Lizza Tiangco. The complaint-in-intervention was admitted by the trial court in an Order dated May 4, 1994.^[3]

The facts of the case, as stated by the trial court and adopted by the appellate court, are as follows:

"This action was originally for the annulment of the Deed of Absolute Sale dated September 4, 1990 between defendants Rosencor and Eufrocina de Leon but later amended (sic) praying for the rescission of the deed of sale.

Plaintiffs and plaintiffs-intervenors averred that they are the lessees since 1971 of a two-story residential apartment located at No. 150 Tomas Morato Ave., Quezon City covered by TCT No. 96161 and owned by spouses Faustino and Cresencia Tiangco. The lease was not covered by any contract. The lessees were renting the premises then for P150.00 a month and were allegedly verbally granted by the lessors the pre-emptive right to purchase the property if ever they decide to sell the same.

Upon the death of the spouses Tiangcos in 1975, the management of the property was adjudicated to their heirs who were represented by Eufrocina de Leon. The lessees were allegedly promised the same pre-emptive right by the heirs of Tiangcos since the latter had knowledge that this right was extended to the former by the late spouses Tiangcos. The lessees continued to stay in the premises and allegedly spent their own money amounting from P50,000.00 to P100,000.00 for its upkeep. These expenses were never deducted from the rentals which already increased to P1,000.00.

In June 1990, the lessees received a letter from Atty. Erlinda Aguila demanding that they vacate the premises so that the demolition of the building be undertaken. They refused to leave the premises. In that same month, de Leon refused to accept the lessees' rental payment claiming that they have run out of receipts and that a new

collector has been assigned to receive the payments. Thereafter, they received a letter from Eufrocina de Leon offering to sell to them the property they were leasing for P2,000,000.00. xxx.

The lessees offered to buy the property from de Leon for the amount of P1,000,000.00. De Leon told them that she will be submitting the offer to the other heirs. Since then, no answer was given by de Leon as to their offer to buy the property. However, in November 1990, Rene Joaquin came to the leased premises introducing himself as its new owner.

In January 1991, the lessees again received another letter from Atty. Aguila demanding that they vacate the premises. A month thereafter, the lessees received a letter from de Leon advising them that the heirs of the late spouses Tiangcos have already sold the property to Rosencor. The following month Atty. Aguila wrote them another letter demanding the rental payment and introducing herself as counsel for Rosencor/Rene Joaquin, the new owners of the premises.

The lessees requested from de Leon why she had disregarded the pre-emptive right she and the late Tiangcos have promised them. They also asked for a copy of the deed of sale between her and the new owners thereof but she refused to heed their request. In the same manner, when they asked Rene Joaquin a copy of the deed of sale, the latter turned down their request and instead Atty. Aguila wrote them several letters demanding that they vacate the premises. The lessees offered to tender their rental payment to de Leon but she refused to accept the same.

In April 1992 before the demolition can be undertaken by the Buiding Official, the barangay interceded between the parties herein after which Rosencor raised the issue as to the rental payment of the premises. It was also at this instance that the lessees were furnished with a copy of the Deed of Sale and discovered that they were deceived by de Leon since the sale between her and Rene Joaquin/Rosencor took place in September 4, 1990 while de Leon made the offer to them only in October 1990 or after the sale with Rosencor had been consummated. The lessees also noted that the property was sold only for P726,000.00.

The lessees offered to reimburse de Leon the selling price of P726,000.00 plus an additional P274,000.00 to complete their P1,000,000.00 earlier offer. When their offer was refused, they filed the present action praying for the following: a) rescission of the Deed of Absolute Sale between de Leon and Rosencor dated September 4, 1990; b) the defendants Rosencor/Rene Joaquin be ordered to reconvey the property to de Leon; and c) de Leon be ordered to reimburse the plaintiffs for the repairs of the property, or apply the said amount as part of the price for the purchase of the property in the sum of P100,000.00."[4]

After trial on the merits, the Regional Trial Court rendered a Decision[5] dated May 13, 1996 dismissing the complaint. The trial court held that the right of redemption on which the complaint was based was merely an oral one and as such, is unenforceable under the law. The dispositive portion of the May 13, 1996 Decision is as follows:

"WHEREFORE, in view of the foregoing, the Court DISMISSES the instant action. Plaintiffs and plaintiffs-intervenors are hereby ordered to pay their respective monthly rental of P1,000.00 per month reckoned from May 1990 up to the time they leave the premises. No costs.

SO ORDERED."[6]

Not satisfied with the decision of the trial court, respondents herein filed a Notice of Appeal dated June 3, 1996. On the same date, the trial court issued an Order for the elevation of the records of the case to the Court of Appeals. On August 8, 1997, respondents filed their appellate brief before the Court of Appeals.

On June 25, 1999, the Court of Appeals rendered its decision[7] reversing the decision of the trial court. The dispositive portion of the June 25, 1999 decision is as follows:

"WHEREFORE, premises considered, the appealed decision (dated May 13, 1996) of the Regional Trial Court (Branch 217) in Quezon City in Case No. Q-93-18582 is hereby REVERSED and SET ASIDE. In its stead, a new one is rendered ordering:

(1)

The rescission of the Deed of Absolute Sale executed between the appellees on September 4, 1990;

(2)

The reconveyance of the subject premises to appellee Eufrocina de Leon;

(3)

The heirs of Faustino and Crescencia Tiangco, thru appellee Eufrocina de Leon, to afford the appellants thirty days within which to exercise their right of first refusal by paying the amount of ONE MILLION PESOS (P1,000,000.00) for the subject property; and

(4)

The appellants to, in turn, pay the appellees back rentals from May 1990 up to the time this decision is promulgated.

No pronouncement as to costs.

SO ORDERED."[8]

Petitioners herein filed a Motion for Reconsideration of the decision of the Court of Appeals but the same was denied in a Resolution dated October 15, 1999.[9]

Hence, this petition for review on certiorari where petitioners Rosencor Development Corporation and Rene Joaquin raise the following assignment of errors[10]:

I.

THE COURT OF APPEALS GRAVELY ERRED WHEN IT ORDERED THE RESCISSION OF THE ABSOLUTE DEED OF SALE BETWEEN EUFROCINA DE LEON AND PETITIONER ROSENCOR.

II.

THE COURT OF APPEALS COMMITTED MANIFEST ERROR IN MANDATING THAT EUFROCINA DE LEON AFFORD RESPONDENTS THE OPPORTUNITY TO EXERCISE THEIR RIGHT OF FIRST REFUSAL.

III.

THE COURT OF APPEALS GRIEVOUSLY ERRED IN CONCLUDING THAT RESPONDENTS HAVE ESTABLISHED THEIR RIGHT OF FIRST REFUSAL DESPITE PETITIONERS' RELIANCE ON THEIR DEFENSE BASED ON THE STATUTE OF FRAUDS.

Eufrocina de Leon, for herself and for the heirs of the spouses Faustino and Crescencia Tiangco, did not appeal the decision of the Court of Appeals.

At the onset, we note that both the Court of Appeals and the Regional Trial Court relied on Article 1403 of the New Civil Code, more specifically the provisions on the statute of frauds, in coming out with their respective decisions. The trial court, in denying the petition for reconveyance, held that right of first refusal relied upon by petitioners was not reduced to writing and as such, is unenforceable by virtue of the said article. The Court of Appeals, on the other hand, also held that the statute of frauds governs the "right of first refusal" claimed by

respondents. However, the appellate court ruled that respondents had duly proven the same by reason of petitioners' waiver of the protection of the statute by reason of their failure to object to the presentation of oral evidence of the said right.

Both the appellate court and the trial court failed to discuss, however, the threshold issue of whether or not a right of first refusal is indeed covered by the provisions of the New Civil Code on the statute of frauds. The resolution of the issue on the applicability of the statute of frauds is important as it will determine the type of evidence which may be considered by the trial court as proof of the alleged right of first refusal.

The term "statute of frauds" is descriptive of statutes which require certain classes of contracts to be in writing. This statute does not deprive the parties of the right to contract with respect to the matters therein involved, but merely regulates the formalities of the contract necessary to render it enforceable. Thus, they are included in the provisions of the New Civil Code regarding unenforceable contracts, more particularly Art. 1403, paragraph 2. Said article provides, as follows:

"Art. 1403. The following contracts are unenforceable, unless they are ratified:

x x x

(2) Those that do not comply with the Statute of Frauds as set forth in this number. In the following cases an agreement hereafter made shall be unenforceable by action, unless the same, or some note or memorandum thereof, be in writing, and subscribed by the party charged, or by his agent; evidence, therefore, of the agreement cannot be received without the writing, or a secondary evidence of its contents:

a) An agreement that by its terms is not to be performed within a year from the making thereof;

b) A special promise to answer for the debt, default, or miscarriage of another;

c) An agreement made in consideration of marriage, other than a mutual promise to marry;

d) An agreement for the sale of goods, chattels or things in action, at a price not less than five hundred pesos, unless the buyer accept and receive part of such goods and chattels, or the evidences, or some of them, of such things in action, or pay at the time some part of the purchase money; but when a sale is made by auction and entry is made by the auctioneer in his sales book, at the time of the sale, of the amount and kind of property sold, terms of sale, price, names of purchasers and person on whose account the sale is made, it is a sufficient memorandum;

e) An agreement for the leasing of a longer period than one year, or for the sale of real property or of an interest therein;

f) A representation to the credit of a third person."

The purpose of the statute is to prevent fraud and perjury in the enforcement of obligations depending for their evidence on the unassisted memory of witnesses by requiring certain enumerated contracts and transactions to be evidenced by a writing signed by the party to be charged.[11] Moreover, the statute of frauds refers to specific kinds of transactions and cannot apply to any other transaction that is not enumerated therein.[12] The application of such statute presupposes the existence of a perfected contract.[13]

The question now is whether a "right of first refusal" is among those enumerated in the list of contracts covered by the Statute of Frauds. More specifically, is a right of first refusal akin to "an agreement for the leasing of a longer period than one year, or for the sale of real property or of an interest therein" as contemplated by Article 1403, par. 2(e) of the New Civil Code.

We have previously held that not all agreements "affecting land" must be put into writing to attain

enforceability[14]. Thus, we have held that the setting up of boundaries,[15] the oral partition of real property[16], and an agreement creating a right of way[17] are not covered by the provisions of the statute of frauds. The reason simply is that these agreements are not among those enumerated in Article 1403 of the New Civil Code.

A right of first refusal is not among those listed as unenforceable under the statute of frauds. Furthermore, the application of Article 1403, par. 2(e) of the New Civil Code presupposes the existence of a perfected, albeit unwritten, contract of sale.[18] A right of first refusal, such as the one involved in the instant case, is not by any means a perfected contract of sale of real property. At best, it is a contractual grant, not of the sale of the real property involved, but of the right of first refusal over the property sought to be sold[19]

It is thus evident that the statute of frauds does not contemplate cases involving a right of first refusal. As such, a right of first refusal need not be written to be enforceable and may be proven by oral evidence.

The next question to be ascertained is whether or not respondents have satisfactorily proven their right of first refusal over the property subject of the Deed of Absolute Sale dated September 4, 1990 between petitioner Rosencor and Eufrocina de Leon.

On this point, we agree with the factual findings of the Court of Appeals that respondents have adequately proven the existence of their right of first refusal. Federico Bantugan, Irene Guillermo, and Paterno Inquing uniformly testified that they were promised by the late spouses Faustino and Crescencia Tiangco and, later on, by their heirs a right of first refusal over the property they were currently leasing should they decide to sell the same. Moreover, respondents presented a letter[20] dated October 9, 1990 where Eufrocina de Leon, the representative of the heirs of the spouses Tiangco, informed them that they had received an offer to buy the disputed property for P2,000,000.00 and offered to sell the same to the respondents at the same price if they were interested. Verily, if Eufrocina de Leon did not recognize respondents' right of first refusal over the property they were leasing, then she would not have bothered to offer the property for sale to the respondents.

It must be noted that petitioners did not present evidence before the trial court contradicting the existence of the right of first refusal of respondents over the disputed property. They only presented petitioner Rene Joaquin, the vice-president of petitioner Rosencor, who admitted having no personal knowledge of the details of the sales transaction between Rosencor and the heirs of the spouses Tiangco[21] They also dispensed with the testimony of Eufrocina de Leon[22] who could have denied the existence or knowledge of the right of first refusal. As such, there being no evidence to the contrary, the right of first refusal claimed by respondents was substantially proven by respondents before the lower court.

Having ruled upon the question as to the existence of respondents' right of first refusal, the next issue to be answered is whether or not the Court of Appeals erred in ordering the rescission of the Deed of Absolute Sale dated September 4, 1990 between Rosencor and Eufrocina de Leon and in decreeing that the heirs of the spouses Tiangco should afford respondents the exercise of their right of first refusal. In other words, may a contract of sale entered into in violation of a third party's right of first refusal be rescinded in order that such third party can exercise said right?

The issue is not one of first impression.

In *Guzman, Bocaling and Co, Inc. vs. Bonnevie*[23], the Court upheld the decision of a lower court ordering the rescission of a deed of sale which violated a right of first refusal granted to one of the parties therein. The Court held:

"xxx Contract of Sale was not voidable but rescissible. Under Article 1380 to 1381 (3) of the Civil Code, a contract otherwise valid may nonetheless be subsequently rescinded by reason of injury to third persons, like

creditors. The status of creditors could be validly accorded the Bonnevie for they had substantial interests that were prejudiced by the sale of the subject property to the petitioner without recognizing their right of first priority under the Contract of Lease.

According to Tolentino, rescission is a remedy granted by law to the contracting parties and even to third persons, to secure reparations for damages caused to them by a contract, even if this should be valid, by means of the restoration of things to their condition at the moment prior to the celebration of said contract. It is a relief allowed for the protection of one of the contracting parties and even third persons from all injury and damage the contract may cause, or to protect some incompatible and preferent right created by the contract. Rescission implies a contract which, even if initially valid, produces a lesion or pecuniary damage to someone that justifies its invalidation for reasons of equity.

It is true that the acquisition by a third person of the property subject of the contract is an obstacle to the action for its rescission where it is shown that such third person is in lawful possession of the subject of the contract and that he did not act in bad faith. However, this rule is not applicable in the case before us because the petitioner is not considered a third party in relation to the Contract of Sale nor may its possession of the subject property be regarded as acquired lawfully and in good faith.

Indeed, Guzman, Bocaling and Co. was the vendee in the Contract of Sale. Moreover, the petitioner cannot be deemed a purchaser in good faith for the record shows that it categorically admitted that it was aware of the lease in favor of the Bonnevie, who were actually occupying the subject property at the time it was sold to it. Although the Contract of Lease was not annotated on the transfer certificate of title in the name of the late Jose Reynoso and Africa Reynoso, the petitioner cannot deny actual knowledge of such lease which was equivalent to and indeed more binding than presumed notice by registration.

A purchaser in good faith and for value is one who buys the property of another without notice that some other person has a right to or interest in such property without and pays a full and fair price for the same at the time of such purchase or before he has notice of the claim or interest of some other person in the property. Good faith connotes an honest intention to abstain from taking unconscientious advantage of another. Tested by these principles, the petitioner cannot tenably claim to be a buyer in good faith as it had notice of the lease of the property by the Bonnevie and such knowledge should have cautioned it to look deeper into the agreement to determine if it involved stipulations that would prejudice its own interests."

Subsequently^[24] in *Equatorial Realty and Development, Inc. vs. Mayfair Theater, Inc.*^[25], the Court, en banc, with three justices dissenting,^[26] ordered the rescission of a contract entered into in violation of a right of first refusal. Using the ruling in *Guzman Bocaling & Co., Inc. vs. Bonnevie* as basis, the Court decreed that since respondent therein had a right of first refusal over the said property, it could only exercise the said right if the fraudulent sale is first set aside or rescinded. Thus:

"What Carmelo and Mayfair agreed to, by executing the two lease contracts, was that Mayfair will have the right of first refusal in the event Carmelo sells the leased premises. It is undisputed that Carmelo did recognize this right of Mayfair, for it informed the latter of its intention to sell the said property in 1974. There was an exchange of letters evidencing the offer and counter-offers made by both parties. Carmelo, however, did not pursue the exercise to its logical end. While it initially recognized Mayfair's right of first refusal, Carmelo violated such right when without affording its negotiations with Mayfair the full process to ripen to at least an interface of a definite offer and a possible corresponding acceptance within the "30-day exclusive option" time granted Mayfair, Carmelo abandoned negotiations, kept a low profile for some time, and then sold, without prior notice to Mayfair, the entire Claro M. Recto property to Equatorial.

Since Equatorial is a buyer in bad faith, this finding renders the sale to it of the property in question, rescissible. We agree with respondent Appellate Court that the records bear out the fact that Equatorial was aware of the lease contracts because its lawyers had, prior to the sale, studied the said contracts. As such,

Equatorial cannot tenably claim that to be a purchaser in good faith, and, therefore, rescission lies.

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As also earlier emphasized, the contract of sale between Equatorial and Carmelo is characterized by bad faith, since it was knowingly entered into in violation of the rights of and to the prejudice of Mayfair. In fact, as correctly observed by the Court of Appeals, Equatorial admitted that its lawyers had studied the contract of lease prior to the sale. Equatorial's knowledge of the stipulations therein should have cautioned it to look further into the agreement to determine if it involved stipulations that would prejudice its own interests.

Since Mayfair had a right of first refusal, it can exercise the right only if the fraudulent sale is first set aside or rescinded. All of these matters are now before us and so there should be no piecemeal determination of this case and leave festering sores to deteriorate into endless litigation. The facts of the case and considerations of justice and equity require that we order rescission here and now. Rescission is a relief allowed for the protection of one of the contracting parties and even third persons from all injury and damage the contract may cause or to protect some incompatible and preferred right by the contract. The sale of the subject real property should now be rescinded considering that Mayfair, which had substantial interest over the subject property, was prejudiced by the sale of the subject property to Equatorial without Carmelo conferring to Mayfair every opportunity to negotiate within the 30-day stipulate period."^[27]

In *Paranaque Kings Enterprises, Inc. vs. Court of Appeals*,^[28] the Court held that the allegations in a complaint showing violation of a contractual right of "first option or priority to buy the properties subject of the lease" constitute a valid cause of action enforceable by an action for specific performance. Summarizing the rulings in the two previously cited cases, the Court affirmed the nature of and concomitant rights and obligations of parties under a right of first refusal. Thus:

"We hold however, that in order to have full compliance with the contractual right granting petitioner the first option to purchase, the sale of the properties for the amount of P9,000,000.00, the price for which they were finally sold to respondent Raymundo, should have likewise been offered to petitioner.

The Court has made an extensive and lengthy discourse on the concept of, and obligations under, a right of first refusal in the case of *Guzman, Bocaling & Co. vs. Bonnevie*. In that case, under a contract of lease, the lessees (Raul and Christopher Bonnevie) were given a "right of first priority" to purchase the leased property in case the lessor (Reynoso) decided to sell. The selling price quoted to the Bonnevies was 600,000.00 to be fully paid in cash, less a mortgage lien of P100,000.00. On the other hand, the selling price offered by Reynoso to and accepted by Guzman was only P400,000.00 of which P137,500.00 was to be paid in cash while the balance was to be paid only when the property was cleared of occupants. We held that even if the Bonnevies could not buy it at the price quoted (P600,000.00), nonetheless, Reynoso could not sell it to another for a lower price and under more favorable terms and conditions without first offering said favorable terms and price to the Bonnevies as well. Only if the Bonnevies failed to exercise their right of first priority could Reynoso thereafter lawfully sell the subject property to others, and only under the same terms and conditions previously offered to the Bonnevies.

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This principle was reiterated in the very recent case of *Equatorial Realty vs. Mayfair Theater, Inc.* which was decided en banc. This Court upheld the right of first refusal of the lessee Mayfair, and rescinded the sale of the property by the lessor Carmelo to Equatorial Realty "considering that Mayfair, which had substantial interest over the subject property, was prejudiced by its sale to Equatorial without Carmelo conferring to Mayfair every opportunity to negotiate within the 30-day stipulated period"

In that case, two contracts of lease between Carmelo and Mayfair provided "that if the LESSOR should desire to sell the leased premises, the LESSEE shall be given 30 days exclusive option to purchase the same."

Carmelo initially offered to sell the leased property to Mayfair for six to seven million pesos. Mayfair indicated interest in purchasing the property though it invoked the 30-day period. Nothing was heard thereafter from Carmelo. Four years later, the latter sold its entire Recto Avenue property, including the leased premises, to Equatorial for P11,300,000.00 without priorly informing Mayfair. The Court held that both Carmelo and Equatorial acted in bad faith: Carmelo for knowingly violating the right of first option of Mayfair, and Equatorial for purchasing the property despite being aware of the contract stipulation. In addition to rescission of the contract of sale, the Court ordered Carmelo to allow Mayfair to buy the subject property at the same price of P11,300,000.00.

In the recent case of *Litonjua vs. L&R Corporation*,^[29] the Court, also citing the case of *Guzman, Bocaling & Co. vs. Bonnevie*, held that the sale made therein in violation of a right of first refusal embodied in a mortgage contract, was rescissible. Thus:

"While petitioners question the validity of paragraph 8 of their mortgage contract, they appear to be silent insofar as paragraph 9 thereof is concerned. Said paragraph 9 grants upon L&R Corporation the right of first refusal over the mortgaged property in the event the mortgagor decides to sell the same. We see nothing wrong in this provision. The right of first refusal has long been recognized as valid in our jurisdiction. The consideration for the loan mortgage includes the consideration for the right of first refusal. L&R Corporation is in effect stating that it consents to lend out money to the spouses Litonjua provided that in case they decide to sell the property mortgaged to it, then L&R Corporation shall be given the right to match the offered purchase price and to buy the property at that price. Thus, while the spouses Litonjua had every right to sell their mortgaged property to PWHAS without securing the prior written consent of L&R Corporation, they had the obligation under paragraph 9, which is a perfectly valid provision, to notify the latter of their intention to sell the property and give it priority over other buyers. It is only upon the failure of L&R Corporation to exercise its right of first refusal could the spouses Litonjua validly sell the subject properties to the others, under the same terms and conditions offered to L&R Corporation.

What then is the status of the sale made to PWHAS in violation of L & R Corporation's contractual right of first refusal? On this score, we agree with the Amended Decision of the Court of Appeals that the sale made to PWHAS is rescissible. The case of *Guzman, Bocaling & Co. v. Bonnevie* is instructive on this point.

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It was then held that the Contract of Sale there, which violated the right of first refusal, was rescissible.

In the case at bar, PWHAS cannot claim ignorance of the right of first refusal granted to L & R Corporation over the subject properties since the Deed of Real Estate Mortgage containing such a provision was duly registered with the Register of Deeds. As such, PWHAS is presumed to have been notified thereof by registration, which equates to notice to the whole world.

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All things considered, what then are the relative rights and obligations of the parties? To recapitulate: the sale between the spouses Litonjua and PWHAS is valid, notwithstanding the absence of L & R Corporation's prior written consent thereto. Inasmuch as the sale to PWHAS was valid, its offer to redeem and its tender of the redemption price, as successor-in-interest of the spouses Litonjua, within the one-year period should have been accepted as valid by the L & R Corporation. However, while the sale is, indeed, valid, the same is rescissible because it ignored L & R Corporation's right of first refusal."

Thus, the prevailing doctrine, as enunciated in the cited cases, is that a contract of sale entered into in violation of a right of first refusal of another person, while valid, is rescissible.

There is, however, a circumstance which prevents the application of this doctrine in the case at bench. In the cases

cited above, the Court ordered the rescission of sales made in violation of a right of first refusal precisely because the vendees therein could not have acted in good faith as they were aware or should have been aware of the right of first refusal granted to another person by the vendors therein. The rationale for this is found in the provisions of the New Civil Code on rescissible contracts. Under Article 1381 of the New Civil Code, paragraph 3, a contract validly agreed upon may be rescinded if it is "undertaken in fraud of creditors when the latter cannot in any manner collect the claim due them." Moreover, under Article 1385, rescission shall not take place "when the things which are the object of the contract are legally in the possession of third persons who did not act in bad faith." [30]

It must be borne in mind that, unlike the cases cited above, the right of first refusal involved in the instant case was an oral one given to respondents by the deceased spouses Tiangco and subsequently recognized by their heirs. As such, in order to hold that petitioners were in bad faith, there must be clear and convincing proof that petitioners were made aware of the said right of first refusal either by the respondents or by the heirs of the spouses Tiangco.

It is axiomatic that good faith is always presumed unless contrary evidence is adduced. [31] A purchaser in good faith is one who buys the property of another without notice that some other person has a right or interest in such a property and pays a full and fair price at the time of the purchase or before he has notice of the claim or interest of some other person in the property. [32] In this regard, the rule on constructive notice would be inapplicable as it is undisputed that the right of first refusal was an oral one and that the same was never reduced to writing, much less registered with the Registry of Deeds. In fact, even the lease contract by which respondents derive their right to possess the property involved was an oral one.

On this point, we hold that the evidence on record fails to show that petitioners acted in bad faith in entering into the deed of sale over the disputed property with the heirs of the spouses Tiangco. Respondents failed to present any evidence that prior to the sale of the property on September 4, 1990, petitioners were aware or had notice of the oral right of first refusal.

Respondents point to the letter dated June 1, 1990 [33] as indicative of petitioners' knowledge of the said right. In this letter, a certain Atty. Erlinda Aguila demanded that respondent Irene Guillermo vacate the structure they were occupying to make way for its demolition.

We fail to see how the letter could give rise to bad faith on the part of the petitioner. No mention is made of the right of first refusal granted to respondents. The name of petitioner Rosencor or any of its officers did not appear on the letter and the letter did not state that Atty. Aguila was writing in behalf of petitioner. In fact, Atty. Aguila stated during trial that she wrote the letter in behalf of the heirs of the spouses Tiangco. Moreover, even assuming that Atty. Aguila was indeed writing in behalf of petitioner Rosencor, there is no showing that Rosencor was aware at that time that such a right of first refusal existed.

Neither was there any showing that after receipt of this June 1, 1990 letter, respondents notified Rosencor or Atty. Aguila of their right of first refusal over the property. Respondents did not try to communicate with Atty. Aguila and inform her about their preferential right over the disputed property. There is even no showing that they contacted the heirs of the spouses Tiangco after they received this letter to remind them of their right over the property.

Respondents likewise point to the letter dated October 9, 1990 of Eufrocina de Leon, where she recognized the right of first refusal of respondents, as indicative of the bad faith of petitioners. We do not agree. Eufrocina de Leon wrote the letter on her own behalf and not on behalf of petitioners and, as such, it only shows that Eufrocina de Leon was aware of the existence of the oral right of first refusal. It does not show that petitioners were likewise

aware of the existence of the said right. Moreover, the letter was made a month after the execution of the Deed of Absolute Sale on September 4, 1990 between petitioner Rosencor and the heirs of the spouses Tiangco. There is no showing that prior to the date of the execution of the said Deed, petitioners were put on notice of the existence of the right of first refusal.

Clearly, if there was any indication of bad faith based on respondents' evidence, it would only be on the part of Eufrocina de Leon as she was aware of the right of first refusal of respondents yet she still sold the disputed property to Rosencor. However, bad faith on the part of Eufrocina de Leon does not mean that petitioner Rosencor likewise acted in bad faith. There is no showing that prior to the execution of the Deed of Absolute Sale, petitioners were made aware or put on notice of the existence of the oral right of first refusal. Thus, absent clear and convincing evidence to the contrary, petitioner Rosencor will be presumed to have acted in good faith in entering into the Deed of Absolute Sale over the disputed property.

Considering that there is no showing of bad faith on the part of the petitioners, the Court of Appeals thus erred in ordering the rescission of the Deed of Absolute Sale dated September 4, 1990 between petitioner Rosencor and the heirs of the spouses Tiangco. The acquisition by Rosencor of the property subject of the right of first refusal is an obstacle to the action for its rescission where, as in this case, it was shown that Rosencor is in lawful possession of the subject of the contract and that it did not act in bad faith.[34]

This does not mean however that respondents are left without any remedy for the unjustified violation of their right of first refusal. Their remedy however is not an action for the rescission of the Deed of Absolute Sale but an action for damages against the heirs of the spouses Tiangco for the unjustified disregard of their right of first refusal[35].

WHEREFORE, premises considered, the decision of the Court of Appeals dated June 25, 1999 is REVERSED and SET ASIDE. The Decision dated May 13, 1996 of the Quezon City Regional Trial Court, Branch 217 is hereby REINSTATED insofar as it dismisses the action for rescission of the Deed of Absolute Sale dated September 4, 1990 and orders the payment of monthly rentals of P1,000.00 per month reckoned from May 1990 up to the time respondents leave the premises.

SO ORDERED.

Melo, (Chairman), Panganiban, and Sandoval-Gutierrez, JJ., concur.

Vitug, J., in the result; reiterated the Court's opinion in *Ang Yu vs. CA* (238 SCRA 602).

[1] Penned by Associate Justice Ramon Mabutas, Jr. and concurred in by Associate Justices Hilarion L. Aquino and Wenceslao I. Agnir, Jr.

[2] Penned by Judge Gil P. Fernandez, Sr.

[3] RTC Records, p. 80.

[4] Rollo, pp. 37-39.

[5] Annex "F" of Petition; Rollo, pp. 73-77.

[6] Rollo, p. 77.

[7] Annex "A" of Petition; Rollo, pp. 36-49.

[8] Rollo, pp. 48-49.

- [9] Annex "B" of Petition; Rollo, pp. 50-51.
- [10] Rollo, p. 17.
- [11] Asia Production Co., Inc., et al vs. Pano, et al, 205 SCRA 458.
- [12] Western Mindanao Lumber Co. vs. Medalla, 79 SCRA 708; Cruz vs. J.M. Tuazon, 76 SCRA 543.
- [13] Villanueva vs. Court of Appeals, 267 SCRA 89.
- [14] Victorino Hernandez vs. Court of Appeals, 160 SCRA 321.
- [15] Ibid.
- [16] Simprosa Vda. De Espina vs. Abaya, 196 SCRA 312.
- [17] Western Mindanao Lumber Co. vs. Medalla, supra.
- [18] Villanueva vs. Court of Appeals, supra.
- [19] Equatorial Realty Development, Inc. vs. Mayfair Theater, Inc., 264 SCRA 483.
- [20] Exhibit "B"; RTC Records, p. 177.
- [21] T.S.N., October 05, 1995, p. 33.
- [22] RTC Records, p. 199.

[23] 206 SCRA 668.

[24] Previous to this case, the Court en banc promulgated the case of Ang Yu Asuncion vs. Court of Appeals, 238 SCRA 602. In this case, the Court refused to rescind a contract of sale which violated the right of first refusal of petitioner therein. The Court characterized a right of first refusal as belonging to a class of preparatory juridical relations governed not by contracts but by, among other laws of general application, the pertinent scattered provisions of the Civil Code on human conduct. The Court held that the breach of the right of first refusal granted to a party cannot justify the issuance of a writ of execution, nor would it sanction an action for specific performance as the indispensable element of consensuality in contracts would be negated. As such, the remedy of a person aggrieved by an unjustified disregard of his right of first refusal is not an action for the rescission of the contract but an action for recovery of damages under Article 19 of the Civil Code. On the issue of whether or not the alleged purchaser of the property therein acted in good or bad faith in purchasing the property subject to the right of first refusal, the Court held that the matter should be independently addressed in appropriate proceedings.

[25] 264 SCRA 483.

[26] namely Justices Flerida Ruth P. Romero, Jose C. Vitug and Justo P. Torres.

[27] In their dissent, the three justices concurred with the ruling that the stipulation in the contract involves a right of first refusal. However, they disagreed with the ruling of the Court regarding the rescissible nature of the contract entered into in violation of the said right, citing the case of Ang Yu Asuncion vs, Court of Appeals, supra, as precedent.

[28] 268 SCRA 727.

[29] 320 SCRA 405.

[30] Guzman, Bocaling and Co. vs. Bonnevie, supra, citing Cordovero and Alcazar vs. Villaruz and Borromeo, 46 Phil. 473.

[31] Heirs of Severa P. Gregorio vs. Court of Appeals, 300 SCRA 565.

[32] Co vs. Court of Appeals, 196 SCRA 705.

[33] Exhibit "G", RTC Records, p. 181.

[34] Guzman, Bocaling & Co. vs. Bonnevie, supra.

[35] Ang Yu Asuncion vs. Court of Appeals, supra.

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