

Forms of Business Ownership

Tourism and hospitality businesses must decide on the form of business they will deal with to be ready when threatened by legal concerns.

The following are the different forms of business organizations (Maranan et al., 2019):

- **Sole Proprietorship.** The owner is in command of his whole business and stands to lose as much as he puts in and even more to the extent of all his personal holdings. The establishment, operations, and management of this form of business are not governed by a special law. If some legal issues and disputes confront it, the proprietor can use general laws and prevailing civil obligations and contracts in commercial transactions.

The sole proprietor has control over the whole management of the business, hence, has limitless liability. The law does not make any difference between the personal affairs of the proprietor and his business interest. Before the law, they are one and the same; the business an extension of his being.

- **Partnership.** The law on partnership is governed by the Civil Code of the Philippines. Article 1767 states, "*By the contract of partnership two or more persons bind themselves to contribute money, property or industry to a common fund, with the intention of dividing the profits among themselves.*" Two (2) or more persons may also form a partnership for the exercise of a profession. With their separate property, partners (except in limited partnership) are personally liable in proportion to the debts of the partnership (Art. 1813, CC). A **partnership contract** is based on trust and confidence. Hence, the **fiduciary relationship** (relationship in which an individual places complete confidence, trust, and reliance in someone who has a duty to act for the individual's benefit) in a partnership stems from the principle of **delectus personae**; wherein no one can become a partner in a partnership without the consent of all the partners.

Forms of Partnership

Partnerships may be found in any of the following forms:

- *General Partnership.* It is a partnership in which all other partners manage the business and are personally liable for its debts.
- *Limited Partnership.* In this form of partnership, certain limited partners give up their ability to manage the business in exchange for limited liability for the partnership's debts.
- *Limited Liability Partnership.* It is a partnership where all partners have some degree of limited liability.
- **Corporation.** The law on corporation is governed by Republic Act No. 11232, known as the Revised Corporation Code of the Philippines. Section 2 defines a corporation as "*An artificial being created by operation of law, having the right of succession and the powers, attributes, and properties expressly authorized by law or incidental to its existence.*" *Artificial being* means that by operation of law, a corporation becomes a being with the attributes of an individual with full capacity to enter into contractual relations. It is a legal or juridical person with a personality separate and distinct from individual members. The *right to succession* means that a corporation can exist regardless of the death, withdrawal, insolvency, or incapacity of the individual stockholders and regardless of the transfer interest or shares of stock.

The distinction between a corporation and a partnership as to legal capacity are the following:

- Corporation has a stronger legal personality, enabling it to continue despite the death, insolvency, or withdrawal of any of its stockholders or members. In partnership, the withdrawal, death, or insolvency of any partners would automatically bring about the dissolution of a partnership.
- Limited liability is the main feature in a corporate setting, whereas general partners are liable personally for partnership debts not only to what they have invested in the partnership but even as to their other properties.

Classifications of Corporation

Corporations may be classified according to the following:

- *In relation to the State.*
 - ✓ **Public corporations** are those formed for the government of a portion of the State. An example is the municipality of government functions.
 - ✓ **Private corporations** are those formed for private purpose, benefit, or end. Examples are San Miguel Corporation and Jollibee Food Corporation.
 - ✓ A **quasi-public corporation** is a cross between private and public corporations. Examples are water districts.
- *The place of incorporation.*
 - ✓ A **domestic corporation** obtained its personality through incorporation under the Philippine laws.
 - ✓ A **foreign Corporation** is licensed by the Securities and Exchange Commission (SEC) to do business in the Philippines after complying with set requirements and conditions under Philippine laws.
- *As to stock.*
 - ✓ **Stock corporations** are private corporations with capital stock divided into shares, and the stockholders are entitled to their shares of dividends or allotment of the corporate surplus profits based on their stockholdings or subscriptions.
 - ✓ **Non-stock corporations** are corporations that do not issue stocks and are composed of members, not stockholders. They may be civic, charitable, religious, or professional organizations.

One Person Corporation

A One Person Corporation (OPC) is a corporation with a single stockholder, who can only be a natural person (who must be of legal age), trust, or an estate (Section 116).

One Person Corporation vs. Sole Proprietorship

	One Person Corporation	Sole Proprietorship
<i>Separate Juridical Personality</i>	A corporation is a separate juridical personality from its shareholders. This means that the corporation has an independent existence from that of its individual shareholders.	A sole proprietorship is one and the same as its proprietor.
<i>Liability</i>	The separate juridical personality of a corporation means that the liability of the corporation is not the liability of its shareholders. The liability of a shareholder for the debts of a corporation is limited only to what the shareholder owes to the corporation.	Since the personality of a sole proprietorship is one and the same as its proprietor, whatever the sole proprietorship owes, the proprietor also owes. There is no limit to the liability of the proprietor for the debts of the sole proprietorship.
<i>Succession</i>	When the sole shareholder of an OPC dies, his/her legal heirs can continue managing the OPC.	When the proprietor of the sole proprietorship dies, the existence of the sole proprietorship is also terminated.
<i>Requirements Under the Corporation Code</i>	An OPC is required to appoint a President, Treasurer, and Corporate Secretary. The sole shareholder is automatically the President, but s/he cannot be the Corporate Secretary. The sole shareholder	A sole proprietorship is not subject to any of the mentioned requirements for an OPC.

	can be both the President and Treasurer, subject to the submission of a bond. Furthermore, OPCs are subject to the regulation of the Securities and Exchange Commission and are required to file articles of incorporation and submit annual reportorial requirements.	
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Table 1. Sole Proprietorship vs. One Person Corporation

Source: <https://www.floresofrinlaw.com/entries/8utjwq856v7ufbfrnhf3yi66sc4tw8>

Corporation Law Doctrines

The following are the relevant corporation law doctrines under the Revised Corporation Code:

- **Doctrine of Piercing the Veil of Corporate Existence.** It is a general principle under the law that a corporation has a personality that is separate and distinct from its members. The doctrine of piercing the veil of corporate fiction is a legal precept that allows a corporation's separate personality to be disregarded under certain circumstances so that a corporation and its stockholders or members, or a corporation and another related corporation could be treated as a single entity. It is meant to apply only in situations where the separate corporate personality of a corporation is being abused or being used for wrongful purposes.
- **Doctrine of Business Opportunity.** It refers to the case when a director or officer of the corporation is presented with a business venture which can be profitably handled by the corporation. He must give that business opportunity to the corporation and, if he fails to do so and undertakes the business on his own, he shall be held liable to refund to the corporation whatever profits and benefits he may have derived from such business opportunity.
- **Trust Fund Doctrine.** When the directors of the solvent of insolvent corporation distribute all corporate assets to the stockholders without reserving any assets for payment of corporate debts and liabilities. The directors, officers, or stockholders who received the assets, are considered trustees, and the corporation and creditors can recover the assets from the directors, officers, or stockholders. Such corporate assets they received shall be sold at public auction for the settlement of corporate liabilities.
- **Perpetual Existence.** A corporation shall have perpetual existence unless its articles of incorporation provide otherwise.
- **Corporation may exercise only express, implied, or incidental powers.** No corporation shall possess or exercise corporate powers other than those conferred by the RCC or by its articles of incorporation and except as necessary or incidental to the exercise of the powers conferred.
- **Corporation generally acts through its board.** Unless otherwise provided, the board of directors or trustees shall exercise the corporate powers, conduct all business, and control all properties of the corporation.
- **Business Judgment Rule.** Questions of policy and management are left to the honest decision of the Board of Directors and officers of a corporation, and the courts are without authority to substitute their judgment for that of the Board of Directors unless said judgment had been attended with bad faith.

The Law on Sales, Agency, and Credit Transactions

In the tourism and hospitality industry, agreements arising from contracts are usually made, and potential breaches from these agreements will be encountered. Thus, it is necessary to know the different provisions involving sales, agency, and credit transactions. These are contained in the **Civil Code of the Philippines**.

The Law on Sales

Article 1458. *By the contract of sale, one of the contracting parties obligates himself to transfer ownership of and to deliver a determinate thing, and the other to pay therefor a price certain in money or its equivalent.*

A contract of sale may be absolute or conditional.

Characteristics of a Contract of Sale

The following are the characteristics of a contract of sale:

- *Consensual.* A contract of sale is perfected by mere consent. No form is prescribed for the perfection in a contract of sale, except in the following instances:
 - Those covered under the Statute of Frauds must appear in writing; otherwise, the sale is considered unenforceable (i.e., Sale of real property or any interest therein; and sale of chattels or goods for a price not less than Php500).
 - Sale of real property made through an agent, in which case, the agent's authority must be in writing; otherwise, the agency and sale made through an agent are void.
- *Reciprocal.* It gives rise to reciprocal obligations, where each party is effectively a debtor and a creditor of the other, such that the obligation of one is dependent upon the obligation of the other.
- *Principal.* It can stand by itself without the need for another contract.
- *Onerous.* The consideration of each party is the delivery of the thing or the payment of the price.
- *Commutative.* What the vendor (seller) delivers is considered equivalent of the price paid by the vendee (buyer).
- *Nominate.* It has a designated name under the Civil Code of the Philippines, which is "sale."
- *Transmissive of ownership.* The vendor transfers ownership of the subject matter to the vendee.

Requisites of a Contract of Sale

The following are the requisites of a contract of sale:

- *Consent.* Consent is manifested as the meeting of the offer (which must be certain) and the acceptance (which must be absolute) upon the thing and the cause which are to constitute the contract.
- *Object or Subject Matter.* The object must be *existing or possible, must be licit, and must be determinate.* In a contract of sale, the thing and the price are the subject matter. The price must be understood to be in money or its equivalent.
- *Cause or Consideration.* It represents the why of the contracts. This is the essential reason which moves the contracting parties to enter into the contract. For the seller, the consideration is the price certain in money or its equivalent. For the buyer, the consideration is the thing in a contract of sale.

Effect of Loss of the Object in a Contract of Sale

Article 1480. *Any injury to or benefit from the thing sold, after the contract has been perfected, from the moment of the perfection of the contract to the time of delivery, shall be governed by Articles 1163 to 1165, and 1262.*

Article 1262. *An obligation which consists in the delivery of a determinate thing shall be extinguished if it should be lost or destroyed without the fault of the debtor and before he has incurred in delay.*

Article 1496. *The ownership of the thing sold is acquired by the vendee from the moment it is delivered to him in any manner of the ways specified in Articles 1497 to 1501, or in any other manner signifying an agreement that the possession is transferred from the vendor to the vendee.*

- **If the thing is lost before the perfection of the consent,** the contract is considered nonexistent; therefore, the loss is borne by the seller based on the principle of *res perit domino* ([res pe-rit do-mi-no]; it is the owner of the thing who bears the consequences of the loss).

- **If the thing is lost at the time of the perfection of the contract,** the contract shall be considered without any effect. The legal effect is the same as the object is lost before the perfection of the contract of sale.
- **If the thing is lost after delivery,** the buyer bears the risk of loss since delivery transfers ownership, following the principle of *res perit domino*.
- **If the thing is lost after perfection, but before delivery,** the seller bears the risk of loss since there is no delivery yet, hence, no transfer of ownership to the buyer. This is considered just and equitable, being more in conformity with the principle of *res perit domino*. In this case, the buyer may demand the return of the price in case the payment has been made. The reciprocal nature of a contract of sale dictates that when there is an obligation to deliver a determinate object, there is also a correlative obligation to pay the price. Therefore, once the obligation to deliver is extinguished, the correlative obligation to pay the price is also extinguished. This rule will apply even if the thing is lost through a fortuitous event or even without the fault of the debtor.

Obligations of the Vendor

Article 1495. *The vendor is bound to transfer the ownership of and deliver, as well as warrant the thing which is the object of the sale.*

Article 1496. *The ownership of the thing sold is acquired by the vendee from the moment it is delivered to him xxx.*

Article 1497. *The thing sold shall be understood as delivered when it is placed in the control and possession of the vendee (1462a).*

Under the above provisions, the obligations of the vendor are: **to deliver the thing, to transfer ownership of the thing, and to warrant against eviction and hidden defects.**

• **Delivery** is not only a necessary condition for the enjoyment of the thing, but it also determines the transmission of ownership. The fact that the price of the property delivered has not yet been paid in full is not an obstacle to the acquisition of the ownership thereof by the vendee if such condition has not been stipulated in the contract.

• **Warranty in Case of Eviction.** A *warranty in case of eviction* is an implied warranty in contracts of sale, by virtue of which if the vendee is deprived of the whole or a part of the thing purchased by final judgment based on a right prior to the sale or an act imputable to the vendor, such vendor shall answer for the eviction even though nothing has been said in the contract on the subject.

The requisites of eviction include (i) the deprivation of the vendee of the thing purchased wholly or partially; (ii) the deprivation is by final judgment; (iii) the deprivation is based on a right prior to the sale of an act imputable to the vendor; and (iv) the vendor was summoned in the suit for eviction at the instance of the vendee.

Liability for eviction includes the return of the value at the time of eviction; return of income or fruits that the buyer had to surrender; costs of the suit; expenses of the contract; and damages in case the vendor acted in bad faith.

• **Warranty Against Hidden Defects (Redhibitory).** A **defect** is considered *redhibitory* (a defect that renders a thing useless) if it is hidden, unknown to the buyer, existing prior to the sale at least in origin, and which renders the thing unfit for the use intended. The vendee may elect between withdrawing from the contract and demanding a proportionate reduction of the price with damages in either case. Generally, the period of prescription is six (6) months. However, in redhibitory actions against the faults or defects of animals, the period is 40 days. The period must be counted from the date of delivery to the vendee.

Obligations of the Vendee

Article 1582. *The vendee is bound to accept delivery and pay the price of the thing sold at the time and place stipulated in the contract.*

Actions for the Breach of Contract of Sale

The following are the remedies in case of breach of contract of sale.

	Extrajudicial Remedies	Judicial Remedies
Of the buyer	<ul style="list-style-type: none">• The buyer need not pay unless there is delivery.• The buyer may reject improper deliveries.• The buyer may suspend payment if he is disturbed in the possession or ownership of the thing or has reasonable grounds to fear such disturbance.	<ul style="list-style-type: none">• Damages for breach of contract
Of the seller	<ul style="list-style-type: none">• The vendor is not bound to deliver the thing sold if the vendee has not paid the price.• Installment sales	<ul style="list-style-type: none">• Recovery of the price• Damages in case of <i>bad faith</i> (lack of honesty in dealing with other people)

Law on Agency

Article 1868. *By the contract of agency, a person binds himself to render some service or to do something in representation or on behalf of another, with the consent or authority of the latter (1709a).*

A *contract of agency* is a relationship in which one person, the agent, acts on behalf of another with the authority of the latter, the principal. It is a relationship that results from the manifestation of consent by one person that another shall act on the former's behalf and subject to his control, with consent by the other so to act. The acts of the agent will be binding on his principal.

Example: If a tourism or hospitality company (principal) requests its counterpart located in another place (agent) to enter into certain transactions (e.g., book rooms for the former's guests), an agency relationship is formed.

Article 1918: The principal is not liable for the expenses incurred by the agent in the following cases:

- If the agent acted in contravention of the principal's instructions, unless the latter should wish to avail himself of the benefits derived from the contract;
- When the expenses were due to the fault of the agent;
- When the agent incurred them with the knowledge that an unfavorable result would ensue, if the principal was not aware thereof; and
- When it was stipulated that the expenses would be borne by the agent or that the latter would be allowed only a certain sum.

Article 1919: A contract of agency is extinguished by:

- its revocation;
- the withdrawal of the agent;
- the death, civil interdiction, insanity, or insolvency of the principal or the agent;
- the dissolution of the firm or corporation which entrusted or accepted the agency;
- the accomplishment of the object or purpose of the agency;
- the expiration of the period for which the agency was constituted.

Article 1927: An agency cannot be revoked if a bilateral contract depends upon it, or if it is the means of fulfilling an obligation already contracted, or if a partner is appointed manager of a partnership in the contract of partnership and his removal from the management is unjustifiable.

Article 1927 is an exception to the general rule that an agency is revocable at will.

The Concept of Independent Contractor

It has been a practice in the tourism and hospitality industry to enter into a contract with cooperatives, associations, or establishments engaged in providing messenger, janitorial, laundry, or security services. The principle of independent contractor states that the contractor shall be directly liable for the wages and other labor benefits of its employees.

An association, cooperative, or establishment qualifies to be an independent contractor if it has been contracted to do the work according to its methods and without being subject to the control of the employer, except only as to the results of the work and provided the following requisites concur:

- The contractor has *substantial capital or investment* (tools, equipment, machinery, and work premises) which relates to the job, work, or service to be performed, and the employees recruited, supplied, or placed by such contractor are performing activities that are not directly related to the main business of the principal; or
- The contractor exercises the right to control over the performance of the work of the contractual employees.

Failure to qualify as an independent contractor makes the association, cooperation, or establishment merely a *labor-only contractor*. In such a case, the contractor is considered merely an agent of the principal employer, and the latter is responsible to the employees of the labor-only contractor as if such employees have been directly employed by the principal employer.

Liability of the Principal and the Agent

Article 1883. *If an agent acts in his own name, the principal has no right of action against the persons with whom the agent has contracted; neither have such persons against the principal.*

In such a case, the agent is the one directly bound in favor of the person with whom he has contracted, as if the transaction were his own, except when the control involved things belonging to the principal.

When an agent transacts business in his name, it shall not be necessary for him to state the name of the principal, and he shall be directly liable as if the business were for his own account to the persons with whom he transacts the same. Moreover, an agent is personally liable for acts beyond the scope of his authority and acts in violation of the terms of the written authority.

When it is clear that the agent is acting only on behalf of a disclosed principal, the agent cannot be held personally liable for the contract entered into in such a manner, provided he acts within the scope of his authority.

Law on Credit Transactions

Tourism and hospitality companies are likely to face debts. Hence, it is important to know the different ways of handling debts as well as credit transactions emanating within their respective companies.

Article 1933. *By a contract of loan, one of the parties delivers to another, either something not consumable so that the latter may use the same for a certain time and return it, in which case the contract is called a commodatum, or money or other consumable thing, upon the condition that the same amount of the same kind and quality shall be paid, in which case the contract is simply called loan or Mutuum.*

Commodatum is essentially gratuitous. A simple loan may be gratuitous or with a stipulation to pay interest.

Commodatum is a loan for use wherein the property lent must be returned. Commodatum is essentially gratuitous. For example, when Mr. Smith, a visiting tourist, borrowed the house of Dr. Magno, and Mr. Smith was allowed its free use, Dr. Magno became a bailor in commodatum and Mr. Smith, the bailee.

Simple Loan or Mutuum

Article 1956. *No interest shall be due unless it has been expressly stipulated in writing.*

A *simple loan* or *mutuum* is simply the delivery of a sum of money to another under a contract to return at some future time an equivalent amount with or without an additional sum (i.e., interest) agreed upon for its use. It is a transaction wherein the property owner, called the **lender**, allows another party, the **borrower**, to use the property. The borrower customarily promises to return the property after a specified period with payment for its use, called **interest**. The documentation of the promise is called a **promissory note** when the property is cash.

The **credit** of an individual means his ability to borrow money under the confidence and trust reposed by a lender that he will pay what he may promise. The concession of a "credit" necessarily involves the granting of "loans" up to the limit of the amount fixed in the credit.

In both commodatum and mutuum, the object loaned must be returned, as a general rule, upon demand or the expiration of a stipulated period.

Under Bangko Sentral ng Pilipinas Circular No. 799, Series of 2013, the rate of legal interest is 6% per annum beginning on July 1, 2013. This interest rate applies in case of default (failure of the borrower to pay upon demand or on the due date if demand is not necessary) in the absence of stipulation.

Article 1249: The payment of debts in money shall be made in the currency stipulated, and if it is not possible to deliver such currency, then in the currency which is legal tender in the Philippines. The delivery of promissory notes payable to order or bills of exchange or other mercantile documents shall produce the effect of payment only when they have been cashed or when through the fault of the creditor they have been impaired.

Example 1: If X borrowed from Y \$10,000 payable after two (2) years, he must pay \$10,000 on the due date regardless of the fluctuation in the exchange rate.

Example 2: If X borrowed from Y Php10,000 payable after two (2) years, and X issues a check to Y on the due date as payment, the debt is not considered extinguished until the check is encashed.

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