INTRODUCTION

HISTORY AND ORIGIN

Under the Civil Law.—The law of damages finds its place in the most ancient codes existing. The Twelve Tables of Rome provide means of reparation for injuries done to a person or thing. The Lex Aquilia had for its purpose the providing of compensation for injuries to property. It was the nucleus of the Roman law of damages. It supplemented but did not repeal the damage provisions of the Twelve Tables. It prescribes the measure of damages. It was finally incorporated into the Justinian Digest, Lib. IX, Tit. II, 117-144. The imperial legislator advises his subjects, in making contracts for the doing of anything, to fix the amount of damages by inserting a precise stipulation to that effect (Inst. Lib. II, Tit. XV). In the "Digesto" book 45, Tit. I, Laws 35, 126, we find provisions regarding obligations with a penal clause similar to those in the Civil Code. In the law of Partidas the object of a penal clause is very well defined: "Ponen los omes á las vegadas en las promisiones que facen porque sean mas firmes ó mejor guardadas." (Ley 34, Tit. XI, Part. V.) Finally, in our Civil Code obligations with a penal clause are incorporated (Articles 1152-1155, C. C.)

Under the American Rule.—At Common Law, a contract to pay a specified sum of money upon the happening of a certain event, was enforced according to its terms. The fact that the sum of money, designated as agreed upon to punish breach or to coerce performance, did not have any effect in making such a contract unenforceable. Equity, however, looked at the intent and not the outward form of the contract, and relieved against forfeitures and penalties. (Page on Contracts, Vol. II, p. 1795.)

Before the passage of statutes of William III, 8 and 9 in an action of debt on agreement, performance of which was secured by a penalty, the recovery was for the entire penalty. Relief was solely in equity and originally was granted only in cases of fraud, extemity or accident. The effect of this statute was to put actions for the recovery of penalties for default in the performance of agreements upon the same basis as actions directly upon the agreement to recover damages, with respect to the
quantum of recovery; in other words to provide substantially the same measure of relief in an action at law as the defendant might have obtained in a court of equity. (13 Cyc., pp. 89-90.)

This doctrine which converts damages apparently stipulated or fixed by the parties into a penalty came from the civil law through the courts of chancery, and has at length obtained a firm hold in the courts of common law (Spencer vs. Tilden, 5 Cow. 144, cited in 706, Feb. 391).

In the United States, partly by the adoption of this English Statute (8 and 9, William III) as a part of the American Common Law and partly by American statutes the power of restricting to the collection of actual damages is very generally exercised by the courts of common law (2 Page, Section 1169).

Definition.—In order to dispel confusion and clarify all doubts, a clear understanding of the meanings of the terms “penalty” under the civil law and “liquidated damages” and “penalty” under the common law should be had.

Under the Civil Law.—Art. 1152. In obligations with a penal clause, the penalty shall substitute the indemnity for damages and the payment of interest in case of failure to comply therewith, if it has not been otherwise stipulated.

This penalty can only be made effective, when it is exigible in accordance with the provisions of this code.

Penal clause is that in which a person, in order to insure the performance of an obligation, subjects himself to a penalty or fine in case of delay or non-performance of the obligation, (Argentina, Civil Code, Art. 686).

By obligation with a penal clause is meant that in which the debtor (deudor) obliges himself to give or to do a certain thing in case the principal obligation is not complied with. (Ley 34, Tit. XI, Part. 5.)

In order to insure more the observance of contracts, penalty is sometimes inserted in contracts to subject the obligated to pay indemnity in case of non-performance, and the obligation which result from whatever agreement of this kind is called obligation with a penal clause. (Escriche’s Diccionario Razonado.)

The penal clause is that in which a person, to warrant the performance of an obligation, subjects himself to a penalty which consists in giving or doing something in case of non-performance or delay of the principal obligation (Chile, Civil Code, Art. 1535).

A contract can be celebrated with a penal clause; that is, with obligation to pay a certain sum in cases of delay or want of performance (Guatemala, Art. 1472).

Art. 56. Code of Commerce.—In a commercial contract containing an indemnification clause against the person who fails to comply therewith, the party aggrieved may take legal steps to demand the fulfillment of the contract or the indemnification stipulated; but in resorting to either of these two actions the other one shall be annulled unless there is an agreement to the contrary.
Under the American law. As a general rule, the parties to a contract may stipulate in advance as to the amount which shall be paid in compensation for loss or injury which may result in the event of a breach of the agreement, at least in those cases where the damages which would so result are not fixed by law, and where the amount stipulated does not manifestly exceed the injury which will be suffered, the damages so fixed are termed liquidated or stipulated, the distinction between a penalty and liquidated damages being that the one is a surety for, and the other is to be paid in the event of non-performance of, the act to be done. (Butler vs. Moore, 45 Am. Rep. 508; Williams vs. Vance, 30 Am. Rep. 26; Scofield vs. Tompkins, 35 Am. Rep. 160; Morse vs. Rathburn, 97 Am. Rep. 359; Note 30 Am. Rep. 29.)

It is competent for parties entering upon an agreement to avoid all future questions as to the amount of damages which may result from the violation of the contract and to agree upon a definite sum as that which shall be paid to the party who alleges and establishes the violation of the contract. In this case the damages so fixed are termed liquidated, stipulated or stated damages (1 Sedgwick on Damages, p. 758).

Liquidated damages are an ascertained and certain sum stipulated in a contract to be paid by a party, should he violate it, in recompense to the other (Bishop on Contracts, Sec. 1449).

A contract for a penalty is an agreement to pay a stipulated sum in case of default, intended to coerce performance, to punish default or to secure payment of actual damages (United. States vs. Cutajar, 67 Fed. Rep. 530).

Liquidated damages in the proper sense of the term are a positive debt excluding evidence of actual damages wherever a breach is proved to which they apply (Beale vs. Hayes, 5 Sandf. 640).

PART I

Characteristics of the Penal Clause

From a study of the various definitions given we can conclude that the characteristics of a penal clause are:

First: That it is an accessory agreement;

Second: It serves as a medium of reinforcing the principal obligation in whole or in part;

Third: It is a conventional estimation of damages which insures to the benefit of the creditor in case of non-performance of the principal obligation. These characteristics are true to both systems of law of damages of English and Spanish jurisprudence.

Obligations with a penal clause as distinguished from other classes or kinds of obligation.

Under the Spanish law. Penal clause is distinguished from (1) Suspensive obligation. The former constitutes an obligation, though accessory, while the latter, does not; for this reason the first (penal) can be demanded in case of non-compliance with the principal obligation, or even with the principal obligation, while the suspen-
sive condition can never be exacted to be performed, but according whether this happens or not, the obligation which it affects only can be asked for (8 Manresa, 327).

(2) Alternative obligation. An alternative obligation contains two principal objects, two prestation equally due, even if the payment or performance of one extinguishes the obligation. The obligor by general rule, and the obligee by exception, can elect between the two alternatives. If one perishes, the obligation is concentrated in the other; if one is impossible or illicit the obligation is maintained by the possible or illicit one. This does not occur in penal clause in which the object of the obligation is only one; that is, the principal prestation, and the penalty is a mere accessory, due only in case of non-performance. For this reason the obligor can never offer the penalty in place of the prestation, nor the obligee ask for the penalty if the obligor is not in default. If the principal obligation is illicit or impossible or it becomes so without the fault of the obligor, the penal clause shall be without effect; for, once the principal disappears, there is no basis for the accessory. (Giorgi, Teoría de las Obligaciones, Vol. IV, page 475.)

(3) From the potestative condition. There is a great similarity between the potestative condition and the obligation with a penal clause. In both, the object of the obligation is only one, in which the validity of the obligation depends. The great distinction between the two is: in the potestative, the obligor may prefer to liberate himself from the prestation put in “facultate solutionis”, while in the obligation with a penal clause, he cannot arbitrarily offer the penalty instead of the principal prestation. (Idem.)

Under the American Law.—An alternative contract is one which gives to one of the contracting parties the choice of doing one of two or more different acts as performance of the contract. (Smith & Bergengren, 10 L. R. A. 768.)

Both penalties and liquidated damages are payable on breach of one or more covenants of a contract, whereas the payment provided for in the alternative contract is a performance of the contract, not a compensation for breach.

We have seen that the penal obligations, both Spanish and American, differ from other kinds of obligations. It is now important to know whether the “penalty” as known under the Civil Law has the same nature and scope as the liquidated damages and penalty under the common law. Under the American Law there exists such a wide difference between the liquidated damages and the penalty that it is indispensable to know just wherein lies such discrepancy, before any intelligent comparative study can be made on the two legal systems, the civil and the common law. A short discussion, therefore, of the legal effects of liquidated damages and penalty will not be amiss at this juncture.

The importance of the distinction between liquidated damages and a penalty is this:

If a stipulated payment of forfeiture is considered liquidated damages, the parties are bound by it. The amount is fixed and is not subject to change. But if the forfeiture is regarded as a penalty, the defaulting party may be relieved of it. The
courts will inquire into it to see whether it is unconscionable or excessive. Hence, it is to the advantage of the other party to have the forfeiture construed as liquidated damages. (8 Ruling Case Law, 560.)

It must be confessed that a wide divergence of able opinions, at times highly conflicting, is manifested by courts in matters connected with liquidated damages and penalty. Certain principles however, have guided tribunals of justice in dealing with this difficult question of fixing the right amount to compensate a loss or injury arising either through delay or non-performance.

(1) Intention of the parties.—As to whether a sum agreed to be paid as damages for the violation of an agreement shall be considered as liquidated damages or only as a penalty is held to depend upon the meaning and intent of the parties as gathered from a full view of the provisions of the contract, the terms used to express the intent, and the peculiar circumstances of the agreement. (Williams vs. Green, 14 Art. 315.)

The contract is to govern; and the true question, what was the contract? Whether it was folly or wisdom for the contracting parties thus to bind themselves is of no consequence if the intention is clear. If there be no fraud, circumvention or illegality in the case, the court is bound to enforce the agreement. (Cushing vs. Drew, 97 Mass. 445.)

(2) Nature of damages expressed. No technical words are necessary if the intention of the parties is fairly to be gathered from the instrument. The name given by parties will not have a controlling effect, if their intention appears otherwise from the consideration of the whole agreement. The use of the word "penalty" is not decisive in the point, nor is the use of the words "liquidated damages" conclusive. In determining whether an amount named in a contract is a penalty or liquidated damages, courts are influenced largely by the reasonableness of the transaction and are restrained by the form of the contract nor even by their manifest intent. For instance, if the instrument provide that a larger sum shall be paid on the failure of the party to pay a less sum, the larger sum is a penalty. (Lindsay vs. Ancsby, 28 N. C. 186.)

So where the agreement imposes several distinct duties or obligations of different degrees of importance and the same sum is named as damages for a breach of either indifferently, the sum is to be regarded as a penalty.

Where the damages are capable of being known and estimated, the sum fixed upon as damages will be treated as a penalty, although declared to be intended as liquidated damages.

Where the parties have agreed on the amount of damages, ascertained by fair calculation and adjustment and have expressed this agreement in clear and explicit terms, the amount so fixed will be treated as the true measure of damages and not as a penalty.

Rules of Interpretation

(1) Where the stipulated sum is wholly collateral to the object of the contract, being evidently inserted merely as security for performance, it will not be allowed as
liquidated damages. (Richards vs. Edick, 17 Bard. 260; Law vs. House, 3 Hill 268; Wilkes vs. Bierne, 69 S. E. 266.)

(2) Whenever the stipulated sum is obviously greater than the damage could be, it will not be allowed as liquidated damages (Scofield vs. Tompkins, 85 Ill. 190; Greenleaf vs. Stockton, 78 Cal. 606; Daniel vs. Lumber Co., 85 S. W. 1092.)

(3) Whenever an amount stipulated is to be paid on the payment of a less amount or on default in delivering a thing of less value, the sum will generally be treated as a penalty. (Haldeman vs. Jennings, 14 Ark. 329; Tiernan vs. Hinman, 16 Ill. 400; Peine vs. Weber, 47 Ill. 41.)

(4) Where damages for breach of some of the covenants of an agreement can be readily ascertained, yet there are others where the loss would be difficult to estimate, the damages will usually be construed as a penalty and not as liquidated damages. (McPherson vs. Robertson, 82 Ala. 459; Trower vs. Elder, 77 Ill. 452; Carpenter vs. Lochart, 1 Ind. 434.)

(5) Damages disproportionate to covenants. Where the damages provided for in the agreement are disproportionate to the several covenants therein provided, in some cases being grossly excessive and in others entirely inadequate, they will be construed as a penalty rather than as liquidated. (Watts vs. Sheppard, 2 Ala. 425; Clement vs. Cash, 21 N. Y. 253.)

(6) Uncertainty as to amount of damages. Where the damages are uncertain in their nature, difficult to ascertain or impossible to be estimated with certainty, by reference to any pecuniary standard, and where the parties themselves are more intimately acquainted with all the peculiar circumstances, and are therefore better able to compute the actual or probable damages, it has been the rule to allow the parties to ascertain for themselves, and provide in the agreement itself the amount of damages which shall be paid. (Watts vs. Sheppard, 2 Ala. 425; Williams vs. Green, 14 Ark. 325; Streeter vs. Rush, 25 Cal. 11.)

(7) Delay of performance. Where a party has defaulted in the performance of some contract involving a stipulation of forfeiture, the courts as a general rule construe the same as liquidated damages rather than as a penalty, unless it can be seen from the evidence that the forfeiture is disproportionate to the breach (O'Brien vs. Anniston Pipe Works, 93 Ala. 583; Nelson vs. Jonesboro, 57 Ark. 168; Hall vs. Crowley, 81 Am. Dec. 745).

(8) Partial and entire breach. As a general rule, where a contract provides for the payment of stipulated damages for a particular breach, such stipulation is applicable only to the breach provided for and upon the abandonment or repudiation of the entire contract, the injured party, if his damages are the greater, is not limited to the stipulated damages or vice versa, if the latter are the greater, he is limited to the actual damages. If the breach alleged is not the one provided for or contemplated in fixing the measure of damages, the loss, if any, sustained by the plaintiff because of it should be determined, not by the stipulation contained in the contract.
but by the law. And so where liquidated damages are stipulated for to compensate
for failure to complete work within a specified time and there is refusal to perform
any part of it, such liquidated damages are not applicable when it is apparent that the
parties so stipulating did not contemplate such refusal, but only a failure to complete
within the specified time. (Moses vs Autono, 59 Fla. 499.)

A sum named is not recoverable in case of a partial breach where the measure
of damages for past performance is ascertainable, for under such circumstances the sum
named is generally regarded as a penalty and recovery will be limited to the damages
actually sustained. (Condon vs Kemper, 47 Kan. 126; 13 L. R. A. 671; Wilkes vs
Bierne, 68 W. Va. 82, 31 L. R. A. 937 ns.)

(9) Building Contracts. Liquidated damages often are stipulated in case of
contracts for building, which provide a forfeiture of a certain amount for each day
in which the work is delayed. The courts have usually construed such forfeiture
clauses as liquidated rather than as a penalty, on the ground of the uncertainty in
calculating the damages claimed. (Nelson vs Jonesboro, 57 Ark. 168.)

(10) Contract not to engage in particular business. Where a contract has been
made not engage in any particular profession or business within stated limits, it has
been the custom of the courts to construe such agreement as liquidated damages
rather than as a penalty, in the absence of any evidence to show that the amount is
unjust or oppressive or that the amount claimed is disproportionate to the damages
that would result from the breach or breaches of the several covenants of the agree­
ment. (Perkins vs Lyman, 11 Mass. 76; Mueller vs Keine, 27 Ill. App. 473.)

APPLICATION OF RULES TO PARTICULAR CLASSES OF CONTRACTS

Provisions for liquidated damages are frequently found in contract not to engage
in particular kinds of business within certain territory or for a certain length of time,
(Holbrook vs Tobey, 22 Am. Rep. 589), contracts involving money deposits (38
L. R. A. 817), contracts to convey land; an agreement to convey real property to one
in case of breach of contract with him may be regarded as liquidated damages (Dorcey
vs. Dorcey, 23 L. R. A. 886) and contracts for service. The injury caused by the
sudden breaking off a contract of service by either party involves such difficulties
concerning the actual loss as to render appropriate for stipulated damages. If a
fixed sum or a maximum within which wages unpaid and accruing since the last pay
day might be forfeited is agreed and is not unreasonable or an oppressive exaction,
the stipulation will be regarded as one for liquidated damages if both parties are equally
and justly protected. (Tennessee Mfg. Co. vs James, 15 L. R. A. 211.)

A provision for the forfeiture of all wages due an employee who quits the work
without giving specified number of days' notice may be valid and enforceable (Potts­
ville Iron and Steel Co. vs Good, 116 Pa. St. 385); but a contract which provides
for the forfeiture of all wages due at the time for the breach, regardless of amount
due and regardless as to whether the arrearages were the consequence of the default
of the employer and which preserves no proportion between the sum forfeited and the
actual damages and put all employees upon the same footing, whether much or little was earned or was due when the breach occurred, will be held to provide for as penalty (Tennessee Mfg. Co. vs. James, 15 L. R. A. 211.)

In all these cases, courts are given great discretion in regulating the measure of damages. They do not look upon forfeitures with favor. In a case in the Supreme Court of the United States, it was held, "It will be incumbent on the party who claims them as liquidated damages to show that it was so considered by the contracting parties. (Taylor vs. Sandiford, 7 Wheat. 13.) It must not be understood, however, that courts never enforce the damages stipulated by the parties. As was said in one case, "though courts do not look upon forfeiture with favor, and will, where the contract is susceptible of so doing, construe such a provision as a penalty rather than liquidated damages, such construction should be given as will carry out the intent of the parties, if such intent is clearly ascertainable from the contract. (Turner vs. City of Eremont, 15 Fed. 221.)"

The reason of the American law of liquidated damages and penalty cannot perhaps be more forcibly illustrated than that was said by Judge Deady in Harris vs. Miller, 11 Fed. 118. Says he, "The law is peculiar and instead of giving effect to the contract of the parties according to their intentions, it assumes to control them according to its standard of justice." In a note to Spencer vs. Tilden, 5 Cow. 144 (cited in 106 Fed. 391) it was said, "The doctrine which converts damages apparently stipulated or fixed by the parties into a penalty came from the civil law through the courts of chancery, and has at length obtained a firm hold in the courts of common law. It is obvious that in order to enforce it, courts must disregard the particular expressions of the parties; for the moment we agree that a party may by calling a real penalty "liquidated damages" or throwing it into the form of an alternative in a contract, or substituting its payment for some specified default, secure the whole to himself without regard to the real damages, we bring back the oppressive rule of the common law. The gripping creditor will always use the particular form or phraseology of contract which will secure him his pound of flesh unless the courts interfere in all cases, and tell him that from the very nature and essence of his bond, whatever he claims and in whatever shape or upon whatever footing if it be in truth plainly beyond the legal amount of damages, so far it shall be no more than nominal."

PART II

PENALTY UNDER THE CIVIL LAW COMPARED WITH LIQUIDATED DAMAGES AND PENALTY UNDER THE COMMON LAW

The question that will naturally be asked is whether what is known as "penalty" in the American courts has the same nature and effect has the Civil Law "penalty." We have seen that the American cases make distinction between liquidated damages and penalty. In cases of liquidated damages, the measure of damages enforced by the courts is that which is stipulated by the parties. When "penalty" is involved,
courts have the power to change the measure of damages, by taking into consideration the reasonableness of the contract, the intent of the parties, the circumstances, and so on, of the case.

The Supreme Court of the Philippine Islands has expressly laid down the doctrine that in this jurisdiction "there is no difference between a penalty and liquidated damages so far as the legal results are concerned. Whatever difference exists between them as a matter of language, they are treated the same legally. In either case the party to whom payment is to be made is entitled to recover the sum stipulated without the necessity of proving damages. (Lambert vs. Fox, 26 Phil. 590.)

In the Philippines, courts give much weight to the intention of the parties. The freedom of making contracts is given a wide sphere. Within the liberty to make contract, sanctioned by our laws, everyone is free to execute the contracts he may consider suitable, provided they are not contrary to law, morality and good customs (Gsell vs. Kock, Phil. 6). In this jurisdiction penalties provided in contracts of this character are enforced. It is the rule that parties who are competent to contract may make such agreement within the limitation of the law and public policy as they desire, and that courts will enforce them according to their terms. (Fornow vs. Hoffmeister, 6 Phil. 33; Palacios vs. Municipality of Cavite, 12 Phil. 140; Gsell vs. Kock, 16 Phil. ....)

From a study of the two systems of law, we can deduce that the American liquidated damages is similar to that of obligations with a penal clause under the Civil Law, for in both cases courts enforce the amount stipulated, as the measure of damages in case of breach of the terms of the contract.

ELEMENTS COMMON TO BOTH SYSTEMS OF LAW

As to Sources.—Under the Spanish law. Penal clauses may proceed from obligation or law; from obligation, when parties in making contracts stipulate for liquidated damages in case of non-performance or delay; from law as in case of bonds required by the government. (8 Manresa, 244.)

Act No. 610, Sec. 24, provides, for the exaction of a bond from persons securing license for the use of fire arms. In the case of Insular Government vs. Punsalan (7 Phil., 546) the court ruled that the bond required by Act No. 610 partakes of the nature of an obligation with a penal clause. Upon breach of the conditions imposed by the government, the court adjudged the bond forfeited and the defendants had to pay the sum stated in the bond.

Under the American Law. Penal clauses may also proceed from obligation or law, as in the case of Spanish law (Bishop on Contracts, Sec. 1449). When a statute imposes a specified penalty for an omission of duty prescribed by statute, the amount of the penalty is the amount of damages (Waite vs. Dowley, 94 U. S. 527).

Purpose of the Penal Clause.—Under the Spanish law. The end of the penal clause is to reinforce the contractual tie and establish a conventional indemnity.
Its cause is founded on the fear of non-performance; its source is the freewill of the parties (Giorgi, Teorfa de las Obligaciones, Vol. IV, p. 464).

Another purpose of the penal clause is to avoid the necessity of proving damages (Lambert vs. Fox, 26 Phil. 590; Palacios vs. The Municipality of Cavite, 13 Phil. 140; Sentence of Feb. 19, 1904, Supreme Court of Spain). By means of the penal clause an exact representation of losses and injuries which may flow from the breach of the contract is effected by the parties at the time of the celebration of the same. In this matter, litigations may be avoided; the difficult proof of the extent of losses and injuries is obviated.

Par. I, Art. 1152, Civil Code. In obligations with a penal clause, the penalty shall substitute the indemnity for damages and the payment of interest in case of a failure to comply therewith, if it has not been otherwise stipulated.

Art. 56, Code of Commerce. In a commercial contract containing an indemnification clause against the person who fails to comply therewith, the party aggrieved may take legal steps to demand the fulfillment of the contract or the indemnification stipulated; but in resorting to either of these two actions, the other one shall be annulled, unless there is an agreement to the contrary.

Under the American law. A contract for a penalty is an agreement to pay a stipulated sum in case of default, intended to coerce performance, to punish default or to secure payment of actual damages. (U. S. vs. Cutajar, 67 Fed. 530.)

In liquidated damages, proof of actual damage is unnecessary (Clark vs. Bernard, 108 U. S., 436; City of Salem vs. Anson, 56 L. R. A., 169.)

Under both systems, therefore, the purpose of the penal clause is to obviate the necessity of proving damages, to have the damages ascertained before hand in case of breach, and to coerce performance.

When is the Penalty Exigible.—Under the Spanish law. Art. 1152, par. 2. This penalty can only be made when it is exigible in accordance with the provision of this code.

Impossible conditions, those against good customs and those prohibited by law will annul the obligation which depend on them (Art. 1116, Civil Code).

Art. 1102. Liability arising from fraud is exigible in all cases. The renunciation of action to make it effective is null and void. Is this article in contradiction with Article 1152? Manresa says, no. This article does not authorize in any manner the impurity of fraud on account of previous agreement. The party who alleges fraud must prove injuries and losses in order that he can recover more besides the stipulated damages. (See Manresa's Commentary on Art. 1152.)

Under the American law. The liquidation must be reasonable. Just compensation for the injury sustained is the principle at which law aims and the parties will not be permitted by express stipulation, to set aside this principle applied that the liquidation provided by a contract may, as the circumstances show to be equitable in one case be upheld, and in another set aside (Myer vs. Hart, 40 Mich. 517, 523).
Generally speaking, in determining the reasonableness of the amount the court will take into consideration, the absence or presence of fraud or oppression and the purpose the agreements seeks to subserve (Note to Madler vs. Silverstone, N. S., 29).

Exception from obligation. The debtor cannot exempt himself from the fulfillment of the obligation by paying the penalty, unless in case that such right has been expressly reserved to him. (Art. 1153, par. 1, Civil Code.)

Neither can the creditor jointly exact the fulfillment of the obligation and the payment of the penalty, unless such right has been granted to him. (Part II, 1153, C. C.)

But the creditor cannot ask for the fulfillment of the obligation and the penalty, unless the penalty has been stipulated for mere delay or that the payment of the penalty shall not extinguish the obligation. (Argentina, Art. 693, C. C.)

The reason of this is clear. The penalty is established as an accessory obligation. It cannot be admitted that instead of guaranteeing the performance of the principal obligation, the penalty should be substituted, leaving the principal obligation unperformed and depriving the creditor of the power to exacting its fulfillment. (8 Manresa, 239.)

Under the American law. A penal obligation being secondary to a primary one the performance of which it is intended to assure, the creditor cannot, except in two contingencies, avail himself of the double remedy on the event of his debtor's failure to fulfill the primary obligation to accept the subsequent performance of that and exact the penalty at one and the same time; and those contingencies are: First, when the penalty is expressly stipulated for the mere delay; and second, when by a special stipulation the penalty may be exacted if the principal obligation is not executed (Barrow vs. Bloom, 18 La. Ann. 276).

Accrual of right. Spanish law. The debtor is obliged to pay the stipulated penalty when (1) by his negligence delay or non-performance results; (2) and the creditor demands the payment of the penalty.

The debtor is held liable for the penalty of absolute non-performance or contravention when for acts imputable to him the prestation to give or to do becomes impossible or the contravention not to do is consummated. If there is no term, delay will begin from the time of judicial demand in which the creditor asks for the penalty or demonstrate that the performance in specific form has become impossible by the default of the debtor (IV Georgi, 478).

Art. 1100, Civil Code. Persons obliged to deliver or to do something are in default from the moment on which the creditor exacts judicially or extrajudicially the compliance of their obligation.

However the intimation of the creditor, in order that default may exist, shall not be necessary:

1. When the obligation or law declares it expressly.
2. When from its nature and circumstances, it may appear that the fixing of the time on which the thing was to be delivered or the service was to be done, was a determinate cause to constitute the obligation. In reciprocal obligation, none of the obliged parties shall incur default, if the other does not comply with or does not submit to duly comply with what he is bound to do. From the moment on which one of the obligated parties complies with his obligation, the default begins for the other party.

Art. 1125, Civil Code. Obligations, the fulfillment of which has been fixed for a certain day, are exigible only when such day arrives.

Art. 1128. When the obligation does not fix a term, but it can be inferred from its nature and circumstances that there was an intention of granting it to the debtor, the courts shall fix the duration of such a term. The courts shall also fix the duration of a term when it may have been left at the will of the debtor.

American law. As a general rule, the right to claim damages as liquidated damages or a penalty accrues after an offer and refusal to perform the agreement, coupled with present ability to do so. In all cases however regard should be had to the term of the contract itself and to the intention of the parties and the surrounding circumstances under which the agreement was made. (Hammond vs. Gilmore, 14 Conn. 249; Thorndike vs. Locke, 98 Mass. 340.)

Once undertaking to do a thing on particular day is broken it, when the day pass, with no default in the other party and no excuse appearing it is not done (Marshall vs. Ferguson, 23 Cal. 65; Weeks vs. Little, 89 N. Y. 566).

When Performance Excused.—Under the Civil Law. Art. 1105, Civil Code. No one shall be liable for events which could not be foreseen or those, even when foreseen, were inevitable aside from the cases expressly stated by the law or those in which the obligation so declares. When the delay or non-performance is due to fortuitous events the obligor is not liable for the payment (Giorgi Teoria de las Obligaciones, Vol. IV, page 477).

Under the American law. Non-performance of an express covenant can be excused only by showing that its performance is unlawful, or has been rendered impossible by the intervention of causes beyond human control. (Morrow vs. Campbell, 31 American Dec., 701.)

Where condition of bond is to do a thing impossible or illegal the obligor is discharged (Brown vs. Dillhunty, 43 American Dec. 499).

Under the Civil law. It is not necessary that the amount or importance of the losses and injuries should be established; if their existence is proven that is all is required. (Sentence of Feb. 19, 1914, Spain; Palacios vs. Municipality of Cavite, 12 Phil., 140.)

To ask for the penalty, the creditor (or obligee) is not obliged to prove that he has sustained damages and the debtor cannot exempt himself from paying by proving that the creditor has not suffered any damages (Argentina, Art. 690). The penalty
shall be exigile in case in which it has been stipulated, the debtor not being allowed to allege that the performance of the obligation has not done any damage to the creditor or that it has benefited him (Chile, Art. 1542; Columbia, Art. 1599).

Under the Common law. In an action to recover a sum stipulated in a contract as liquidated damages, no proof of actual damages is necessary (Spicer vs. Hoop, 51 Ind. 365; Sandford vs. First National Bank, 94 Iowa, 680).

Extent of recovery. Under the Civil law. Art. 1152. Part I, Civil Code. In obligation with a penal clause the penalty shall substitute the indemnity for damages and the payment of interest if it has not been otherwise stipulated. The question is, are the parties confined to the amount of damages stipulated in case of breach or total loss of the object of the obligation? The writer does not think so. In support of his opinion he cites Manresa, Vol. 8, page 239, wherein the commentator says in case of fraud, the obligee has to prove this fact in order to recover more besides the penalties stipulated. Art. 1109, Civil Code, provides that interest due shall produce legal interest from the date on which it was judicially demanded, even if the obligation is silent on this point. Georgi says on this point: "The judge can besides the penalty concede an indemnification for injuries arising from acts which the agreed penalty does not cover, or for acts of losses different from those stipulated for by the penalty." For instance, there is an agreement to pay five pesos for every day's delay of delivery of thing purchased. Now, suppose the vendor delays and besides destroys or injures the thing. Is it not reasonable that the vendee is entitled both to the value of the thing and compensation for the delay? (Georgi, Vol. IV, p. 473.)

Under the American law. Penalties are often stipulated to be paid in agreements and covenants in the event of the breach of affirmative stipulations. In such cases the party injured is not confined to his actions for the penalty, but has an election to sue on the agreements or covenants. In that action he is entitled to recover full damages without regard to the penalty. It is not the measure of damages, nor does it limit the recovery thereof, if the actual injury requires a larger amount for just compensation (Meinert vs. Bottecher, 60 Minn. 204; New Holland Turnpike Co. vs. Lancaster, 71 Pa. 442). In case of penal bond with condition for the payment of money only the plaintiff is entitled to recover the full amount of the penalty as a debt and the excess of interest beyond the penalty in the shape of damages for the detention of the debt (Long vs. Long, N. J. Eq., 59).

Nullity of the Principal Obligation or Penal Clause.—Civil law. The nullity of the penal clause does not carry with it that of the principal obligation. The nullity of the principal obligation carries with it that of the penal clause Art. 1155, Civil Code; Argentina, Art. 697. The reason of this rule is this: The parties when contracting have in mind the performance of the principal obligation. The penal clause is nothing more than a guarantee for its fulfillment. The performance of the obligation should not therefore be frustrated by the mere nullity of the accessory, which is secondary in character. The nullity of the principal obligation carries with it that
of the penal clause. It is a maxim of law that the accessory follows the principal. A penalty presupposes an offended right. If the principal obligation is void, there is no right offended.

Under the American law. If the condition be impossible when the bond was made or becomes so afterwards by the act of God, the law or the obligee, the penalty is saved and bond in one case is void and in the other is discharged. (Commonwealth vs. Oberry, 44 Am. Rep. 471; where condition of bond is to do a thing impossible or illegal, the obligor is discharged. (Brown vs. Dillahunt, 43 American Decision, 499.)

In terrorem.—Exorbitant and oppressive interests stipulated in penal obligations when their object is to coerce and intimidate the debtor are reduced by the courts (Sentencia de 9 de Febrero, 1906, Supreme Court, Sp.). A sentence of the Court of Trani, Italy, Aug. 3, 1898, has ruled that the penal clause cannot be enforced when, by its enormity, it appears to have been inserted solely to intimidate the debtor.

Under the American law. Where a contract provides for a forfeiture of a sum so great that it is apparent that the provision was inserted in terrorem, it will be treated as a penalty and not as a liquidated damage.

Power to reduce the penalty. Under the Civil law. The judge shall equitably modify the penalty, when the principal obligation has been partly or irregularly complied with by the debtor. (Spain, Art. 1154, C. C.; Argentina, Art. 694; Bolivia, Art. 822.) The only case recognized by the Civil Code in which the court is authorized to intervene for the purpose of reducing the penalty stipulated in the contract is when the principal obligation has been partially or irregularly fulfilled and the court can see that the person demanding has received the benefit of such part or irregular performance. In such case the Court is authorized to reduce the penalty to the extent of the benefit received by the party enforcing the penalty. (Lambert vs. Fox, 26 Phil. 590; Fornow vs. Hoffmeister, 6 Phil. 33; Palacios vs. Municipality of Cavite, 12 Phil. 140; Gsell vs. Kock, 16 Phil. 1.)

Judges cannot moderate the penalty when the obligation is absolutely unperformed, and its fulfillment is demanded side by side with the penalty. The liberty of stipulation is respected. (Sentence of Feb. 6, 1906, Supreme Court, Spain.) Georgi, however, the great commentator of the Italian Code whose provision on this subject is exactly like that of the civil code enforced in these islands give three instances in which the judge may intervene as to the modifications of the penalty.

(1) The judge can mitigate the penalty when the parties have conceded him this power.

(2) The judge can, besides the penalty, concede an indemnization for losses and injuries to which the stipulated penalty does not extend, or in other words, for causes of injuries different from those which are the subject of the penalty. If the creditor
maliciously desires not to perform his contract in order to cause greater damages than that which is stipulated in the penal clause, the judge can also adjust the penalty or damages.

(3) The judge may reduce the penalty when there is partial fulfillment of the obligation.

Under the American law. Where the agreement has been partially performed, it is the policy of the Court to regard the damages as a penalty and allow the plaintiff to recover only such damages as he actually sustained (Cook vs. Finch, 19 Minn. 407). It must be noted, however, that the American courts have greater powers than our courts with regard to the modifications or reductions of the penalty. Where there is partial compliance or no compliance at all the courts can modify the penalty. That is why they make such distinctions between liquidated damages and penalty. In case of liquidated damages, courts enforce the stipulated damages. If the covenant is considered a penalty, they substitute their judgment in place of what is stipulated and make such modifications as the case warrants. American Courts do not favor forfeiture. As was said by Judge Deady in Harris vs. Miller, 11 Fed. 118. "The law is peculiar, and instead of giving effect to the contract of the parties according to their intentions, it assumes to control them according to its standard of justice."

CONCLUSION

In concluding this laborious task of comparison, which is not free from difficulties—the author finds that the Civil law on the subject of obligations with a penal clause is very similar in its nature, scope and effect to that of the Common Law liquidated damages; that is to say, courts enforce the penal stipulation as the measure of damages in case of breach of the contract, without admitting evidence as to the extent of the injury done, so long as the breach is proved. It resembles the Common Law penalty in that the judge is empowered to reduce the penal sum in certain circumstances. with this notable difference, however, that under the Civil Law, the judge can modify the penalty only when there is part or irregular performance; whereas, under the American law, the judge is given great discretion. Whether there is irregular or part performance or no performance at all, American courts do "not favor forfeiture," but will enforce the penalty only to such an extent as will justly and equitably compensate the injured party.

The question is likely to arise whether or not it is desirable in the Philippines to adopt the American law on the subject of Liquidated Damages and penalty. The author, inspired by the completeness and thoroughness of the American Jurisprudence on the subject is strongly persuaded to the conclusion that it is wise that the courts of the Philippine Islands should have the same ample powers as the courts of the United States and England have with regard to the modification of the "penalty" reducing the sum stipulated or mitigating the penalty covenanted as the reason of the case warrants.
If often happens that a penalty is stipulated simply as a security for the principal obligation or as an intimidation to the obligor. Its amount may far exceed the value of the principal obligation. In case of absolute non-performance is it reasonable to enforce a penalty of five thousand pesos ($5,000) when the obligation is worth only one hundred pesos? We should be guided by the principle that the liquidation must be reasonable. "Just compensation for the injury sustained is the principle at which the law aims."