

FIRST DIVISION

[G.R. No. 119033, July 09, 2008]

**EK LEE STEEL WORKS CORPORATION, PETITIONER, VS. MANILA
CASTOR OIL CORPORATION, ROMY LIM, AND THE COURT OF
APPEALS, RESPONDENTS.**

D E C I S I O N

CARPIO, J.:

The Case

Before this Court is a petition for review^[1] of the Decision^[2] dated 7 February 1995 of the Court of Appeals in CA-G.R. CV No. 34743. The Court of Appeals reversed the decision^[3] of the Regional Trial Court, Branch 123, Kalookan City in a collection suit filed by Ek Lee Steel Works Corporation against Manila Castor Oil Corporation and Romy Lim.

The Antecedents

Ek Lee Steel Works Corporation (petitioner) is engaged in the construction business while Manila Castor Oil Corporation (respondent) claims to be a pioneer in the castor oil industry with Romy Lim (Lim) as its President.

In November 1987, respondent contracted petitioner for the construction of respondent's castor oil plant and office complex in Sasa, Davao City. Petitioner agreed to undertake the construction of the following structures with their respective costs:

Project	Price
I. Office Building (Building I) and Boiler Room	P2,000,000
II. Concrete Fence 10- feet-high on three sides of the factory site	P283,662 ^[4]
III. 20-meter x 52-meter Concrete Pavement	P318,800
IV. 90,000-gallon Steel Oil Tank with Stand	P472,500
V. 40- feet-high 10,000-gallon Water Tank	P103,556.60
VI. Steel Oil Tank Foundation	P175,650
VII. 40-ton Oil Tank	P88,837

Under the seven letter-agreements, respondent would make various stipulated down payments upon approval of petitioner's proposals. The remaining balance of the contract prices was payable to petitioner through progress billings.

In April 1988, petitioner alleged that respondent verbally agreed to have another building (Building II-Warehouse) constructed on the project site worth P349,249.25.

Respondent denied the existence of this contract because it never approved such contract. Therefore, petitioner discontinued its construction of Building II-Warehouse after finishing its foundation and two side walls.

On 16 May 1988, petitioner submitted a Statement of Account to respondent showing respondent's accumulated payables totaling P764,466. [5] Respondent paid P500,000 as shown in a letter of even date. In the same letter, respondent promised to pay certain amounts thereafter upon the completion of specific portions of the project. The full text of the letter dated 16 May 1988 [6] reads:

May 16, 1988

MR. DANNY ANG
General Manager
Ek Lee Steel Works Corp.
#171 5th St., 8th Avenue
Caloocan City, M.M.

SUBJECT: FIFTH PARTIAL PAYMENT OF P500,000.00

Dear Danny,

This is to confirm that upon payment of the subject above, the fifth (5) partial payment which represent 70.5% of the total project cost of 3.4 Million, you will have to accomplished [sic] all the contracted work by June 15, 1988, except the office building. Thereafter, we will pay you the 6th partial payment with the amount of P200,000.00. And upon the completion of the office building we will then pay you the amount of P460,000.00 which will represent 90% of the contracted work. As per the terms of our contract we will keep the P340,000.00 which represent the 10% retention.

Yours truly,

R.T. LIM
President

Conforme:

Mr. Danny Ang

Date: signed

On 5 July 1988, respondent paid petitioner P70,000.

Sometime thereafter, petitioner allegedly demanded payment of respondent's remaining balance, but to no avail. Hence, petitioner stopped its construction in the project site. Thereafter, petitioner requested the Office of the City Engineer of Davao City to conduct an ocular inspection of the project site to determine the percentage of its finished work. Engineer Demetrio C. Alindada of the Davao Engineering Office reported that most of the scope of the work items were 100% completed.

On 4 November 1988, petitioner filed a collection suit against respondent and Lim, with an application for a writ of preliminary attachment. The complaint prayed, among others, that respondent and Lim be held jointly and severally liable for the amount of P1,623,013.81 with interest.

In their answer filed on 23 December 1988, respondents jointly alleged, as an affirmative defense, that as of 16 May 1988, petitioner was already in delay. They claimed that petitioner abandoned the project on 16 July 1988. Respondents further alleged that certain portions of the construction work did not conform to the specifications agreed upon by the parties.

Then, on 8 May 1990, respondents filed a Supplemental Answer, alleging that sometime in July 1989, the 90,000-gallon capacity oil tank tilted towards the sea resulting in the stoppage of respondent's operations. Consequently, respondents were constrained to hire a contractor to remedy the damage caused by the poor and substandard installation of the oil tank. Respondents prayed for the payment of surveyor's fee, contractor's fee, operating expenses, and unrealized income during the shut-down period.

During the trial, respondents presented as evidence a Technical Verification Report submitted by Engineer Raul D. Moralizon to prove that the project was incomplete and had no utility value at the time petitioner abandoned the project.

The Ruling of the Trial Court

The trial court ruled in favor of petitioner. The trial court held that petitioner was justified in abandoning its construction of the project. As of 5 July 1988, when respondent paid P70,000, petitioner's billings reached P3,895,872.85, while payments totaled only P2,505,534, or short by P1,390,338.85, exclusive of other charges. Considering respondent's non-payment of this remaining balance, petitioner was understandably unwilling to proceed with the construction of the project. Respondent's non-payment was a clear violation of the stipulated progress billings.

The trial court likewise noted petitioner's request for an inspection from the Engineering Office of Davao City prior to the issuance of an occupancy permit. The trial court declared that "no contractor who has unreasonably abandoned a job ever bothered itself making such a request; an abandoning contractor just packs up and goes." In addition, the trial court found that respondent never reported the supposed "abandonment" to the Engineering Office of Davao City. Neither did respondent send a notice or letter demanding the completion of the project. Had there been abandonment, respondent would have filed a suit against petitioner.

On the "modifying" agreement dated 16 May 1988, the trial court found the parties' diametrically-opposed versions equally true. Respondent claimed that it gave petitioner an extension of the deadline until 15 June 1988. On the other hand, petitioner insisted that it gave respondent an equivalent extension to raise enough funds to meet the accumulated bills. However, the trial court held that this particular agreement is not crucial in this case.

The trial court also gave the Report of Engineer Demetrio C. Alindada of the Davao Engineering Office (Alindada Report) a higher probative value than the Technical

Verification Report submitted by respondent's hired Civil Engineer, Raul D. Moralizon (Moralizon Report). The trial court found the Moralizon Report self-serving. Based on the Alindada Report, most of the items contracted for construction were 100% completed. Hence, the trial court applied Article 1234 of the Civil Code which states that "[i]f the obligation has been substantially performed in good faith, the obligor may recover as though there had been a strict and complete fulfillment, less the damages suffered by the obligee."

The trial court disposed of the collection case, as follows:

WHEREFORE, judgment is hereby rendered in favor of the plaintiff and against the defendants, ordering the latter, jointly and severally, as follows:

1. To pay the plaintiff the amount of P1,426,176.45 with legal interest to be computed from the date of the filing of the complaint until fully paid;
2. To pay the plaintiff the amount of P154,883.33 representing actual damages in the form of interest payment for loans;
3. To pay the amount of P100,000.00 as and for attorney's fees; and
4. Costs of the suit.

Defendants' counterclaims are hereby dismissed for lack of merit.

SO ORDERED.^[7]

The Ruling of the Court of Appeals

The Court of Appeals reversed the decision of the trial court. The appellate court ruled that the 16 May 1988 letter novated all the earlier agreements between the parties. It held that the letter specified the scope of the remaining construction work, the amounts payable by respondent, and the schedules for the completion of the remaining work and for the corresponding payments.

The Court of Appeals stated that petitioner was not entitled to further payments from respondent because petitioner failed to comply with its obligation of finishing all the contracted work, except the office building, on 15 June 1988 as clearly stipulated in the 16 May 1988 letter.

The Court of Appeals found that the petitioner's failure to complete the project rendered the same useless for the object which the parties had intended it to be, specifically, an office, plant, and warehouse complex.

The Court of Appeals disagreed with the trial court's reliance on the Alindada Report. The appellate court stated that the Alindada Report should rather have indicated the scope of work items enumerated in the parties' seven letters-contracts and the percentage of work accomplished in each of these items, instead of enumerating merely the scope of work items which Alindada found completed. The Alindada Report was therefore not a reliable evidence in determining the percentage of accomplishment in the project.

The Court of Appeals went on to say that even assuming that Article 1234 of the Civil Code applies to this case, the trial court should have correspondingly decreased the amount to be recovered by petitioner by the amount of damages suffered by respondent, as stated in the same provision.

However, the Court of Appeals faulted respondent for the trial court's failure to correspondingly reduce the amount recoverable by petitioner. There was no showing that respondent demanded that petitioner should finish the project; otherwise, respondent would hire another contractor to complete it. Respondent did not report petitioner's abandonment of the project to the Office of the Building Official of Davao City. Respondent simply hired another contractor to complete the unfinished job left by petitioner. In addition, the building permits obtained for the supposed continuation of the works indicated that they were for "new construction" instead of "addition," "repair," "renovation," or "others."

The Court of Appeals ordered petitioner to reimburse P70,000 as overpayment by respondent.

The dispositive portion of the Court of Appeals' decision reads:

WHEREFORE, and for all the foregoing considerations, the Decision appealed from is hereby REVERSED and SET ASIDE, and another one entered:

1. Dismissing the complaint;
2. Ordering the plaintiff:
 - (a) To reimburse the defendants the amount of P70,000.00;
 - (b) To pay defendant Manila Castor Oil Corporation the sum of P50,000.00 as damages for besmirched reputation;
 - (c) To pay defendant Romy Lim the amount of P50,000.00 for moral damages;
 - (d) To pay defendants their attorney's fees in the amount of P10,000.00.

With costs in this instance against the plaintiff-appellee.

SO ORDERED.^[8]

Hence, this petition.

The Issues

The issues in this case are:

1. Whether the 16 May 1988 letter novated the previous agreements of the parties;
2. Whether petitioner can validly collect from respondent the remaining balance of the total contract price;