

Title: EK Lee Steel Works Corporation v. Manila Castor Oil Corporation & Romy Lim

Facts:

EK Lee Steel Works Corporation (petitioner), a construction business, entered into multiple contracts with Manila Castor Oil Corporation (respondent; a castor oil industry pioneer, led by its president Romy Lim) and agreed to construct several structures for the respondent's plant in Davao City with corresponding costs, through seven letter-agreements. Progress billings were stipulated for payments, pending completion.

In April 1988, petitioner claimed a verbal agreement for additional warehouse construction, which the respondent denied, resulting in the petitioner discontinuing its work on the warehouse after partially completing it. On May 16, 1988, after submitting a statement of account showing pending payables, the petitioner received PHP 500,000 from the respondent who promised future payments upon completion milestones.

The respondent made another payment of PHP 70,000 on July 5, 1988, but petitioner eventually ceased work due to alleged non-payment. After requesting an ocular inspection, Engineer Alindada of the Davao Engineering Office reported that most work items were 100% complete.

The petitioner filed a collection suit with an application for a writ of preliminary attachment for an outstanding amount, but the respondent counter-claimed that the petitioner abandoned the project and left substandard work, causing damage for which they hired another contractor to remedy.

Procedural Posture:

The Regional Trial Court favored the petitioner, finding justification in the abandonment due to non-payment and ruling for a substantial performance under Article 1234 of the Civil Code. Upon the respondents' appeal, the Court of Appeals reversed this decision, emphasizing that the May 16, 1988, letter novated the agreement by setting a completion date and specific payment schedules. It enumerated deficiencies in the project, considered it incomplete, and held that the petitioner's claim was not due as it had not fulfilled its obligations.

Issues:

1. Whether the May 16, 1988, letter served to novate previous agreements between the parties.
2. Whether the petitioner was entitled to collect the remaining balance of the contract price.

3. Whether there was an overpayment entitling the respondent to reimbursement.
4. Whether Romy Lim was solidarily liable for any outstanding amount.

Court's Decision:

The Supreme Court held that:

1. The May 16, 1988, letter did not novate the previous agreements but modified the manner of payment.
2. The petitioner was not entitled to the remaining balance as it failed to complete the contracted works by the stipulated deadline.
3. Reimbursement of PHP 70,000 was not justified as it was not specifically pleaded as overpayment.
4. The last issue became moot due to the resolution of the other issues.

The High Court found that the petitioner relied on flawed evidence to show project completion and did not discharge the burden of proof. The petition was denied and the CA's decision was modified to delete the order for reimbursement.

Doctrine:

The Supreme Court reiterated that in reciprocal obligations, neither party incurs in delay if the other does not comply or is not ready to comply in a proper manner with what is incumbent upon them. The Court also touched upon the principle that an agreement does not constitute novation by the mere fact that it expressly recognizes the performance of an existing obligation unless it is clearly indicated that the parties intend to dissolve the old obligation in lieu of a new one.

Class Notes:

- Parties to a contract must comply in good faith with their respective reciprocal obligations (Civil Code, Article 1169).
- Novation requires an express agreement to extinguish an old obligation in favor of a new one (Civil Code, Article 1292).
- Substantial performance under Article 1234 of the Civil Code allowing for recovery less damages, requires the obligation to be in fact substantially fulfilled.

Historical Background:

This case reflects the intricacies of contract performance and construction agreements. It illustrates the challenges in determining contract completion and the significance of specific milestones and payment terms in construction-related contracts. The reversal of the trial

court's ruling by the Court of Appeals, and the subsequent scrutiny by the Supreme Court, epitomizes the meticulous legal process involved in the interpretation and enforcement of contracts in the Philippines.