

## **PHESCO INCORPORATED, PLAINTIFF-APPELLANT, VS. FIRST QUEZON CITY INSURANCE COMPANY, INC. DEFENDANT-APPELLEE,**

Ponente: BARRIOS, J.

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### **BARRIOS, J.:**

This is an appeal from the Decision dated July 3, 2003 and the subsequent Order dated November 17, 2003 issued in a case of Sum of Money with Damages filed by the appellant Phesco Incorporated (or Phesco for brevity) against Salvan Construction & Trading Enterprises, Ltd. (or Salvan Construction) and the appellee First Quezon City Insurance Co., Inc. (or FQCICI). The dispositive portion of the said Decision reads:

WHEREFORE, a decision is hereby rendered in this case in favor of the plaintiff ordering the defendants Salvan Construction and Trading Enterprises, Ltd. and First Quezon City Insurance Co., Inc., to pay plaintiff Phesco, Inc. jointly and severally the following:

- The sum of P155,363.00 representing the balance of cash advances after deducting the value of the work accomplished by defendant Salcon (sic) plus legal rate of interest thereon computed from August 1996, date of service of the demand letters until fully paid;
- The sum equivalent to 1/10 of 1% of the contract price for every day of delay reckoned April 23, 1996, plus legal rate of interest thereon computed from August 1996 until fully paid by way of liquidated damages.
- The sum of P50,000.00 as attorney's fees.
- The costs of suit.

The liability of defendant First Quezon City Insurance Co., Inc., is limited only to the amount of P250,000.00.

The counterclaims of both defendants are denied for lack of merit. (pp. 307-308, record)

The Department of Transportation and Communication had this Municipal Telephone Projects for the Province of Benguet. The principal construction contractor for this project is Saxtex International of Canada which sub-contracted some portions of the project to Canac International of Canada. Phesco, a local construction firm was then sub-contracted by Canac International to accomplish the project and in turn Phesco sub-contracted the project to Salvan Construction. Thus on February 6, 1996, Phesco and Salvan Construction entered into a Contract for the Construction of Public Calling Office Buildings and Construction of Monopoles and Masts Foundation for the Municipal Telephone Projects for the Province of Benguet wherein the latter undertook to construct 3m x 3m PCO Buildings in twelve (12) Municipalities, including the construction of 13 Monopole and 6 Mast Foundations x x x and excavation of the PCO, monopole and mast grounding lines x x x and providing AC Power connections for the Municipal Telephone Projects all in the province of Benguet (Exh. "A", p. 7, record, Vol. 1). The contract price was P1,065,200.00. In the said contract a Performance Bond was required, wherein it was stipulated that:

SALCON (sic) shall furnish PHESCO Performance Bond in the form of surety bond acceptable to PHESCO in the amount of Twenty (20%) percent of the Contract Price to cover any defects that may arise from the

completed work. This bond shall be effective until the work is completed and accepted by PHESCO, CANAC SI and MTPO.

In compliance therewith, Salvan Construction secured a surety bond from FQCICI in the amount of P250,000.00 (Exh. "B", p. 13, record).

To fund the project, Salvan Construction obtained cash advances from Phesco which as of August 13, 1996 has reached P660,063.00. Despite its cash advances however, Salvan Construction failed to finish the project. Phesco sent letters demanding that it complete the undertaking, but this fell on deaf ears and Phesco was then forced to complete the project at its own expense. FQCICI as the surety was likewise notified of Salvan Construction's non-completion of the construction.

On April 14, 1997, Phesco instituted the instant suit alleging that despite the lapse of the 75 days agreed date of completion of the project, Salvan Construction failed to do so.

Salvan Construction admitted that it failed to complete the project under the contract but it defended that its failure to do so was the fault of Phesco. According to Salvan Construction, it was not able to fully comply with the works as stipulated because the project engineers of Phesco, Canac and MPTO were too strict and could not agree with each other as to the scope of work and the specifications of materials. For the non-accomplishment of the 4th group of projects consisting of Bakun, Mankayan and Buguias, Salvan Construction reasoned that this was because of the failure of Phesco to secure the approval from the Mayors of said places which resulted in the loss of construction materials that were already put up in those areas. There was delay too because Phesco willfully and unjustly refused to pay wages in the total amount of P156,170.00 as a result of its unilateral takeover of the construction works.

For FQCICI, it claimed that it should not be solidarily liable with Salvan Construction. While it admitted the Surety Bond contracted, it however alleged that the true agreement and contents of this is actually a guaranty, and as such Salvan Construction is primarily liable and all remedies against it should first be exhausted before FQCIC can be proceeded against.

After trial, the court a quo on July 3, 2003 ruled in favor of Phesco and held Salvan Construction and FQCICI jointly and severally liable (p. 307, record, Vol. 1).

On September 29, 2003, FQCICI filed a Motion to Adopt Defendant's FQC's Memorandum as its Motion for Reconsideration (pp. 328-330, record, Vol. 1). The court a quo on November 17, 2003 denied the motion for lack of merit (p. 357, record, Vol. 1). A Motion for Reconsideration (pp. 364-377, record, Vol. 1) was filed by FQCICI on December 17, 2003, and before it could be resolved on January 18, 2004 Phesco filed a Motion for the Issuance of a Writ of Execution (pp. 391-392, record, Vol. 1).

The court a quo on February 10, 2004 denied the motion for reconsideration (p. 397, record, Vol. 1) and subsequently on March 2, 2004 granted the motion for execution (p. 413, record, Vol 1). These were made the subjects of a special civil action for certiorari before the 14th Division of the Court of Appeals which in its decision promulgated on March 15, 2005 granted the petition and NULLIFIED AND SET ASIDE the Orders dated November 17, 2003 and February 10, 2004 (p.12, record, Vol. 2) issued by the court a quo. It further ordered that:

Respondent Judge is DIRECTED to consider the petitioner's memorandum as its motion for reconsideration and to resolve such motion for reconsideration with dispatch.

Complying therewith, the court a quo turned around on the motion for reconsideration. Convinced on second look that FQCICI as surety cannot be held liable to secure that which is not provided for in the principal contract, it

disposed in its Order of April 5, 2005 that:

WHEREFORE, the Motion for reconsideration is GRANTED and the decision of the Court dated July 3, 2003 is hereby amended DISMISSING the complaint as far as FQCICI is concerned. (p. 22, record, Vol. 2)

Disappointed with the exclusion of FQCICI from liability and firm that the Decision of July 3, 2003 should stand, Phesco came to Us on appeal assigning the following as the errors committed by the court a quo:

I

THE COURT A QUO ERRED WHEN IT ISSUED THE ORDER DATED APRIL 5, 2005 ABSOLVING APPELLEE FROM LIABILITY AS SURETY EVEN FOR THE LIQUIDATED DAMAGES STIPULATED IN THE SUBJECT CONTRACT FOR WHICH DEFENDANT SALVAN WAS HELD LIABLE.

II

THE COURT A QUO ERRED WHEN IT CONSIDERED THE ARGUMENTS CONTAINED IN APPELLEE'S MOTION FOR RECONSIDERATION DESPITE THE FACT THAT THEY HAVE NOT BEEN RAISED AS ISSUES IN APPELLEE'S ANSWER. (p. 52, rollo)

The appeal is not meritorious.

In the Surety Bond agreement between Salvan and FQCICI, it was provided among the conditions of the obligation:

TO GUARANTEE THE PERFORMANCE OF SALCON (sic) IN CONSTRUCTING THE PCO BUILDING AND MONOPOLE AND MAST FOUNDATIONS OF THE MUNICIPAL TELEPHONE PROJECTS IN BENGUET. (Exh. "B", p.13, record, Vol.1)

It is clear from this that what was being guaranteed by FQCICI was the construction of the project but not the payment of any and all sums owed by Salvan Construction. The court a quo was then correct when it discussed in the assailed Order that:

The Court finds merit in the Motion for Reconsideration and agrees with FQCICI that the cash advances secured by Salvan Construction Enterprises Limited pursuant to the contract of construction between itself and plaintiff PHESCO is not covered by the surety bond/performance bond issued by FQCICI in favor of PHESCO Inc. There is nothing in said suretyship agreement or contract which states any liability on the part of the surety for failure of Salvan Construction to account for and/or to return said cash advances to PHESCO Inc. Moreover, whatever covenants or agreements, if any, entered into by and between PHESCO Inc., and Salvan Construction Enterprises Limited pertaining to cash advances does not bind FQCICI, the latter's undertaking being limited only to such undertakings embodied in its surety-performance bond.

x x x A careful examination of the contract of construction between PHESCO Inc. and Salvan Construction Enterprises Limited reveals that the giving or release of advance payments in favor of Salvan Construction Enterprises Limited is not part of their written agreement. It stands to conclude, therefore, that FQCICI as surety for the construction project cannot be held liable to secure that which is not provided for in the principal contract of construction. (p. 21, record, Vol. 2)

To emphasize, the contract specifically stated the "Payments Terms", but contrary to the stated payment scheme provided, Phesco allowed Salvan Construction to procure cash advances. Undoubtedly there was a material deviation or an alteration of the contract and this was done without the knowledge of FQCICI. An essential alteration in the terms of a Loan Agreement without the consent of the surety extinguishes the latter's obligation. As the Court held in *National Bank v. Veraguth*, "[i]t is fundamental in the law of suretyship that any agreement between the creditor and the principal debtor which essentially varies the terms of the principal contract, without

the consent of the surety, will release the surety from liability” (Security Bank and Trust Company, Inc. vs. Cuenca, 341 SCRA 781, 783).

The second assigned error too must fail.

Rule 10, Sec. 5 of the Rules of Civil Procedure provides:

Sec 5. Amendment to conform to or authorize presentation of evidence . - When issues not raised by the pleadings are tried with the express or implied consent of the parties, they shall be treated in all respects as if they had been raised in the pleadings. x x x

While it is true that the issue of liability of Salvan Construction for cash advances was never raised in the pleadings, said omission was cured because this was litigated upon. In fact it was even Phesco which presented evidence that there were cash advances and this was not objected to. The rule on amendment need not be applied rigidly, particularly where no surprise or prejudice is caused the objecting party. And x x x we held that where there is a variance in the defendant’s pleadings and the evidence adduced by it in the trial, the Court may treat the pleading as amended to conform with the evidence (Northern Cement Corp. vs. Intermediate Appellate Court, 158 SCRA 408, 409).

In fine, the rules of procedure ought not to be applied in a very rigid, technical sense, for they have been adopted to help secure – not override – substantial justice (Remulla vs. Manlongat, 442 SCRA 226).

WHEREFORE, the appeal is DENIED and the Order appealed from is hereby AFFIRMED.

SO ORDERED.

Guariña III and Romilla-Lontok, JJ., concur.

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