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SECOND DIVISION

[G.R. No. 169975, March 18, 2010]

PAN PACIFIC SERVICE CONTRACTORS, INC. AND RICARDO F. DEL ROSARIO, PETITIONERS, VS. EQUITABLE PCI BANK (FORMERLY THE PHILIPPINE COMMERCIAL INTERNATIONAL BANK), RESPONDENT.

D E C I S I O N

CARPIO, J.:

The Case

Pan Pacific Service Contractors, Inc. and Ricardo F. Del Rosario (petitioners) filed this Petition for Review [1] assailing the Court of Appeals' (CA) Decision [2] dated 30 June 2005 in CA-G.R. CV No. 63966 as well as the Resolution [3] dated 5 October 2005 denying the Motion for Reconsideration. In the assailed decision, the CA modified the 12 April 1999 Decision [4] of the Regional Trial Court of Makati City, Branch 59 (RTC) by ordering Equitable PCI Bank [5] (respondent) to pay petitioners P1,516,015.07 with interest at the legal rate of 12% per annum starting 6 May 1994 until the amount is fully paid.

The Facts

Pan Pacific Service Contractors, Inc. (Pan Pacific) is engaged in contracting mechanical works on airconditioning system. On 24 November 1989, Pan Pacific, through its President, Ricardo F. Del Rosario (Del Rosario), entered into a contract of mechanical works (Contract) with respondent for P20,688,800. Pan Pacific and respondent also agreed on nine change orders for P2,622,610.30. Thus, the total consideration for the whole project was P23,311,410.30. [6] The Contract stipulated, among others, that Pan Pacific shall be entitled to a price adjustment in case of increase in labor costs and prices of materials under paragraphs 70.1 [7] and 70.2 [8] of the "General Conditions for the Construction of PCIB Tower II Extension" (the escalation clause). [9]

Pursuant to the contract, Pan Pacific commenced the mechanical works in the project site, the PCIB Tower II extension building in Makati City. The project was completed in June 1992. Respondent accepted the project on 9 July 1992. [10]

In 1990, labor costs and prices of materials escalated. On 5 April 1991, in accordance with the escalation clause, Pan Pacific claimed a price adjustment of P5,165,945.52. Respondent's appointed project engineer, TCGI Engineers, asked for a reduction in the price adjustment. To show goodwill, Pan Pacific reduced the price adjustment to P4,858,548.67. [11]

On 28 April 1992, TCGI Engineers recommended to respondent that the price adjustment should be pegged at P3,730,957.07. TCGI Engineers based their evaluation of the price adjustment on the following factors:

1. Labor Indices of the Department of Labor and Employment.
2. Price Index of the National Statistics Office.
3. PD 1594 and its Implementing Rules and Regulations as amended, 15 March 1991.
4. Shipping Documents submitted by PPSCI.
5. Sub-clause 70.1 of the General Conditions of the Contract Documents. [12]

Pan Pacific contended that with this recommendation, respondent was already estopped from disclaiming liability of at least P3,730,957.07 in accordance with the escalation clause. [13]

Due to the extraordinary increases in the costs of labor and materials, Pan Pacific's operational capital was becoming inadequate for the project. However, respondent withheld the payment of the price adjustment under the escalation clause despite Pan Pacific's repeated demands. [14] Instead, respondent offered Pan Pacific a loan of P1.8 million. Against its will and on the strength of respondent's promise that the price adjustment would be released soon, Pan Pacific, through Del Rosario, was constrained to execute a promissory note in the amount of P1.8 million as a requirement for the loan. Pan Pacific also posted a surety bond. The P1.8 million was released directly to laborers and suppliers and not a single centavo was given to Pan Pacific. [15]

Pan Pacific made several demands for payment on the price adjustment but respondent merely kept on promising to release the same. Meanwhile, the P1.8 million loan matured and respondent demanded payment plus interest and penalty. Pan Pacific refused to pay the loan. Pan Pacific insisted that it would not have incurred the loan if respondent released the price adjustment on time. Pan Pacific alleged that the promissory note did not express the true agreement of the parties. Pan Pacific maintained that the P1.8 million was to be considered as an advance payment on the price adjustment. Therefore, there was really no consideration for the promissory note; hence, it is null and void from the beginning. [16]

Respondent stood firm that it would not release any amount of the price adjustment to Pan Pacific but it would offset the price adjustment with Pan Pacific's outstanding balance of P3,226,186.01, representing the loan, interests, penalties and collection charges. [17]

Pan Pacific refused the offsetting but agreed to receive the reduced amount of P3,730,957.07 as recommended by the TCGI Engineers for the purpose of extrajudicial settlement, less P1.8 million and P414,942 as advance payments. [18]

On 6 May 1994, petitioners filed a complaint for declaration of nullity/annulment of the promissory note, sum of money, and damages against the respondent with the

RTC of Makati City, Branch 59. On 12 April 1999, the RTC rendered its decision, the dispositive portion of which reads:

> WHEREFORE, premises considered, judgment is hereby rendered in favor of the plaintiffs and against the defendant as follows:
>
> 1. Declaring the promissory note (Exhibit "B") null and void;
> 2. Ordering the defendant to pay the plaintiffs the following amounts:
>
>   a. P1,389,111.10 representing unpaid balance of the adjustment price, with interest thereon at the legal rate of twelve (12%) percent per annum starting May 6, 1994, the date when the complaint was filed, until the amount is fully paid;
>
>   b. P100,000.00 representing moral damages;
>
>   c. P50,000.00 representing exemplary damages; and
>
>   d. P50,000.00 as and for attorney's fees.
>
> 3. Dismissing defendant's counterclaim, for lack of merit; and
> 4. With costs against the defendant.
>
> SO ORDERED. [19]

On 23 May 1999, petitioners partially appealed the RTC Decision to the CA. On 26 May 1999, respondent appealed the entire RTC Decision for being contrary to law and evidence. In sum, the appeals of the parties with the CA are as follows:

> 1. With respect to the petitioners, whether the RTC erred in deducting the amount of P126,903.97 from the balance of the adjusted price and in awarding only 12% annual interest on the amount due, instead of the bank loan rate of 18% compounded annually beginning September 1992.
>
> 2. With respect to respondent, whether the RTC erred in declaring the promissory note void and in awarding moral and exemplary damages and attorney's fees in favor of petitioners and in dismissing its counterclaim.

In its decision dated 30 June 2005, the CA modified the RTC decision, with respect to the principal amount due to petitioners. The CA removed the deduction of P126,903.97 because it represented the final payment on the basic contract price. Hence, the CA ordered respondent to pay P1,516,015.07 to petitioners, with interest at the legal rate of 12% per annum starting 6 May 1994. [20]

On 26 July 2005, petitioners filed a Motion for Partial Reconsideration seeking a

reconsideration of the CA's Decision imposing the legal rate of 12%. Petitioners claimed that the interest rate applicable should be the 18% bank lending rate. Respondent likewise filed a Motion for Reconsideration of the CA's decision. In a Resolution dated 5 October 2005, the CA denied both motions.

AGGRIEVED BY THE CA'S DECISION, PETITIONERS ELEVATED THE CASE BEFORE THIS COURT.

The Issue

Petitioners submit this sole issue for our consideration: Whether the CA, in awarding the unpaid balance of the price adjustment, erred in fixing the interest rate at 12% instead of the 18% bank lending rate.

Ruling of the Court

We grant the petition.

This Court notes that respondent did not appeal the decision of the CA. Hence, there is no longer any issue as to the principal amount of the unpaid balance on the price adjustment, which the CA correctly computed at P1,516,015.07. The only remaining issue is the interest rate applicable for respondent's delay in the payment of the balance of the price adjustment.

The CA denied petitioners' claim for the application of the bank lending rate of 18% compounded annually reasoning, to wit:

> Anent the 18% interest rate compounded annually, while it is true that the contract provides for an interest at the current bank lending rate in case of delay in payment by the Owner, and the promissory note charged an interest of 18%, the said proviso does not authorize plaintiffs to unilaterally raise the interest rate without the other party's consent. Unlike their request for price adjustment on the basic contract price, plaintiffs never informed nor sought the approval of defendant for the imposition of 18% interest on the adjusted price. To unilaterally increase the interest rate of the adjusted price would be violative of the principle of mutuality of contracts. Thus, the Court maintains the legal rate of twelve percent per annum starting from the date of judicial demand. Although the contract provides for the period when the recommendation of the TCGI Engineers as to the price adjustment would be binding on the parties, it was established, however, that part of the adjusted price demanded by plaintiffs was already disbursed as early as 28 February 1992 by defendant bank to their suppliers and laborers for their account. [21]

In this appeal, petitioners allege that the contract between the parties consists of two parts, the Agreement [22] and the General Conditions, [23] both of which provide for interest at the bank lending rate on any unpaid amount due under the contract. Petitioners further claim that there is nothing in the contract which requires the consent of the respondent to be given in order that petitioners can charge the bank

lending rate. [24] Specifically, petitioners invoke Section 2.5 of the Agreement and Section 60.10 of the General Conditions as follows:

> Agreement
>
> 2.5 **If any payment is delayed, the CONTRACTOR may charge interest thereon at the current bank lending rates**, without prejudice to OWNER'S recourse to any other remedy available under existing law. [25]
>
> General Conditions
>
> 60.10 Time for payment
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> The amount due to the Contractor under any interim certificate issued by the Engineer pursuant to this Clause, or to any term of the Contract, shall, subject to clause 47, be paid by the Owner to the Contractor within 28 days after such interim certificate has been delivered to the Owner, or, in the case of the Final Certificate referred to in Sub-Clause 60.8, within 56 days, after such Final Certificate has been delivered to the Owner. In the event of the failure of the Owner to make payment within the times stated, the Owner shall pay to the Contractor interest at the rate based on banking loan rates prevailing at the time of the signing of the contract upon all sums unpaid from the date by which the same should have been paid. The provisions of this Sub-Clause are without prejudice to the Contractor's entitlement under Clause 69. [26] ***(Emphasis supplied)***

Petitioners thus submit that it is automatically entitled to the bank lending rate of interest from the time an amount is determined to be due thereto, which respondent should have paid. Therefore, as petitioners have already proven their entitlement to the price adjustment, it necessarily follows that the bank lending interest rate of 18% shall be applied. [27]

On the other hand, respondent insists that under the provisions of 70.1 and 70.2 of the General Conditions, it is stipulated that any additional cost shall be determined by the Engineer and shall be added to the contract price after due consultation with the Owner, herein respondent. Hence, there being no prior consultation with the respondent regarding the additional cost to the basic contract price, it naturally follows that respondent was never consulted or informed of the imposition of 18% interest rate compounded annually on the adjusted price. [28]

A perusal of the assailed decision shows that the CA made a distinction between the consent given by the owner of the project for the liability for the price adjustments, and the consent for the imposition of the bank lending rate. Thus, while the CA held that petitioners consulted respondent for price adjustment on the basic contract price, petitioners, nonetheless, are not entitled to the imposition of 18% interest on the adjusted price, as petitioners never informed or sought the approval of respondent for such imposition. [29]