

THIRD DIVISION

[G.R. No. 159731, April 22, 2008]

**EASTERN ASSURANCE AND SURETY CORPORATION,
PETITIONER, CON-FIELD CONSTRUCTION AND DEVELOPMENT
CORPORATION, RESPONDENT.**

D E C I S I O N

AUSTRIA-MARTINEZ, J.:

Before the Court is a Petition for Review on *Certiorari* under Rule 45 of the Rules of Court assailing the March 28 2003 Decision^[1] and August 26, 2003 Resolution^[2] of the Court of Appeals (CA) in CA-G.R. CV No. 68409.

The facts of the case are as follows:

Con-Field Construction and Development Corporation (Con-Field) is a domestic corporation contracted by the ABS-CBN Corporation to construct and install a centralized air-conditioning system in the latter's building in Bacolod City, Negros Occidental.

In a document notarized on November 23, 1995, Con-Field (respondent) entered into an Agreement^[3] with Freezinhot, an entity which represents itself as a corporation duly organized and existing under the laws of the Philippines. In the said Agreement, Freezinhot, as sub-contractor, agreed to furnish, at its expense, equipment, tools, labor, supervision and other facilities necessary to complete the project of constructing and installing the required air-conditioning system of ABS-CBN's building in Bacolod. For the said project, Con-Field Agreed to pay Freezinhot the amount of P1,730,150.00.

One of the provisions of the Agreement required Freezinhot to furnish Con-Field with a performance bond equivalent to the sum of P346,150.00 which would insure the prompt and faithful performance of Freezinhot's obligation. In accordance with such provision, Freezinhot secured from Eastern Assurance and Surety Corporation (EASCO) the required performance bond.^[4]

Subsequently, Freezinhot commenced work on the project.

In a letter dated April 8, 1996,^[5] Con-Field, through its project engineers, brought to Freezinhot's attention its observations regarding the latter's slow pace of work as well as the defects in some parts of the project which had been finished.

On May 4, 1996, Freezinhot's President, Demetrio de Guzman, wrote Con-Field a letter expressing its desire that their contract be terminated.^[6] The whole text of the letter reads as follows:

I HEREBY MR. DEMETRIO M. DE GUZMAN TENDER MY TERMINATION OUR SIGNED CONTRACT FOR ABS-CBN BACOLOD MECHANICAL WORK DUE TO TECHNICAL REASONS AND ALSO INFORMING YOU AND YOUR COMPANY THAT ANY OF MY EMPLOYEE YOU ABSORBED EFFECTIVE THIS DAY, MAY 4TH 1996 THAT I HAVE NO MORE RESPONSIBILITIES TO ANY UNTOWARD INCIDENT OR ANY ACCIDENT THAT WILL OCCUR.^[7]

Martin S. Co, the Executive Vice-President of Con-Field, responded to de Guzman with a letter dated May 7, 1996,^[8] to wit:

In response to your letter dated May 04, 1996, please be informed that CON-FIELD CONST. & DEVT. CORP. is not pressuring your company to terminate your contract for MECHANICAL WORKS at Radio-TV station Bldg. In Bacolod City. As we understand, it is your own decision to terminate the contract.

Let it be known that CON-FIELD did not in any way intend to terminate the contract neither facilitated any action for the termination of your contract with us. But on the other hand extended our support by financing the project, i.e. Mechanical Works thru our provision of materials & consumables, in addition to payroll of your workers.

We had accepted your termination of contract with the ff: basis;

1. Lack of Equipment to complete the project up to commissioning
2. Lack of technical capability in respect with shop drawing and other documents to be submitted to us, works schedules submittals.
3. Lack of manpower & supervision to complete the project on time. This resulted to A/C equipment damages and lack of coordination to other works.
4. Lack of financial support for the project.

We wish to inform you that the cost of labor & materials that we will purchase for the said works will be deducted on your remaining contract balance.

We thank you for your understanding in your move to terminate the contract as this reflects the true situation of your work & by this move also impede the jeopardy of over shooting more in the mechanical work schedule.

We hope that we have made our position clear and we hope this is the last time that we discuss this issue.^[9]

Subsequently, Con-Field took over and completed the project.

On January 8, 1997, Con-Field filed with the Regional Trial Court (RTC) of Quezon City a Complaint^[10] against Freezinhot, de Guzman and EASCO (petitioner) seeking to recover the amount of P616,961.14 representing the sum incurred by Con-Field in completing the said project, as well as the P346,150.00 performance bond stipulated in its Agreement with Freezinhot. Con-Field also sought recovery of attorney's fees and litigation expenses.

Freezinhot and de Guzman failed to file their answer to the complaint. Con-Field filed a motion to declare them in default.^[11]

In its Order dated July 11, 1997, the RTC declared Freezinhot and de Guzman in default.^[12]

Meanwhile, EASCO filed its Answer with Compulsory Counterclaim.^[13]

After trial, the RTC rendered judgment in favor of Con-Field.^[14] The dispositive portion of the RTC Decision reads:

WHEREFORE, premises considered, the Court hereby renders judgment in favor of the plaintiff and against the defendants ordering:

1. Defendant FREEZINHOT to pay plaintiff the amount of P616,961.14 as principal obligation plus the legal interest from the filing of the complaint;
2. Defendants FREEZINHOT and EASCO jointly and severally to pay plaintiff the sum of P346,150.00 for and as the amount of Performance Bond plus legal interest from the date of filing of the instant case until fully paid;
3. Defendants FREEZINHOT and EASCO jointly and severally to pay plaintiff the amount of P20,000.00 for attorney's fees;
4. On the cross-claim, the defendant FREEZINHOT to reimburse the defendant EASCO the sum equivalent to its share plus legal interest from the date of payment of EASCO to the plaintiff; and
5. Defendants to pay the cost of suit.

SO ORDERED.^[15]

EASCO appealed the RTC Decision to the CA.

On March 28, 2003, the CA promulgated its presently assailed Decision^[16] with the following dispositive portion:

WHEREFORE, premises considered, the instant appeal is hereby PARTLY GRANTED, in that the Decision of the Regional Trial Court of Quezon City, Branch 216, dated June 22, 2000 is hereby AFFIRMED, with the sole MODIFICATION that the Eastern Assurance Surety Corporation's liability to pay plaintiff attorney's fees is hereby DELETED.

SO ORDERED.^[17]

EASCO filed a Motion for Reconsideration^[18] but the CA denied it in its Resolution^[19] dated August 26, 2003.

Hence, the present petition filed by EASCO based on the following assignment of errors:

I. The appellate court glaringly committed an error of law when it wrongfully concluded in its assailed decision that:

"By no stretch of imagination can this set of circumstances and evidence be construed to mean that the plaintiff had mutually terminated its agreement with defendant Freezinhot, as it appears that such pre-termination was due to the unilateral act of Freezinhot and Demetrio de Guzman." (par. 1, p. 7, Decision, Annex "A-1" of Petition)

which aforecited ruling is contradicted by the oral testimony or express admission of plaintiff's witness, Executive Vice-President Martin S. Co, which unmistakably shows or tends to show that:

1) The agreement (Exh. A) was not consummated, implemented, carried into effect, or its conditions fulfilled or performed, except for Freezinhot's securing of a performance bond in the amount of Php346,150.00 required under the agreement on the basis of which EASCO issued the required bond in behalf of Freezinhot and in favor of Con-Field.

2) In lieu of the said sub-contracting agreement, the parties effected the prohibited "labor-only" sub-contracting arrangement wherein Freezinhot merely supplied workers to Con-Field who allowed them to work under its (Con-Field's) own account and responsibility due to Freezinhot's inability to execute the agreed work on its own due to lack of substantial capital and the tool, equipment, among others, necessary therefore, without due notice to EASCO.

3) Con-Field's admission in its letter (Exh. E) that it "had accepted your (Demetrio de Guzman's) termination of contract," without the knowledge and consent of EASCO completely extinguished and discharged EASCO from all liability in its contract of suretyship.

II. The accessory contract of suretyship cannot exist without a valid principal obligation as in this case where the sub-contractor failed to fulfill or satisfy the conditions set forth in the said agreement.

III. The appellate court manifestly committed an error of law when it ruled that the 78% work completion by the sub-contractor as testified to by the said plaintiff's witness -

"is by no means conclusive and the same was given as a mere opinion." (Penultimate par., p. 7, Decision, Annex "A-1").

being grounded entirely on surmises or conjectures to justify the award of damages equivalent to EASCO's performance bond, and

which is iniquitous or unconscionable, assuming without admitting that the bond is liable therefor.^[20]

Petitioner contends that respondent admits that Freezinhot lacks substantial capital or investment in the form of tools, equipment, machineries and supply of materials which are needed in executing the agreed project; that the sub-contracting agreement between respondent and Freezinhot was, in fact, not implemented because the project was done under the account of respondent and that Freezinhot simply supplied skill and services to perform the required work; and that, in essence, what was carried into effect by respondent and Freezinhot was a "labor-only" sub-contracting arrangement which is prohibited under the Labor Code.

Petitioner also claims that, based on evidence, respondent and Freezinhot both agreed to terminate their contract leading to a final, mutual and complete settlement of all previous transactions between them.

Petitioner argues that since the sub-contracting agreement between respondent and Freezinhot was never implemented, there can be no valid principal obligation to speak of. As such, under the provisions of Articles 2052^[21] and 2076^[22] of the Civil Code, petitioner is not bound to comply with the terms of the suretyship agreement. Petitioner contends that respondent and Freezinhot's mutual termination of their contract resulted in the extinguishment of Freezinhot's principal obligation and the performance bond's accessory obligation.

Petitioner further avers that it was benefited by the termination of the contract, which has the effect of a compromise, as provided for under the provisions of Article 2063^[23] of the Civil Code.

Petitioner also asserts that respondent's acceptance of Freezinhot's proposal for termination of the contract operates as a renunciation of its right to receive payment of the performance bond from petitioner.

Lastly, petitioner claims that based on the testimony of respondent's own witness, Freezinhot worked on the project for a period of seven months and that when respondent took over, it only took them more than a month to complete the project. Based on this premise, petitioner concludes that the project was actually about to be finished when respondent took over from Freezinhot.

On the other hand, respondent contends that the grounds relied upon by petitioner in the present petition do not constitute questions of law on the basis of which the review powers of the Supreme Court may not be invoked.

Respondent also avers that the CA correctly ruled that the issue on "labor-only" contracting was never raised in the proceedings before the RTC or the CA and that the settled rule is that an issue cannot be raised for the first time on appeal.

Anent petitioner's liability as surety, respondent argues that the termination of the contract between respondent and Freezinhot was predicated on the latter's breach of its obligation under their agreement to provide equipment, tools, labor and materials for the project and that under the said agreement, it is clearly stipulated that petitioner is solidarily liable with Freezinhot to pay the performance bond upon