Republic of the Philippines
Supreme Court
Manila

FIRST DIVISION

J PLUS ASIA DEVELOPMENT CORPORATION,
Petitioner,

- versus -

UTILITY ASSURANCE CORPORATION,
Respondent.

G.R. No. 199650

Present:

SERENO, *C.J.*,
Chairperson,
LEONARDO-DE CASTRO,
BERSAMIN,
VILLARAMA, JR., and
REYES, *JJ.*

Promulgated:

JUN 26 2013

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DECISION

VILLARAMA, JR., *J.*:

Before the Court is a petition for review on certiorari under Rule 45 of the 1997 Rules of Civil Procedure, as amended, assailing the Decision[1] dated January 27, 2011 and Resolution[2] dated December 8, 2011 of the Court of Appeals (CA) in CA-G.R. SP No. 112808.

The Facts

On December 24, 2007, petitioner J Plus Asia Development Corporation represented by its Chairman, Joo Han Lee, and Martin E. Mabunay, doing business under the name and style of Seven Shades of Blue Trading and Services, entered into a Construction Agreement[3] whereby the latter undertook to build the former's 72-room condominium/hotel (Condotel Building 25) located at the Fairways & Bluewaters Golf & Resort in Boracay Island, Malay, Aklan. The project, costing ₱42,000,000.00, was to be completed within one year or 365 days reckoned from the first calendar day after signing of the Notice of Award and Notice to Proceed and receipt

[1] *Rollo*, pp. 57-68. Penned by Associate Justice Samuel H. Gaerlan with Associate Justices Hakim S. Abdulwahid and Ricardo R. Rosario concurring.
[2] Id. at 69-73.
[3] Id. at 87-99.

of down payment (20% of contract price). The ₱8,400,000.00 down payment was fully paid on January 14, 2008.[4] Payment of the balance of the contract price will be based on actual work finished within 15 days from receipt of the monthly progress billings. Per the agreed work schedule, the completion date of the project was December 2008.[5] Mabunay also submitted the required Performance Bond[6] issued by respondent Utility Assurance Corporation (UTASSCO) in the amount equivalent to 20% down payment or ₱8.4 million.

Mabunay commenced work at the project site on January 7, 2008. Petitioner paid up to the 7th monthly progress billing sent by Mabunay. As of September 16, 2008, petitioner had paid the total amount of ₱15,979,472.03 inclusive of the 20% down payment. However, as of said date, Mabunay had accomplished only 27.5% of the project.[7]

In the Joint Construction Evaluation Result and Status Report[8] signed by Mabunay assisted by Arch. Elwin Olavario, and Joo Han Lee assisted by Roy V. Movido, the following findings were accepted as true, accurate and correct:

> III] STATUS OF PROJECT AS OF 14 NOVEMBER 2008
>
> 1) After conducting a joint inspection and evaluation of the project to determine the actual percentage of accomplishment, the contracting parties, assisted by their respective technical groups, SSB assisted by Arch. Elwin Olavario and JPLUS assisted by Engrs. Joey Rojas and Shiela Botardo, concluded and agreed that **as of 14 November 2008, the project is only Thirty One point Thirty Nine Percent (31.39%) complete**.
>
> 2) Furthermore, the value of construction materials allocated for the completion of the project and currently on site has been determined and agreed to be ONE MILLION FORTY NINE THOUSAND THREE HUNDRED SIXTY FOUR PESOS AND FORTY FIVE CENTAVOS (P1,049,364.45)
>
> 3) The additional accomplishment of SSB, reflected in its reconciled and consolidated 8th and 9th billings, is Three point Eighty Five Percent (3.85%) with a gross value of P1,563,553.34 amount creditable to SSB after deducting the withholding tax is P1,538,424.84
>
> 4) The unrecouped amount of the down payment is P2,379,441.53 after deducting the cost of materials on site and the net billable amount reflected in the reconciled and consolidated 8th and 9th billings. The uncompleted portion of the project is 68.61% with an estimated value per construction agreement signed is P27,880,419.52.[9] (Emphasis supplied.)

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4 Id. at 962-967.
5 Id. at 101-103, 606.
6 Id. at 184.
7 Id. at 109.
8 Id. at 109-110.
9 Id. at 110.

On November 19, 2008, petitioner terminated the contract and sent demand letters to Mabunay and respondent surety. As its demands went unheeded, petitioner filed a Request for Arbitration[10] before the Construction Industry Arbitration Commission (CIAC). Petitioner prayed that Mabunay and respondent be ordered to pay the sums of ₱8,980,575.89 as liquidated damages and ₱2,379,441.53 corresponding to the unrecouped down payment or overpayment petitioner made to Mabunay.[11]

In his Answer,[12] Mabunay claimed that the delay was caused by retrofitting and other revision works ordered by Joo Han Lee. He asserted that he actually had until April 30, 2009 to finish the project since the 365 days period of completion started only on May 2, 2008 after clearing the retrofitted old structure. Hence, the termination of the contract by petitioner was premature and the filing of the complaint against him was baseless, malicious and in bad faith.

Respondent, on the other hand, filed a motion to dismiss on the ground that petitioner has no cause of action and the complaint states no cause of action against it. The CIAC denied the motion to dismiss. Respondent's motion for reconsideration was likewise denied.[13]

In its Answer Ex Abundante Ad Cautelam With Compulsory Counterclaims and Cross-claims,[14] respondent argued that the performance bond merely guaranteed the 20% down payment and not the entire obligation of Mabunay under the Construction Agreement. Since the value of the project's accomplishment already exceeded the said amount, respondent's obligation under the performance bond had been fully extinguished. As to the claim for alleged overpayment to Mabunay, respondent contended that it should not be credited against the 20% down payment which was already exhausted and such application by petitioner is tantamount to reviving an obligation that had been legally extinguished by payment. Respondent also set up a cross-claim against Mabunay who executed in its favor an Indemnity Agreement whereby Mabunay undertook to indemnify respondent for whatever amounts it may be adjudged liable to pay petitioner under the surety bond.

Both petitioner and respondent submitted their respective documentary and testimonial evidence. Mabunay failed to appear in the scheduled hearings and to present his evidence despite due notice to his counsel of record. The CIAC thus declared that Mabunay is deemed to have waived his right to present evidence.[15]

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10 Id. at 76-86.
11 Id. at 82.
12 Id. at 189-197.
13 Id. at 115-121, 132-136, 163-164.
14 Id at 165-183.
15 Id. at 211-212.

On February 2, 2010, the CIAC rendered its Decision[16] and made the following award:

> Accordingly, in view of our foregoing discussions and dispositions, the Tribunal hereby adjudges, orders and directs:
>
> 1. Respondents Mabunay and Utassco to jointly and severally pay claimant the following:
>
> a) P4,469,969.90, as liquidated damages, plus legal interest thereon at the rate of 6% per annum computed from the date of this decision up to the time this decision becomes final, and 12% per annum computed from the date this decision becomes final until fully paid, and
>
> b) P2,379,441.53 as unrecouped down payment plus interest thereon at the rate of 6% per annum computed from the date of this decision up to the time this decision becomes final, and 12% per annum computed from the date this decision becomes final until fully paid[.]
>
> It being understood that respondent Utassco's liability shall in no case exceed P8.4 million.
>
> 2. Respondent Mabunay to pay to claimant the amount of P98,435.89, which is respondent [Mabunay's] share in the arbitration cost claimant had advanced, with legal interest thereon from January 8, 2010 until fully paid.
>
> 3. Respondent Mabunay to indemnify respondent Utassco of the amounts respondent Utassco will have paid to claimant under this decision, plus interest thereon at the rate of 12% per annum computed from the date he is notified of such payment made by respondent Utassco to claimant until fully paid, and to pay Utassco P100,000.00 as attorney's fees.
>
> SO ORDERED.[17]

Dissatisfied, respondent filed in the CA a petition for review under Rule 43 of the 1997 Rules of Civil Procedure, as amended.

In the assailed decision, the CA agreed with the CIAC that the specific condition in the Performance Bond did not clearly state the limitation of the surety's liability. Pursuant to Article 1377[18] of the Civil Code, the CA said that the provision should be construed in favor of petitioner considering that the obscurely phrased provision was drawn up by respondent and Mabunay. Further, the appellate court stated that respondent could not possibly guarantee the down payment because it is not Mabunay who owed the down payment to petitioner but the other way around. Consequently, the completion by Mabunay of 31.39% of the construction would not lead to the extinguishment of respondent's liability. The ₱8.4 million was a limit on the

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16 Id. at 600-614.
17 Id. at 614 to 614-A.
18 ART. 1377. The interpretation of obscure words or stipulations in a contract shall not favor the party who caused the obscurity.

amount of respondent's liability and not a limitation as to the obligation or undertaking it guaranteed.

However, the CA reversed the CIAC's ruling that Mabunay had incurred delay which entitled petitioner to the stipulated liquidated damages and unrecouped down payment. Citing *Aerospace Chemical Industries, Inc. v. Court of Appeals*,[19] the appellate court said that not all requisites in order to consider the obligor or debtor in default were present in this case. It held that it is only from December 24, 2008 (completion date) that we should reckon default because the Construction Agreement provided only for delay in the completion of the project and not delay on a monthly basis using the work schedule approved by petitioner as the reference point. Hence, petitioner's termination of the contract was premature since the delay in this case was merely speculative; the obligation was not yet demandable.

The dispositive portion of the CA Decision reads:

> **WHEREFORE**, premises considered, the instant petition for review is **GRANTED**. The assailed Decision dated 13 January 2010 rendered by the CIAC Arbitral Tribunal in CIAC Case No. 03-2009 is hereby **REVERSED and SET ASIDE**. Accordingly, the Writ of Execution dated 24 November 2010 issued by the same tribunal is hereby **ANNULLED and SET ASIDE**.
>
> SO ORDERED.[20]

Petitioner moved for reconsideration of the CA decision while respondent filed a motion for partial reconsideration. Both motions were denied.

The Issues

Before this Court petitioner seeks to reverse the CA insofar as it denied petitioner's claims under the Performance Bond and to reinstate in its entirety the February 2, 2010 CIAC Decision. Specifically, petitioner alleged that –

> A. THE COURT OF APPEALS SERIOUSLY ERRED IN NOT HOLDING THAT THE ALTERNATIVE DISPUTE RESOLUTION ACT AND THE SPECIAL RULES ON ALTERNATIVE DISPUTE RESOLUTION HAVE STRIPPED THE COURT OF APPEALS OF JURISDICTION TO REVIEW ARBITRAL AWARDS.
>
> B. THE COURT OF APPEALS SERIOUSLY ERRED IN REVERSING THE ARBITRAL AWARD ON AN ISSUE THAT WAS NOT RAISED IN THE ANSWER. NOT IDENTIFIED IN THE TERMS OF REFERENCE, NOT ASSIGNED AS AN ERROR, AND NOT ARGUED IN ANY OF THE PLEADINGS FILED BEFORE THE COURT.

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19 G.R. No. 108129, September 23, 1999, 315 SCRA 92.

20 *Rollo*, p. 67.

C. THE COURT OF APPEALS SERIOUSLY ERRED IN RELYING ON THE CASE OF *AEROSPACE CHEMICAL INDUSTRIES, INC. v. COURT OF APPEALS*, 315 SCRA 94, WHICH HAS NOTHING TO DO WITH CONSTRUCTION AGREEMENTS.[21]

Our Ruling

On the procedural issues raised, we find no merit in petitioner's contention that with the institutionalization of alternative dispute resolution under Republic Act (R.A.) No. 9285,[22] otherwise known as the Alternative Dispute Resolution Act of 2004, the CA was divested of jurisdiction to review the decisions or awards of the CIAC. Petitioner erroneously relied on the provision in said law allowing any party to a domestic arbitration to file in the Regional Trial Court (RTC) a petition either to confirm, correct or vacate a domestic arbitral award.

We hold that R.A. No. 9285 did not confer on regional trial courts jurisdiction to review awards or decisions of the CIAC in construction disputes. On the contrary, Section 40 thereof expressly declares that confirmation by the RTC is not required, thus:

> **SEC. 40.** ***Confirmation of Award.*** – The confirmation of a domestic arbitral award shall be governed by Section 23 of R.A. 876.
>
> A domestic arbitral award when confirmed shall be enforced in the same manner as final and executory decisions of the Regional Trial Court.
>
> The confirmation of a domestic award shall be made by the regional trial court in accordance with the Rules of Procedure to be promulgated by the Supreme Court.
>
> **A CIAC arbitral award need not be confirmed by the regional trial court to be executory as provided under E.O. No. 1008.** (Emphasis supplied.)

Executive Order (EO) No. 1008 vests upon the CIAC original and exclusive jurisdiction over disputes arising from, or connected with, contracts entered into by parties involved in construction in the Philippines, whether the dispute arises before or after the completion of the contract, or after the abandonment or breach thereof. By express provision of Section 19 thereof, the arbitral award of the CIAC is final and unappealable, except on questions of law, which are appealable to the Supreme Court. With the amendments introduced by R.A. No. 7902 and promulgation of the 1997 Rules of Civil Procedure, as amended, the CIAC was included in the enumeration of quasi-judicial agencies whose decisions or awards may be appealed to the CA in a petition for review under Rule 43. Such review of the CIAC award may involve either questions of fact, of law, or of fact and law.[23]

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21 Id. at 23.

22 Approved on April 2, 2004.

23 *Metro Construction, Inc. v. Chatham Properties, Inc.*, G.R. No. 141897, September 24, 2001, 365 SCRA 697, 718-719 & 794.

Petitioner misread the provisions of A.M. No. 07-11-08-SC (Special ADR Rules) promulgated by this Court and which took effect on October 30, 2009. Since R.A. No. 9285 explicitly excluded CIAC awards from domestic arbitration awards that need to be confirmed to be executory, said awards are therefore not covered by Rule 11 of the Special ADR Rules,[24] as they continue to be governed by EO No. 1008, as amended and the rules of procedure of the CIAC. The CIAC Revised Rules of Procedure Governing Construction Arbitration[25] provide for the manner and mode of appeal from CIAC decisions or awards in Section 18 thereof, which reads:

> SECTION 18.2 ***Petition for review.*** – A petition for review from a final award may be taken by any of the parties within fifteen (15) days from receipt thereof in accordance with the provisions of Rule 43 of the Rules of Court.

As to the alleged error committed by the CA in deciding the case upon an issue not raised or litigated before the CIAC, this assertion has no basis. Whether or not Mabunay had incurred delay in the performance of his obligations under the Construction Agreement was the very first issue stipulated in the Terms of Reference[26] (TOR), which is distinct from the issue of the extent of respondent's liability under the Performance Bond.

Indeed, resolution of the issue of delay was crucial upon which depends petitioner's right to the liquidated damages pursuant to the Construction Agreement. Contrary to the CIAC's findings, the CA opined that delay should be reckoned only after the lapse of the one-year contract period, and consequently Mabunay's liability for liquidated damages arises only upon the happening of such condition.

We reverse the CA.

Default or *mora* on the part of the debtor is the delay in the fulfillment of the prestation by reason of a cause imputable to the former. It is the non-fulfillment of an obligation with respect to time.[27]

Article 1169 of the Civil Code provides:

> ART. 1169. Those obliged to deliver or to do something incur in delay from the time the obligee judicially or extrajudicially demands from them the fulfillment of their obligation.
>
> x x x x

It is a general rule that one who contracts to complete certain work within a certain time is liable for the damage for not completing it within

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[24] A.M. No. 07-11-08-SC, effective October 30, 2009.

[25] As amended by CIAC Resolution Nos. 15-2006, 16-2006, 18-2006, 19-2006, 02-2007, 07-2007, 13-2007, 02-2008, and 03-2008, which took effect on December 15, 2005.

[26] *Rollo*, pp. 202-210.

[27] IV Arturo M. Tolentino, COMMENTARIES AND JURISPRUDENCE ON THE CIVIL CODE OF THE PHILIPPINES, 101 (1987 ed.).

such time, unless the delay is excused or waived.[28]

The Construction Agreement provides in Article 10 thereof the following conditions as to completion time for the project

> 1. The CONTRACTOR shall complete the works called for under this Agreement within ONE (1) YEAR or 365 Days reckoned from the 1st calendar day after signing of the Notice of Award and Notice to Proceed and receipt of down payment.
>
> 2. In this regard the CONTRACTOR shall submit a detailed work schedule for approval by OWNER within Seven (7) days after signing of this Agreement and full payment of 20% of the agreed contract price. Said detailed work schedule shall follow the general schedule of activities and shall serve as basis for the evaluation of the progress of work by CONTRACTOR.[29]

In this jurisdiction, the following requisites must be present in order that the debtor may be in default: (1) that the obligation be demandable and already liquidated; (2) that the debtor delays performance; and (3) that the creditor requires the performance judicially or extrajudicially.[30]

In holding that Mabunay has not *at all* incurred delay, the CA pointed out that the obligation to perform or complete the project was not yet demandable as of November 19, 2008 when petitioner terminated the contract, because the agreed completion date was still more than one month away (December 24, 2008). Since the parties contemplated delay in the completion of the entire project, the CA concluded that the failure of the contractor to catch up with schedule of work activities did not constitute delay giving rise to the contractor's liability for damages.

We cannot sustain the appellate court's interpretation as it is inconsistent with the terms of the Construction Agreement. Article 1374 of the Civil Code requires that the various stipulations of a contract shall be interpreted together, attributing to the doubtful ones that sense which may result from all of them taken jointly. Here, the work schedule approved by petitioner was intended, not only to serve as its basis for the payment of monthly progress billings, but also for evaluation of the progress of work by the contractor. Article 13.01 (g) (iii) of the Construction Agreement provides that the contractor shall be deemed in default if, among others, it had delayed without justifiable cause the completion of the project "by more than thirty (30) calendar days *based on official work schedule* duly approved by the OWNER."[31]

Records showed that as early as April 2008, or within four months

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28 17 Am Jur 2d §387, p. 832.

29 *Rollo*, p. 93.

30 *Santos Ventura Hocorma Foundation, Inc. v. Santos*, 484 Phil. 447, 457 (2004), citing IV Arturo M. Tolentino, COMMENTARIES AND JURISPRUDENCE ON THE CIVIL CODE OF THE PHILIPPINES, 102 (1987 ed.). See also *Philippine Export and Foreign Loan Guarantee Corporation v. V.P. Eusebio Construction, Inc.*, G.R. No. 140047, July 13, 2004, 434 SCRA 202, 218-219.

31 *Rollo*, p. 94.

after Mabunay commenced work activities, the project was already behind schedule for reasons not attributable to petitioner. In the succeeding months, Mabunay was still unable to catch up with his accomplishment even as petitioner constantly advised him of the delays, as can be gleaned from the following notices of delay sent by petitioner's engineer and construction manager, Engr. Sheila N. Botardo:

> April 30, 2008
>
> Seven Shades of Blue
> Boracay Island
> Malay, Aklan
>
> Attention : Mr. Martin Mabunay
> General Manager
>
> Thru : Engr. Reynaldo Gapasin
>
> Project : Villa Beatriz
>
> Subject : Notice of Delay
>
> Dear Mr. Mabunay:
>
> This is to formalize our discussion with your Engineers during our meeting last April 23, 2008 regarding the delay in the implementation of major activities based on your submitted construction schedule. Substantial delay was noted in concreting works that affects your roof framing that should have been 40% completed as of this date. This delay will create major impact on your over-all schedule as the finishing works will all be dependent on the enclosure of the building.
>
> In this regard, we recommend that you prepare a catch-up schedule and expedite the delivery of critical materials on site. We would highly appreciate if you could attend our next regular meeting so we could immediately address this matter. Thank you.
>
> Very truly yours,
>
> Engr. Sheila N. Botardo
> Construction Manager – LMI/FEPI[32]
>
> October 15, 2008
>
> x x x x
>
> Dear Mr. Mabunay,
>
> We have noticed continuous absence of all the Engineers that you have assigned on-site to administer and supervise your contracted work. For the past two (2) weeks[,] your company does not have a Technical Representative manning the jobsite considering the critical activities that are in progress and the delays in schedule that you have already incurred. In this regard, we would highly recommend the immediate replacement of

[32] Id. at 104.

your Project Engineer within the week.

We would highly appreciate your usual attention on this matter.

x x x x[33]

November 5, 2008

x x x x

Dear Mr. Mabunay,

This is in reference to your discussion during the meeting with Mr. Joohan Lee last October 30, 2008 regarding the construction of the Field Office and Stock Room for Materials intended for Villa Beatriz use only. We understand that you have committed to complete it November 5, 2008 but as of this date there is no improvement or any ongoing construction activity on the said field office and stockroom.

We are expecting deliveries of Owner Supplied Materials very soon, therefore, this stockroom is badly needed. We will highly appreciate if this matter will be given your immediate attention.

Thank you.

x x x x[34]

November 6, 2008

x x x x

Dear Mr. Mabunay,

We would like to call your attention regarding the decrease in your manpower assigned on site. We have observed that for the past three (3) weeks instead of increasing your manpower to catch up with the delay it was reduced to only 8 workers today from an average of 35 workers in the previous months.

Please note that based on your submitted revised schedule you are already delayed by approximately 57% and this will worsen should you not address this matter properly.

We are looking forward for *[sic]* your cooperation and continuous commitment in delivering this project as per contract agreement.

x x x x[35]

Subsequently, a joint inspection and evaluation was conducted with the assistance of the architects and engineers of petitioner and Mabunay and it was found that as of November 14, 2008, the project was only 31.39% complete and that the uncompleted portion was 68.61% with an estimated

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33 Id. at 106.
34 Id. at 107.
35 Id. at 108.

value per Construction Agreement as ₱27,880,419.52. Instead of doubling his efforts as the scheduled completion date approached, Mabunay did nothing to remedy the delays and even reduced the deployment of workers at the project site. Neither did Mabunay, at anytime, ask for an extension to complete the project. Thus, on November 19, 2008, petitioner advised Mabunay of its decision to terminate the contract on account of the tremendous delay the latter incurred. This was followed by the claim against the Performance Bond upon the respondent on December 18, 2008.

Petitioner's claim against the Performance Bond included the liquidated damages provided in the Construction Agreement, as follows:

> ARTICLE 12 – LIQUIDATED DAMAGES:
>
> 12.01 Time is of the essence in this Agreement. Should the CONTRACTOR **fail to complete the PROJECT within the period stipulated herein or within the period of extension granted by the OWNER, plus One (1) Week grace period**, without any justifiable reason, the CONTRACTOR hereby agrees –
>
> a. The CONTRACTOR shall pay the OWNER liquidated damages equivalent to One Tenth of One Percent (1/10 of 1%) of the Contract Amount for each day of delay after any and all extensions and the One (1) week Grace Period until completed by the CONTRACTOR.
>
> b. The CONTRACTOR, even after paying for the liquidated damages due to unexecuted works and/or delays shall not relieve it of the obligation to complete and finish the construction.
>
> Any sum which maybe payable to the OWNER for such loss may be deducted from the amounts retained under Article 9 or retained by the OWNER when the works called for under this Agreement have been finished and completed.
>
> Liquidated Damage[s] payable to the OWNER shall be automatically deducted from the contractors collectibles without prior consent and concurrence by the CONTRACTOR.
>
> 12.02 To give full force and effect to the foregoing, the CONTRACTOR hereby, without necessity of any further act and deed, authorizes the OWNER to deduct any amount that may be due under Item (a) above, from any and all money or amounts due or which will become due to the CONTRACTOR by virtue of this Agreement and/or to collect such amounts from the Performance Bond filed by the CONTRACTOR in this Agreement.[36] (Emphasis supplied.)

Liability for liquidated damages is governed by Articles 2226 to 2228 of the Civil Code, which provide:

> ART. 2226. Liquidated damages are those agreed upon by the parties to a contract, to be paid in case of breach thereof.

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[36] Id. at 93-94.

> ART. 2227. Liquidated damages, whether intended as an indemnity or a penalty, shall be equitably reduced if they are iniquitous or unconscionable.
>
> ART. 2228. When the breach of the contract committed by the defendant is not the one contemplated by the parties in agreeing upon the liquidated damages, the law shall determine the measure of damages, and not the stipulation.

A stipulation for liquidated damages is attached to an obligation in order to ensure performance and has a double function: (1) to provide for liquidated damages, and (2) to strengthen the coercive force of the obligation by the threat of greater responsibility in the event of breach.[37] The amount agreed upon answers for damages suffered by the owner due to delays in the completion of the project.[38] As a precondition to such award, however, there must be proof of the fact of delay in the performance of the obligation.[39]

Concededly, Article 12.01 of the Construction Agreement mentioned only the failure of the contractor to complete the project within the stipulated period or the extension granted by the owner. However, this will not defeat petitioner's claim for damages nor respondent's liability under the Performance Bond. Mabunay was clearly in default considering the dismal percentage of his accomplishment (32.38%) of the work he contracted on account of delays in executing the scheduled work activities and repeated failure to provide sufficient manpower to expedite construction works. The events of default and remedies of the Owner are set forth in Article 13, which reads:

> **ARTICLE 13 – DEFAULT OF CONTRACTOR:**
>
> 13.01 Any of the following shall constitute an Event of Default on the [part] of the CONTRACTOR.
>
> x x x x
>
> g. In case the CONTRACTOR has done any of the following:
>
> (i.) has abandoned the Project
>
> (ii.) without reasonable cause, has failed to commence the construction or has suspended the progress of the Project for twenty-eight days
>
> (iii.) without justifiable cause, **has delayed the completion of the Project by more than thirty (30) calendar days based on official work schedule duly approved by the OWNER**

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37 *Atlantic Erectors, Inc. v. Court of Appeals*, G.R. No. 170732, October 11, 2012, 684 SCRA 55, 65, citing *Philippine Charter Insurance Corporation v. Petroleum Distributors & Service Corporation*, G.R. No. 180898, April 18, 2012, 670 SCRA 166, 177 and *Filinvest Land, Inc. v. Court of Appeals*, G.R. No. 138980, September 20, 2005, 470 SCRA 260, 269.

38 Id., citing *H.L. Carlos Construction, Inc. v. Marina Properties Corporation*, 466 Phil. 182, 205 (2004).

39 Id., citing *Empire East Land Holdings, Inc. v. Capitol Industrial Construction Groups, Inc.*, G.R. No. 168074, September 26, 2008, 566 SCRA 473, 489.

> (iv.) despite previous written warning by the OWNER, is **not executing the construction works in accordance with the Agreement** or is **persistently or flagrantly neglecting to carry out its obligations under the Agreement**.
>
> (v.) has, to the detriment of good workmanship or in defiance of the Owner's instructions to the contrary, sublet any part of the Agreement.
>
> 13.02 If the CONTRACTOR has committed any of the above reasons cited in Item 13.01, the OWNER may after giving fourteen (14) calendar days notice in writing to the CONTRACTOR, enter upon the site and expel the CONTRACTOR therefrom without voiding this Agreement, or releasing the CONTRACTOR from any of its obligations, and liabilities under this Agreement. Also without diminishing or affecting the rights and powers conferred on the OWNER by this Agreement and the OWNER may himself complete the work or may employ any other contractor to complete the work. If the OWNER shall enter and expel the CONTRACTOR under this clause, the OWNER shall be entitled to **confiscate the performance bond of the CONTRACTOR to compensate for all kinds of damages the OWNER may suffer.** All expenses incurred to finish the Project shall be charged to the CONTRACTOR and/or his bond. Further, the OWNER shall not be liable to pay the CONTRACTOR until the cost of execution, damages for the delay in the completion, if any, and all; other expenses incurred by the OWNER have been ascertained which amount shall be deducted from any money due to the CONTRACTOR on account of this Agreement. The CONTRACTOR will not be compensated for any loss of profit, loss of goodwill, loss of use of any equipment or property, loss of business opportunity, additional financing cost or overhead or opportunity losses related to the unaccomplished portions of the work.[40] (Emphasis supplied.)

As already demonstrated, the contractor's default in this case pertains to his failure to substantially perform the work on account of tremendous delays in executing the scheduled work activities. Where a party to a building construction contract fails to comply with the duty imposed by the terms of the contract, a breach results for which an action may be maintained to recover the damages sustained thereby, and of course, a breach occurs where the contractor inexcusably fails to perform substantially in accordance with the terms of the contract.[41]

The plain and unambiguous terms of the Construction Agreement authorize petitioner to confiscate the Performance Bond to answer for all kinds of damages it may suffer as a result of the contractor's failure to complete the building. Having elected to terminate the contract and expel the contractor from the project site under Article 13 of the said Agreement, petitioner is clearly entitled to the proceeds of the bond as indemnification for damages it sustained due to the breach committed by Mabunay. Such stipulation allowing the confiscation of the contractor's performance bond partakes of the nature of a penalty clause. A penalty clause, expressly

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[40] *Rollo*, pp. 94-95.
[41] 13 Am Jur 2d §72, p. 73.

recognized by law, is an accessory undertaking to assume greater liability on the part of the obligor in case of breach of an obligation. It functions to strengthen the coercive force of obligation and to provide, in effect, for what could be the liquidated damages resulting from such a breach. The obligor would then be bound to pay the stipulated indemnity without the necessity of proof on the existence and on the measure of damages caused by the breach. It is well-settled that so long as such stipulation does not contravene law, morals, or public order, it is strictly binding upon the obligor.[42]

Respondent, however, insists that it is not liable for the breach committed by Mabunay because by the terms of the surety bond it issued, its liability is limited to the performance by said contractor to the extent equivalent to 20% of the down payment. It stresses that with the 32.38% completion of the project by Mabunay, its liability was extinguished because the value of such accomplishment already exceeded the sum equivalent to 20% down payment (₱8.4 million).

The appellate court correctly rejected this theory of respondent when it ruled that the Performance Bond guaranteed the full and faithful compliance of Mabunay's obligations under the Construction Agreement, and that nowhere in law or jurisprudence does it state that the obligation or undertaking by a surety may be apportioned.

The pertinent portions of the Performance Bond provide:

The conditions of this obligation are as follows:

> Whereas the JPLUS ASIA, requires the principal SEVEN SHADES OF BLUE CONSTRUCTION AND DEVELOPMENT, INC. to post a bond of the abovestated sum **to guarantee 20% down payment for the construction** of Building 25 (Villa Beatriz) 72-Room Condotel, The Lodgings inside Fairways and Bluewater, Boracay Island, Malay, Aklan.
>
> Whereas, said contract required said Principal to give a good and sufficient bond in the above-stated sum **to secure the full and faithful performance on his part of said contract.**
>
> *It is a special provision of this undertaking that the liability of the surety under this bond shall in no case exceed the sum of* P8,400,000.00 *Philippine Currency.*
>
> Now, Therefore, if the Principal shall well and truly perform and fulfill all the undertakings, covenants, terms, conditions and agreements stipulated in said contract, then this obligation shall be null and void; otherwise to remain in full force and effect.[43] (Emphasis supplied.)

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42 *Suatengco v. Reyes*, G.R. No. 162729, December 17, 2008, 574 SCRA 187, 194, citing *Ligutan v. Court of Appeals*, G.R. No. 138677, February 12, 2002, 376 SCRA 560, 567-568.

43 *Rollo*, p. 100.

While the above condition or specific guarantee is unclear, the rest of the recitals in the bond unequivocally declare that it secures the full and faithful performance of Mabunay's obligations under the Construction Agreement with petitioner. By its nature, a performance bond guarantees that the contractor will perform the contract, and usually provides that if the contractor defaults and fails to complete the contract, the surety can itself complete the contract or pay damages up to the limit of the bond.[44] Moreover, the rule is that if the language of the bond is ambiguous or uncertain, it will be construed most strongly against a compensated surety and in favor of the obligees or beneficiaries under the bond, in this case petitioner as the Project Owner, for whose benefit it was ostensibly executed.[45]

The imposition of interest on the claims of petitioner is likewise in order. As we held in *Commonwealth Insurance Corporation v. Court of Appeals*[46]

> Petitioner argues that it should not be made to pay interest because its issuance of the surety bonds was made on the condition that its liability shall in no case exceed the amount of the said bonds.
>
> We are not persuaded. Petitioner's argument is misplaced.
>
> Jurisprudence is clear on this matter. As early as *Tagawa vs. Aldanese and Union Gurantee Co.* and reiterated in *Plaridel Surety & Insurance Co., Inc. vs. P.L. Galang Machinery Co., Inc.*, and more recently, in *Republic vs. Court of Appeals and R & B Surety and Insurance Company, Inc.*, we have sustained the principle that **if a surety upon demand fails to pay, he can be held liable for interest, even if in thus paying, its liability becomes more than the principal obligation. The increased liability is not because of the contract but because of the default and the necessity of judicial collection.**
>
> Petitioner's liability under the suretyship contract is different from its liability under the law. There is no question that as a surety, petitioner should not be made to pay more than its assumed obligation under the surety bonds. However, it is clear from the above-cited jurisprudence that petitioner's liability for the payment of interest is not by reason of the suretyship agreement itself but because of the delay in the payment of its obligation under the said agreement.[47] (Emphasis supplied; citations omitted.)

WHEREFORE, the petition for review on certiorari is **GRANTED.** The Decision dated January 27, 2011 and Resolution dated December 8, 2011 of the Court of Appeals in CA-G.R. SP No. 112808 are hereby **REVERSED** and **SET ASIDE.**

The Award made in the Decision dated February 2, 2010 of the

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44 17 Am Jur 2d §1, p. 192.
45 17 Am Jur 2d §3, p. 193.
46 466 Phil. 104 (2004).
47 Id. at 112-113.

Construction Industry Arbitration Commission is hereby **REINSTATED with the following MODIFICATIONS**:

> "Accordingly, in view of our foregoing discussions and dispositions, the Tribunal hereby adjudges, orders and directs:
>
> 1) Respondent Utassco to pay to petitioner J Plus Asia Development Corporation the full amount of the Performance Bond, P8,400,000.00, pursuant to Art. 13 of the Construction Agreement dated December 24, 2007, with interest at the rate of 6% per annum computed from the date of the filing of the complaint until the finality of this decision, and 12% per annum computed from the date this decision becomes final until fully paid; and
>
> 2) Respondent Mabunay to indemnify respondent Utassco of the amounts respondent Utassco will have paid to claimant under this decision, plus interest thereon at the rate of 12% per annum computed from the date he is notified of such payment made by respondent Utassco to claimant until fully paid, and to pay Utassco P100,000.00 as attorney's fees.
>
> SO ORDERED."

With the above modifications, the Writ of Execution dated November 24, 2010 issued by the CIAC Arbitral Tribunal in CIAC Case No. 03-2009 is hereby **REINSTATED and UPHELD**.

No pronouncement as to costs.

SO ORDERED.

MARTIN S. VILLARAMA, JR.
Associate Justice

WE CONCUR:

MARIA LOURDES P. A. SERENO
Chief Justice
Chairperson

TERESITA J. LEONARDO-DE CASTRO
Associate Justice

LUCAS P. BERSAMIN
Associate Justice

BIENVENIDO L. REYES
Associate Justice

CERTIFICATION

Pursuant to Section 13, Article VIII of the 1987 Constitution, I certify that the conclusions in the above Decision had been reached in consultation before the case was assigned to the writer of the opinion of the Court's Division.

MARIA LOURDES P. A. SERENO
Chief Justice