



Republic of the Philippines
Supreme Court
Manila

THIRD DIVISION

**PHILIPPINE RECLAMATION
AUTHORITY (Formerly known as the
PUBLIC ESTATES AUTHORITY),**

Petitioner,

G.R. No. 174665

Present:

- versus -

VELASCO, JR., *J.*, *Chairperson*,
ABAD,
MENDOZA,
REYES,* and
LEONEN, *JJ.*

ROMAGO, INCORPORATED,
Respondent.

X ----- X

ROMAGO, INCORPORATED,
Petitioner,

G.R. No. 175221

- versus -

**PHILIPPINE RECLAMATION
AUTHORITY (Formerly PUBLIC
ESTATES AUTHORITY),**
Respondent.

Promulgated:

SEP 18 2013

McCloskey

X ----- X

DECISION

ABAD, *J.*:

These cases pertain to the defense of novation by virtue of the debtor's assignment to a third party of its contractual liability to the creditor.

* Designated Acting Member, in lieu of Associate Justice Diosdado M. Peralta, per Special Order 1541-A dated September 9, 2013.

The Facts and the Case

In order to convert former military reservations and installations to productive use and raise funds out of the sale of portions of the country's military camps,¹ in 1992 Congress enacted Republic Act 7227,² creating the Bases Conversion and Development Authority (BCDA). Pursuant to this law, the President issued Executive Order 40,³ Series of 1992, setting aside portions of Fort Bonifacio in Taguig, Metro Manila, for the Heritage Park Project, aimed at converting a 105-hectare land into a world class memorial park for the purpose of generating funds for the BCDA.⁴

On August 9, 1993 the BCDA entered into a Memorandum of Agreement⁵ (MOA) with the Philippine Reclamation Authority (PRA), formerly the Public Estates Authority, designating it as the Project Manager. On September 9, 1994 the BCDA, PRA, and the Philippine National Bank (PNB) executed a Pool Formation Trust Agreement (PFTA)⁶ under which BCDA, as project owner, was to issue Heritage Park Investment Certificates that would evidence the holders' right to the perpetual use and care of specific interment plots. The PFTA designated PRA as Project Manager, tasked with the physical development of the park. The PNB was to act as trustee for the Heritage Park securitization.⁷

After public bidding, the PRA awarded the outdoor electrical and lighting works for the park to respondent Romago, Inc. (Romago) with which it entered into a Construction Agreement on March 18, 1996 for the contract price of ₱176,326,794.10.⁸ On receipt of the PRA's notice to proceed,⁹ Romago immediately began construction works.¹⁰

Meanwhile, the parties to the PFTA organized the Heritage Park Management Corporation (HPMC) to take over the management of the project.¹¹ On February 24, 2000 the Chairman of HPMC Board of Trustees, Mr. Rogelio L. Singson, sent a notice of termination of management to then PRA General Manager Carlos P. Doble with a demand for the turnover of the park to HPMC.¹² The letter reads:

¹ Section 2 of Republic Act 7227.

² Entitled as "An Act Accelerating the Conversion of Military Reservations Into Other Productive Uses, Creating the Bases Conversion and Development Authority For This Purpose, Providing Funds Therefor and For Other Purposes."

³ Issued on December 8, 1992.

⁴ Section 3 of Executive Order 40, Series of 1992.

⁵ *Rollo* (G.R. 174665), pp. 70-83.

⁶ *Id.* at 226-270.

⁷ Whereas Clause of PFTA, *id.* at 232.

⁸ *Id.* at 128.

⁹ *Id.* at 438.

¹⁰ *Id.*

¹¹ Section 11.01, Article XI of the PFTA, *id.* at 263.

¹² *Rollo* (G.R. 174665), p. 198.

Pursuant to Article 11 of the Pool Formation Trust Agreement (PFTA), the certificate holders of the Heritage Park Management Corporation (HPMC) duly elected its Board of Trustees at the 03 January 2000 meeting held at the BCDA Corporate Center. Attached is a copy of the Secretary's Certificate attesting to said election of the HPMC Board of Trustees.

Section 11.07 of the PFTA provides that upon the election of the Board of Trustees, the PNB shall turnover to the Board all its functions and responsibilities, and all documents in its custody, including all Heritage Park Accounts, except the General Fund, which will go to BCDA. Upon such turnover and upon the complete and faithful performance by PNB and [PRA] of their respective obligations under this Agreement, the respective obligations of [PRA] and PNB under this Agreement shall be deemed terminated. *[PRA] shall turnover to the Board of Trustees all the documents and equipment it has in its possession relating to the Project and the Park, including the computer hardware and software pertaining to the geographical information system of the Park."*

Pursuant to the foregoing provision, we hereby formally advise you of the termination of [PRA's] obligations, duties and responsibilities as Project Manager under the PFTA, effective upon receipt of this letter. We also formally request for [PRA] to turn over, within fifteen (15) days from receipt of this letter, the documents and equipment relating to the Heritage Park Project, including the computer hardware and software in [PRA's] possession pertaining to the geographical information system of the Park.¹³

The PRA lost no time in informing Romago of the consequent termination of its services. Thus, it wrote Romago a letter¹⁴ on March 13, 2000:

As a consequence of the assumption of functions, duties and responsibilities by the Heritage Park Management Corporation, as provided for under the provisions of the Pool Formation Trust Agreement, we are constrained to assign the Electrical Works contract entered with you on March 18, 1996 including all supplemental agreements relative thereto, effective March 18, 2000 in favor of the Heritage Park Management Corporation. The formal turnover on March 17, 2000 by [PRA] to the Heritage Park Management Corporation of all its obligations, duties and responsibilities, and all documents relating to the Heritage Park Project, was made pursuant to the attached letter of the Chairman of HPMC Board of Trustees, Mr. Rogelio L. Singson to the [PRA], received by us on March 02, 2000.

By virtue of this assignment, all the contractual functions, responsibilities and liabilities, if any, as well as any cause of action for or against [PRA] shall hereafter accrue to and devolve upon the assignee hereof.

¹³ Id.

¹⁴ Id. at 197.

Please be guided accordingly.¹⁵

Because the HPMC refused to recognize the PRA's contract with it, on March 17, 2004 Romago filed with the Construction Industry Arbitration Commission (CIAC) a complaint,¹⁶ docketed as CIAC Case 18-2004, seeking to collect its claims totalling ₱24,467,621.64, plus interest from the PRA, HPMC, and Rosehills Memorial Management (Phils.), Inc. (RMMI). Romago claimed that it won the bidding for the construction of the electrical and lighting facilities at the Heritage Park for ₱181,779,800.00¹⁷ but PRA deducted 3% from the bid amount, reducing the contract price to ₱176,326,794.10.¹⁸

Because of problems encountered with illegal settlers, only around 60 of the 105-hectare park was delivered to Romago for lighting work, reducing the contract price to ₱101,083,636.16.¹⁹ But this amount was adjusted to ₱109,330,032.81 due to PRA variation orders.²⁰ Although Romago completed 96.15% of the works, it claimed that the PRA paid it only ₱82,929,577.22 instead of the ₱105,120,826.50 due it.²¹ Romago also claimed that it should be reimbursed the ₱9,336,054.15 retention money that it posted since its services had already been terminated and since it had substantially completed the Heritage Park Project.²²

Romago also sought payment of the additional costs and expenses that it incurred by reason of PRA's delays in turning over the project area, in delivering the owner-supplied equipment, and in solving the security problems at the worksite. These included price escalation of materials and supplies, at ₱857,799.10; and extended overhead costs, at ₱10,051,870.61.²³ And, for mobilizations costs that it spent preparing for works on the entire 105-hectare project area, Romago sought additional payment of ₱7,524,315.79 plus interest of ₱517,923.74 from April 12, 1999 to May 31, 1999 or a total of ₱8,042,239.53. It also claimed proportionate refund of ₱2,327,107.97 out of the 3% discount applied to its original bid²⁴ and ₱420,944.02 in damages for the unceremonious termination of its services.²⁵

¹⁵ Id.

¹⁶ *Rollo* (G.R. 175221), pp. 97-102.

¹⁷ *Rollo* (G.R. 174665), p. 200.

¹⁸ Id. at 128, 202.

¹⁹ Id. at 203.

²⁰ Id.

²¹ Id. Per Romago's Complaint, it valued 96.15% of its work accomplishment at ₱105,120,592.60. However, the amount should be ₱105,120,826.50 computed as follows: Adjusted contract price of ₱109,330,032.81 x 96.15 work accomplishment = ₱105,120,826.50.

²² Id.

²³ Id. at 98-99.

²⁴ Id. at 99.

²⁵ Id.

Romago admitted, however, owing the PRA ₱15,475,835.42 in unrecouped prepaid materials and ₱12,286,795.12 in unrecouped down payment.²⁶

In its answer, the PRA denied liability, claiming that it entered into the construction agreement with Romago after its approval by the Heritage Park Executive Committee, the policy-making and governing body of the Heritage Park Project. The PRA merely processed and recommended payment of all the works done. The money came from the project's Construction and Development Fund that PRA did not control. PNB acted as trustee of the fund under the PFTA. Since these funds had all been turned over to the HPMC when the latter came into being, Romago should not address its claims to PRA.²⁷

Rather than answer the complaint, the HPMC and RMMI moved to dismiss it, claiming that CIAC had no jurisdiction over them since they never agreed to arbitration.²⁸ Additionally, the HPMC said that the PRA's turnover of the Heritage Park project to it did not amount to assignment of the PRA's liabilities under the construction agreement. Further, its termination of the PRA's authority over the project carried with it the termination of any Construction Agreement that the PRA entered into.

For its part, RMMI averred that it was merely the undertaker at the Heritage Park, tasked with providing services for embalming, burial, cremation, and other activities for the care of the dead.²⁹

On July 22, 2004 the CIAC issued an order dropping RMMI as respondent but denying the HPMC's motion to dismiss the case against it.³⁰ The HPMC elevated the CIAC order to the Court of Appeals (CA) by special civil action of *certiorari* and prohibition in CA-G.R. SP 86342.

Meantime, after due proceedings, on October 22, 2004 the CIAC rendered a decision,³¹ holding the PRA and the HPMC jointly and severally liable to Romago for the following amounts:

The unpaid balance of the 96.15%	
accomplishment -----	₱22,191,249.38
Interest from 15 May 2002 to 31	
January 2004 at 6% per annum -----	2,276,372.31

²⁶ Id. at 100.

²⁷ *Rollo* (G.R. 174665), pp. 216-223.

²⁸ Id. at 657.

²⁹ Id.

³⁰ Id. at 657-658.

³¹ Id. at 650-668.

Plus:

1.1.1 – Retention Charges -----	₱9,336,054.15
1.1.2 – Price Escalation -----	775,793.55
1.1.3 – Damages for Closure of Area ----	8,042,239.53
1.1.4 – Reimbursement for Pro-rata discount -----	(not entitled)
1.1.5 – Damages for Stoppage of Works	420,944.02
Sub-Total -----	₱18,575,031.25

Less:

Unrecouped prepaid materials and unrecouped downpayment -----	27,762,642.54
Actual Damages Due -----	₱15,280,012.35

Plus:

Additional 6% interest from February 1, 2004 to August 31, 2004 on the ₱15,280,012.35 -----	534,800.43
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Costs of Arbitration:

Filing Fee -----	₱26,834.39
Administrative Fee -----	28,164.39
Arbitrator's Fees -----	316,296.95
ADF -----	25,323.99
Total Cost of Arbitration -----	₱396,608.73

Total Award ----- ₱16,211,421.51³²

Not satisfied with the CIAC decision, the PRA filed a petition for review of the same with the CA in CA-G.R. SP 88059.

Meantime on February 18, 2005 the CA rendered a Decision in CA-G.R. SP 86342, dismissing Romago's complaint before the CIAC against the HPMC on the ground that the latter did not have an arbitration agreement with Romago.³³

On December 20, 2005 the CA rendered a Decision³⁴ in CA-G.R. SP 88059, the main case, finding that the unpaid accomplishment of Romago should be reduced from ₱22,191,249.33 to ₱18,641,208.89, and that interests on the damages awarded to Romago arising from the reduction in project area and on its unpaid accomplishment from May 15, 2002 to January 31, 2004 should be deleted, therefore entitling it to actual damages in the amount of ₱8,935,673.86³⁵ plus interest from February 1, 2004 to August 31, 2004 and the costs of arbitration.

³² Id. at 663, 667.

³³ CA *rollo*, pp. 744-767.

³⁴ Penned by Associate Justice Portia Aliño-Hormachuelos and concurred in by Associate Justices Mariano C. Del Castillo (now a member of the Court) and Magdangal M. de Leon, *rollo* (G.R. 175221), pp. 6-18.

³⁵ Id. at 12. ₱9,336,054.15 (retention charges) + ₱775,793.55 (price escalation) + ₱7,524,315.79 (damages for closure of area less interests) + ₱420,944.02 (damages for stoppage of works) + ₱18,641,208.89 (unpaid accomplishment) less ₱27,762,642.54 (unrecouped prepaid materials and downpayment).

The CA rejected the PRA's argument that it can no longer be held liable to Romago after turning over and assigning the project, including all its duties and obligations relating to it, to the HPMC. Romago was not a party to the PFTA and it did not give consent to the PRA's supposed assignment of its obligations to the HPMC.

The PRA and Romago separately moved for reconsideration of the decision but the CA denied both motions in its August 24, 2006 Resolution.³⁶ Undeterred, both parties filed separate petitions for review before this Court in G.R. 174665 for the PRA and in G.R. 175221 for Romago.

The Issues Presented

These consolidated cases present the following issues:

1. Whether or not the CA erred in holding the PRA still liable to Romago under the Construction Agreement despite the subsequent turnover of the Heritage Park Project to the HPMC; and
2. Whether or not the CA erred in reducing the CIAC award for actual damages to Romago to just ₱8,935,673.86.

The Rulings of the Court

The PRA claims that its liability under its contract with Romago had been extinguished by novation when it assigned all its obligations to the HPMC pursuant to the provisions of the PFTA. The PRA insists that the CA erroneously applied to the case the 2001 ruling of the Court in *Public Estates Authority v. Uy*³⁷ that also involved the Heritage Park Project. Uy dealt only with the PRA and the HPMC came into the picture only after the case has been filed. Here, while Romago first dealt with the PRA, it eventually dealt with the HPMC before the construction company can finish the contracted works, evidencing novation of parties.

In novation, a subsequent obligation extinguishes a previous one through substitution either by changing the object or principal conditions, by substituting another in place of the debtor, or by subrogating a third person into the rights of the creditor.³⁸ Novation requires (a) the existence of a previous valid obligation; (b) the agreement of all parties to the new

³⁶ Id. at 19-22.

³⁷ 423 Phil. 407, 418 (2001).

³⁸ *Philippine Savings Bank v. Spouses Mañalac, Jr.*, 496 Phil. 671, 686 (2005).

contract; (c) the extinguishment of the old contract; and (d) the validity of the new one.³⁹

There cannot be novation in this case since the proposed substituted parties did not agree to the PRA's supposed assignment of its obligations under the contract for the electrical and light works at Heritage Park to the HPMC. The latter definitely and clearly rejected the PRA's assignment of its liability under that contract to the HPMC. Romago tried to follow up its claims with the HPMC, not because of any new contract it entered into with the latter, but simply because the PRA told it that the HPMC would henceforth assume the PRA's liability under its contract with Romago.

Besides, Section 11.07 of the PFTA makes it clear that the termination of the PRA's obligations is conditioned upon the turnover of documents, equipment, computer hardware and software on the geographical information system of the Park; and the completion and faithful performance of its respective duties and responsibilities under the PFTA. More importantly, Section 11.07 did not say that the HPMC shall, thereafter, assume the PRA's obligations. On the contrary, Section 7.01 of the PFTA recognizes that contracts that the PRA entered into in its own name and makes it liable for the same. Thus:

Section 7.01. Liability of BCDA and [PRA]. BCDA and [PRA] shall be liable in accordance herewith only to the extent of the obligations specifically undertaken by BCDA and [PRA] herein and any other documents or agreements relating to the Project, and in which they are parties.⁴⁰

Romago claims that the CA award should be increased to ₱13,598,139.24 based on the detailed account of expenses and cash payments as of December 31, 2005 that it submitted. But the Court cannot agree. Engineer J. R. Milan testified that Romago received ₱86,479,617.61 out of ₱105,120,826.50 worth of work that it accomplished, thereby leaving a deficiency of only ₱18,641,208.89. Thus:

ATTY. S.B. GARCIA:

Mr. Witness, from the time you became the Project Manager of Heritage Park Project up to the time it turned over its responsibilities to HPMC, can you recall how much [PRA] already paid to Romago? You can refer to any documents we have now with you for recollection.

ENGR. J.R. MILLAN:

Based on progress Report No. 50, which was submitted by the Managing Consultant of Robert Espiritu, the accomplishment as of

³⁹ *Spouses Bautista v. Pilar Development Corporation*, 371 Phil. 533, 541 (1999).

⁴⁰ *Rollo* (G.R. 174665), p. 252.

February 29, 2000, the amount disbursed as of Billing no. 14A is ₱86,479,617.61.

ATTY. S.B. GARCIA:

What document again are you referring to, Mr. Witness?

ENGR. J.R. MILLAN:

This is a Progress Report dated March 8, 2000 addressed to the [Philippine Reclamation Authority], Progress Report No. 50 submitted by Mr. Roberto Espiritu.

ATTY. S.B. GARCIA:

And the one where the ₱86,479,617.61, the document which reflects that amount, that is what the document?

ENGR. J.R. MILLAN:

This is the attachment to the accomplishment of Romago *kasi* the Managing Consultant who made the report, they were the ones computing the accomplishments of the contractors. All the contractors in the project, *bale ito yong* report *nila*. For Romago, *ito yong* report *niya* as of February 29, 2000.

ATTY. S.B. GARCIA:

Your Honor, please, may I request that this accomplishment report as February 29, 2000 for outdoor electrical and lighting works be marked as our exhibit "R-2-10."⁴¹

Had the above testimony been untrue, Romago should have refuted the same considering that it had every opportunity to do so. On the contrary, it even adopted the same document as its own exhibit.⁴² In effect, Romago conceded the correctness of the PRA's valuation of the balance due it.

In keeping with this Court's ruling in *Eastern Shipping Lines, Inc. v. Court of Appeals*,⁴³ the Court deems it proper to impose legal interest of 6% *per annum* on the amount finally adjudged, reckoned from October 22, 2004, the date the CIAC rendered judgment until the same is wholly satisfied.⁴⁴

WHEREFORE, the Court **AFFIRMS** the Decision dated December 20, 2005 and Resolution dated August 24, 2006 of the Court of Appeals in CA-G.R. SP 88059 with **MODIFICATION**, directing the Philippine Reclamation Authority to pay Romago in addition to the ₱8,935,673.86 award of actual damages, legal interest of 6% *per annum* from October 22, 2004 until the judgment against it is wholly paid; and the costs of arbitration in the amount of ₱396,608.73.

⁴¹ Id. at 633-634.

⁴² Id. at 644.

⁴³ G.R. No. 97412, July 12, 1994, 234 SCRA 78, 95.

⁴⁴ *Tan v. OMC Carriers, Inc.*, G.R. No. 190521, January 12, 2011, 639 SCRA 471, 487.

SO ORDERED.



ROBERTO A. ABAD
Associate Justice

WE CONCUR:



PRESBITERO J. VELASCO, JR.
Associate Justice
Chairperson



JOSE CATRAL MENDOZA
Associate Justice



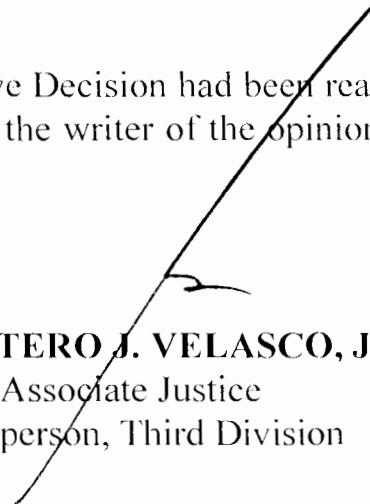
BIENVENIDO L. REYES
Associate Justice



MARVIC MARIO VICTOR F. LEONEN
Associate Justice

ATTESTATION

I attest 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.



PRESBITERO J. VELASCO, JR.
Associate Justice
Chairperson, Third Division

CERTIFICATION

Pursuant to Section 13, Article VIII of the Constitution and the Division Chairperson's Attestation, 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.

A handwritten signature in black ink, appearing to read 'Antonio T. Carpio', written in a cursive style.**ANTONIO T. CARPIO**

Acting Chief Justice