Republic of the Philippines
Supreme Court
Manila

EN BANC

NOEL F. MANANKIL, LIBERATO P LAUS, GLORIA C. MAGTOTO, EVANGELINE G. TEJADA, ALIZAIDO F. PARAS and PHILIP JOSE B. PANLILIO, *Petitioners,*	**G.R. No. 217342**
	Present:
	PERALTA, *C.J.*, PERLAS-BERNABE, LEONEN,* CAGUIOA, GESMUNDO, HERNANDO, CARANDANG, LAZARO-JAVIER, INTING, ZALAMEDA, LOPEZ, DELOS SANTOS, GAERLAN, BALTAZAR-PADILLA,** and ROSARIO, *JJ.*
- versus -	
COMMISSION ON AUDIT *Respondent.*	Promulgated: October 13, 2020

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RESOLUTION

INTING, *J.*:

For the Court's resolution are the following motions filed by Noel F. Manankil, Liberato P. Laus, Gloria C. Magtoto, Evangeline G. Tejada, Alizaido F. Paras, Philip Jose B. Panlilio (collectively, Manankil, *et al.*), and Clark Development Corporation (CDC):

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* On official leave.
** On leave.

(1) Motion for Leave to Admit Second Motion for Reconsideration[1] dated March 12, 2018; and

(2) Second Motion for Reconsideration[2] dated March 12, 2018 of the Court's Resolution[3] dated December 5, 2017 (Main Resolution), dismissing their petition for *certiorari*.

Antecedents

CDC is a subsidiary corporation of the Bases Conversion and Development Authority (BCDA). It was established through Executive Order No. (EO) 80[4] in 1993 for the purpose of becoming BCDA's "operating and implementing arm, x x x to manage the Clark Special Economic Zone (CSEZ)."[5] The CDC is empowered by law[6] to "make contracts, lease, own or otherwise dispose of personal and real property; sue and be sued; and otherwise do and perform any and all things that may be necessary or proper" to carry out the BCDA's purpose and objectives.

Pursuant to this authority, on December 14, 1995, CDC entered into a 25-year Lease Agreement[7] with Amari Duty Free, Inc. (Amari) to rent out a 1.70-hectare parcel of land located along Dyess Highway, CSEZ, Pampanga (leased property). Amari shall use the leased property for its "duty free store/commercial shopping" and "fastfood/cafeteria" operations.[8]

Under the agreement, Amari shall pay for the lease based on either of two schemes: (1) *minimum guaranteed lease payments* amounting to ₱204,000.00 per month for the first two years and subject to a 10% compounded increase thereafter; or (2) *percentage of gross revenues,*

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1 *Rollo*, pp. 447-451.
2 *Id.* at 452-476.
3 *Id.* at 405-410.
4 Authorizing the Establishment of the Clark Development Corporation as the Implementing Arm of the Bases Conversion and Development Authority for the Clark Special Economic Zone, and Directing All Heads of Departments, Bureaus, Offices, Agencies and Instrumentalities of Government to Support the Program [April 3, 1993].
5 Section 1, Executive Order No. (EO) 80.
6 Section 2, EO 80 provides that, "x x x. Pursuant to Section 15 of [Republic Act No.] 7227, the CDC shall have the specific powers of the Export Processing Zone Authority as provided for in Section 4 of Presidential Decree No. 66 (1972) as amended." In turn, Presidential Decree No. (PD) 66 created the Export Processing Zone Authority (EPZA) and revising Republic Act No. (RA) 5490.
7 *Rollo*, pp. 49-65.
8 *Id.* at 50.

which shall be 3%, 5%, and 7% of gross revenues from years 1 to 7, 8 to 15, and 16 to 25, respectively.[9]

Amari also undertook the duty to "improve the best use of the [l]eased [p]roperty by upgrading the facilities" thereon. The parties agreed that the ownership of any improvement introduced to the leased property shall automatically transfer to CDC at the end of the lease term.[10] In this connection, Amari caused the construction of a two-story building (original structure) on the leased property. The structure was completed on November 13, 1996 and had an estimated cost of ₱36,000,000.00.[11]

In addition, Amari insured the original structure as required under the Lease Agreement, *viz.*:

ARTICLE VIII
MISCELLANEOUS

> <u>Section 1</u>. x x x x
>
> <u>Section 2</u>. Insurance – The LESSEE shall insure against all risks including its interest in all existing facilities, new constructions and improvements introduced during the term of the lease, and such insurance shall likewise include the coverage for business interruption in an amount equal to the maximum insurable value, and which shall be adjusted yearly commensurate to the increasing value of said insurable interest of LESSOR in the Leased Property. All premium on any such insurance coverage shall be for the account of the LESSEE.
>
> It is expressly agreed and understood that the insurance coverage herein stipulated shall be secured from the Government Service Insurance System (GSIS) only not later than two (2) months after construction/rehabilitation of facilities, *in which the LESSOR shall be designated as its beneficiary.* However, for moveable properties, insurance coverage may be secured from any insurance company duly authorized by the LESSOR. *It is further agreed, that in case of loss or damage to the Leased Property during the term of this Contract, <u>the LESSOR shall reconstruct or restore the lost or damaged property to its original condition using the proceeds from the insurance for the continued lease and use by the LESSEE</u>. In the event that the insurance proceeds are insufficient for purpose of reconstruction or restoration as herein required, then LESSEE shall provide the*

[9] *Id.* at 51-52.
[10] *Id.* at 59.
[11] *Id.* at 66.

necessary funds to augment the insurance proceeds.[12] (Emphasis and underscoring supplied.)

In the meantime, Amari changed its corporate name to Grand Duty Free Plaza, Inc. (Grand Duty Free).[13] The parties also amended[14] the Lease Agreement to allow Grand Duty Free "[t]o engage in the transshipment of all kinds of goods or commercial products, such as but not limited to, clothing materials (brand new), appliances and house wares, tobacco and liquor products, consumer and health care products, food and other such products."[15]

On December 29, 2005, a fire razed the original structure, forcing Grand Duty Free to shut down its business operations.[16]

In view of this, in a Letter[17] dated January 16, 2006, Grand Duty Free, through its President Antonio See, requested CDC to waive its monthly rental payments starting January 2006. In response, CDC's Executive Committee authorized a moratorium on Grand Duty Free's rentals until December 31, 2007.[18]

Sometime in 2007, Grand Duty Free expressed its intention "to engage in the manufacture of branded cigarettes for export" and "to build a plant at the Grand Duty Free property." In this connection, Grand Duty Free inquired from CDC the tax and regulatory implications of its proposed venture.

In a Letter[19] dated May 30, 2007, CDC wrote Grand Duty Free on the following matters: (1) Grand Duty Free's proposal to manufacture branded cigarettes for export "is not among the Investment Priority Plan" as provided by Republic Act No. (RA) 9400,[20] which classified Clark as a freeport zone; (2) Grand Duty Free should cause the "complete demolition and clearing of all debris and remnants" of the original structure; and (3) As the moratorium on Grand Duty Free's

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12 *Id.* at 58-59.
13 *Id.* at 38.
14 *Id.* at 68-71.
15 *Id.* at 69.
16 *Id.* at 38.
17 *Id.* at 72.
18 *Id.* at 74.
19 *Id.*
20 An Act Amending Republic Act No. 7227, As Amended, Otherwise Known as the Bases Conversion and Development Act of 1992, and For Other Purposes [March 20, 2007].

rental payments had already ceased, the CDC shall resume the collection of rental payments accruing after the moratorium.

Nevertheless, in a Letter[21] dated June 12, 2007, Grand Duty Free pleaded CDC to extend the moratorium. It was still waiting for GSIS's release of the proceeds from the original structure's insurance (insurance proceeds), which it intends to use in clearing the leased property in preparation for the original structure's rebuilding. Moreover, the reconstruction is not expected to be completed for another eight months. Thus, it cannot resume its operations yet.

Meanwhile, on July 5, 2007, the GSIS released the insurance proceeds through a check amounting to ₱39,246,781.37 and payable to "CDC-Grand Duty Free Plaza."[22]

In response[23] to Grand Duty Free's request for extension, the CDC required Grand Duty Free to submit business and construction proposals, detailing its plans to erect a new structure (proposed structure) and the intended use thereof. The plans will be subject to CDC's approval. Thereafter, CDC shall: (1) consider extending the moratorium; and (2) undertake the construction of the proposed structure.

Grand Duty Free questioned CDC's rationale for its requirements, *viz.*: *First*, the activities Grand Duty Free is allowed to engage in are already set forth in the Lease Agreement and its amendment. *Second*, it already submitted a construction plan in relation to the original structure. In moving forward with the proposed structure, it does not intend to deviate from the original plan, which was already approved and found compliant with the National Building Code and CSEZ's master plan. *Third*, on a more practical standpoint, CDC should defer the duty to rebuild the proposed structure to Grand Duty Free. Section 18,[24] Article VIII of the Lease Agreement mandates the parties to amicably settle disputes between them, including the question of who bears the burden of rebuilding the original structure.[25]

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[21] *Rollo*, p. 75-76.

[22] *Id.* at 38.

[23] *Id.* at 77.

[24] Section 18. Amicable Settlement – In case of disputes arising from this Agreement, the parties shall promptly meet and exert best efforts towards amicable settlement of the dispute in good faith. *Id.* at 63.

[25] *Id.* at 78-79.

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In this regard, CDC insisted that Section 2, Article VIII of the Lease Agreement authorizes the lessor to reconstruct or restore the original structure in case of loss or damage to the lease property. The contract is clear on this matter. Thus, there is no dispute to subject to an amicable settlement.[26]

The parties had seemed to reach an impasse after these exchanges. As a result, Grand Duty Free intimated the possibility of discontinuing its business in the Clark Freeport Zone. With this in mind, it proposed the pretermination of the Lease Agreement.[27]

After negotiations between the parties, CDC agreed to preterminate the Lease Agreement, as authorized by its Board of Directors (Board) through Resolution No. SM-03-03, Series of 2008 dated March 13, 2008, *viz.*:

> "RESOLVED THAT, the following recommendations of the Executive Committee (Excom) with regard to the pre-termination of the Lease Agreement of Grand Duty Free Plaza, Inc., be APPROVED, as they are hereby APPROVED:
>
> a. Pre-termination of the Lease Agreement effective 31 December 2007;
> b. 50%-50% sharing of the insurance proceeds of Php39,246,781 between CDC and Grand Duty Free;
> c. Forfeiture of Security Deposit of Php1,224,000 and waiver of all accounts due (Php343,849.58-unpaid rentals) to CDC; and
> d. Release of the 50% (Php19,623,390.68) share of Grand [Duty Free] in the insurance proceeds only upon proof of payments of all utility bills and submission of clearances from the Bureau of Customs and Bureau of Internal Revenues (BIR).[28]

Based on the parties' 50-50 sharing scheme, CDC and Grand Duty Free will each receive ₱19,623,390.68, representing their 50% share in the insurance proceeds. On its end, CDC's *net proceeds* from the pretermination amounted to ₱20,503,541.10 computed as follows:

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26 *Id.* at 80-81.
27 *Id.* at 82-83.
28 *Id.* at 90.

CDC's share in the proceeds	₱19,623,390.68
add Security deposit	1,224,000.00
subtract Unpaid dues	(343,849.58)
Net proceeds received by CDC	₱20,503,541.10

On April 1, 2008, CDC issued a check amounting to ₱19,623,390.68 payable to Grand Duty Free, representing the latter's share in the insurance proceeds (50% Release). However, on October 17, 2008, the Commission on Audit (COA), through Elvira G. Punzalan, State Auditor IV, issued *Notice of Disallowance No. (ND) 2008-10-03 (2008)*[29] finding the aforementioned disbursement "contrary to Article VIII, Sections 2 and 3 of the Lease Agreement."

The following persons were liable under the ND:

1. Grand Duty Free/Antonio See as payee;

2. Noel F. Manankil as approving officer for the check and disbursement voucher;

3. Liberato P. Laus as approving officer for the check;

4. Gloria C. Magtoto, Evangeline G. Tejada, and Alizaido F. Paras as certifying officers for the disbursement voucher; and

5. Philip Jose B. Panlilio as recommending officer.

Herein petitioners appealed the disallowance to the COA Regional Director.

The COA Regional Director's Ruling

In COA Regional Office No. III Decision No. 2011-09[30] dated April 13, 2011, the COA Regional Director Amante A. Liberato upheld the disallowance, *viz.*:

[29] *Id.* at 92.
[30] *Id.* at 102-106.

> WHEREFORE, in the light of the foregoing, the instant appeal cannot be given due course. Consequently, Notice of Disallowance No. 2008-10-03, amounting to PhP19,623,390.68, is AFFIRMED.

The COA Regional Director held that the CDC was entitled to 100% of the proceeds. *Thus, the 50% Release in favor of Grand Duty Free was not legally justified.* He explained as follows: *First*, under the Lease Agreement, the parties intended CDC to be the sole beneficiary of the insurance, as compensation for the loss it sustained from the destruction of its property by fire. *Second*, the insurance proceeds constituted a claim on the GSIS Property Insurance Fund, established to answer for any damage to, or loss of, government properties due to fire. *Third*, only CDC could preterminate the Lease Agreement. Grand Duty Free defaulted when it preterminated the contract and prevented CDC from fulfilling its obligation to reconstruct the original structure. Despite its default, Grand Duty Free collected half of the insurance proceeds. *Fourth*, the defense of "sound business judgment" cannot be used to defeat the rationale of property insurance, which is to compensate a person for such loss as the property insured may have suffered.[31]

Aggrieved, Manankil, *et al.*, elevated the case to the COA Commission Proper (COA Proper) docketed as COA CP Case No. 2011-253.

The COA Proper Ruling

In its Decision No. 2014-421[32] dated December 18, 2014, the COA Proper denied Manankil, *et al.*'s appeal, *viz.*:

> WHEREFORE, premises considered, the instant Petition is hereby DENIED for lack of merit. Accordingly, the assailed Commission on Audit Regional Office 3 Decision No. 2011-09 dated April 13, 2011, which sustained Notice of Disallowance No. 2008-10-03 dated October 17, 2008 in the amount of P19,623,390.68, representing 50% of the insurance proceeds given out to Grand Duty Free Plaza, Inc., is hereby AFFIRMED. The Audit Team Leader and Supervising Auditor, Clark Development Corporation, are, however directed to issue a Supplemental Notice of Disallowance to include the unpaid dues in the amount of P343,849.58.[33]

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[31] *Id.* at 104-106.
[32] *Id.* at 37-48.
[33] *Id.* at 47.

In affirming the Regional Director's Decision, the COA Proper further held that *the 50-50 sharing scheme: (1) finds no basis in law and (2) runs counter with the Lease Agreement.*[34] *First*, the parties constituted CDC as the sole beneficiary under the insurance contract to compensate CDC for the loss of the original structure's property value *and* the rental income pertaining to the remaining term of the lease. Section 53 of the Insurance Code of the Philippines (Insurance Code) provides that the "[i]nsurance proceeds shall be applied exclusively to the proper interest of the person in whose name or for whose benefit it is made x x x."[35] *Second*, when it did not agree to CDC undertaking the original structure's reconstruction, Grand Duty Free breached the Lease Agreement and was deemed to have abandoned the leased property.[36]

The COA Proper also pointed out that preterminating the Lease Agreement disadvantaged CDC, such that it received only the *net proceeds* (₱20,503,541.10), instead of earning the *minimum guaranteed lease rental payments* over the remaining portion of the lease period (₱183,398,896.43).[37] CDC would have derived greater financial benefits had the Grand Duty Free opted to continue the lease.

Lastly, CDC already had a vested right over the total amount of insurance proceeds. The parties' new agreement—preterminating the Lease Agreement and requiring CDC to forego a portion of the insurance proceeds does not affect CDC's exclusive right thereof.[38]

Undaunted, Manankil, *et al.*, elevated the case to the Court *via* a petition for *certiorari*, averring as follows: *first*, the Lease Agreement was superseded by the parties' agreement to preterminate the same. *Second*, the 50% Release to Grand Duty Free was approved by the CDC Board, exercising sound business judgment. The government did not sustain any loss, damage, or injury as a result thereof. *Third*, Grand Duty Free has insurable interest over the original structure, being the builder, possessor, and beneficial owner thereof. *Fourth*, Grand Duty Free was the main beneficiary of the insurance proceeds, leaving CDC to be a residual beneficiary. In fact, the GSIS released the proceeds through a check payable to both parties. *Fifth*, CDC's receipt of the net proceeds upon the Lease Agreement's pretermination duly indemnified and/or compensated it from whatever damage it may have sustained.

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[34] *Id.* at 43.
[35] *Id.* at 42-43.
[36] *Id.* at 46.
[37] *Id.* at 44-45.
[38] *Id.* at 46.

The COA, through the Office of the Solicitor General (OSG), raised[39] the following counter-arguments: *first*, the terms in the Lease Agreement shall prevail because the cause of the loss took place prior to the agreement's pretermination. *Second*, it was CDC's interest over the property that was subject of the fire insurance. The Insurance Code provides that the insurance proceeds shall be applied exclusively to the beneficiary's proper interest. *Third*, the fact that Grand Duty Free funded the original structure's construction does not militate against the parties' intention to insure CDC's interest thereon, not Grand Duty Free's. *Fourth*, the Lease Agreement is the primary law between the parties. *Fifth*, assuming *arguendo* that the CDC Board can validly agree to preterminate the contract, it cannot alter the Lease Agreement's terms considering that the CDC's right over the insurance proceeds had already vested. *Sixth*, Grand Duty Free's refusal to continue the lease released CDC from its contractual obligation to rebuild the original structure. *Seventh*, the CDC's obligation to reconstruct was intended to assure that the lease will continue and provide income to CDC. *Eighth*, the Lease Agreement's pretermination was disadvantageous to CDC. It cannot be used to reduce the CDC's insurable interest.

In the Main Resolution, the Court dismissed Manankil, *et al.*'s petition for *certiorari*.[40] The Court also denied their subsequent Motion for Reconsideration.[41] Thus, the Main Resolution became final and executory on February 6, 2018 and recorded in the book of entries of judgment accordingly.[42] Consequently, the Motion for Leave to Admit Second Motion for Reconsideration of the Resolution dated February 6, 2018, and the aforesaid Second Motion for Reconsideration dated March 12, 2018 were noted without action.[43] Manankil, *et al.* prayed that the Second Motion for Reconsideration be resolved by the Court.[44]

Second Motion for Reconsideration

In the Second Motion for Reconsideration, Manankil, *et al.* insist that the Lease Agreement's pretermination was a valid exercise of management discretion. It was clearly to CDC's advantage because the pretermination allowed it to enter to new Lease Agreement more

[39] *Id.* at 344-377.
[40] *Id.* at 405-410.
[41] *Id.* at 430.
[42] *Id.* at 432.
[43] *Id.* at 477.
[44] *Id.* at 485-486.

profitable than its lease to Grand Duty Free. In the absence of bad faith, the Board's business judgment must be upheld.

Ruling of the Court

After a careful review, the Court finds merit in Manankil, *et al.*'s Second Motion for Reconsideration.

Resolving the Case on a Second Motion for Reconsideration

Previously, the Court resolved to dismiss Manankil, *et al.*'s petition for *certiorari* in the Resolution dated December 5, 2017. The Court also denied petitioners' Motion for Reconsideration. Subsequently, the entry of judgment of the aforementioned Resolution was made on February 6, 2018. Now before the Court is petitioners' Second Motion for Reconsideration.

The COA, through the OSG, urges the Court to deny this motion because, being a second motion for reconsideration, it is already forbidden by the rules.[45]

Verily, the Rules of Court prohibit second and subsequent motions for reconsideration.[46] However, while it is established that rules of procedure are "tools designed to facilitate the attainment of justice," courts shall not strictly and rigidly apply them if it will only "frustrate, rather than promote <u>*substantial justice*</u>."[47]

Thus, in the recent case of *Laya v. Court of Appeals*,[48] the Court *en banc* discussed at length that while "second and subsequent motions for reconsideration are [generally] forbidden," there is a long line of jurisprudence where the Court did not restrain itself from granting a second motion for reconsideration when exceptional circumstances in the case warrant the relaxation of the rules.

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[45] *Id.* at 498.
[46] Section 2. Rule 52, Rules of Court.
[47] *Civil Service Commission v. Almojuela*, G.R. No. 194368, April 2, 2013
[48] G.R. No. 205813, January 10, 2018.

In *Laya*, it was held that procedural rules cannot prevent the Court from correcting a decision/resolution, which is "legally erroneous, patently unjust and potentially capable of causing unwarranted and irremediable injury or damage to the parties. Under these circumstances, even final and executory judgments may be set aside because of the existence of compelling reasons."[49]

As will be discussed below, *the Court has noted acts and omissions by the COA that violate the petitioners' right to due process. That these acts have tainted the assailed issuances with grave abuse of discretion compels the Court to revisit our previous Resolution and grant petitioner's Second Motion for Reconsideration.*

COA's Jurisdiction and Authority to Disallow Government Expenditures

The COA is constitutionally[50] empowered to disallow "expenditures or uses of government funds and properties" based on any of the following grounds:

1) That the expenditure is *illegal* or contrary to law;[51]

2) That the expenditure is *irregular* or "incurred without adhering to established rules, regulations, procedural guidelines, policies, principles or practices that have gained recognition in law" or "in violation of applicable rules and regulations other than the law;"[52]

3) That the expenditure is *unnecessary*, the incurrence of which "could not pass the test of prudence or the diligence of a good father of a family, thereby denoting non-responsiveness to the exigencies of the service;"[53]

4) That the expenditure is *excessive* or "incurred at an immoderate quantity and exorbitant price;"[54]

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[49] G.R. No. 205813, January 10, 2018.

[50] 1987 CONSTITUTION, Article IX(D), Section 2(2) provides that the Commission on Audit (COA) has "exclusive authority, subject to the limitations in this Article, to define the scope of its audit and examination, establish the techniques and methods required therefor, and promulgate accounting and auditing rules and regulations, including those for the prevention and disallowance of irregular, unnecessary, excessive, extravagant, or unconscionable expenditures or uses of government funds and properties."

[51] Section 16.1.1, COA Circular No. 94-001 (January 20, 1994).

[52] Paragraph 3.1, COA Circular No. 85-55-A (September 8, 1985).

[53] Paragraph 3.2, COA Circular No. 85-55-A (September 8, 1985).

[54] Paragraph 3.3, COA Circular No. 85-55-A (September 8, 1985).

5) That the expenditure is *extravagant* or "immoderate, prodigal, lavish, luxurious, waste grossly excessive, and injudicious;"[55] or

6) That the expenditure is *unconscionable* or "unreasonable and immoderate, and which no man in his right sense would make, nor a fair and honest man would accept as reasonable and incurred in violation of ethical and moral standards."[56]

That the COA took pains to define each ground and differentiate them from one another is not inconsequential. The above-cited definitions serve as parameters such that "the COA's power and authority to disallow upon audit can only be exercised over transactions deemed as irregular, unnecessary, excessive, extravagant, illegal or unconscionable expenditures or uses of government funds and property." Thus, the COA may only issue an ND upon such grounds.[57] Stated differently, these grounds are *jurisdictional*. Absent any of these grounds, the COA is not clothed with authority to disallow the subject expenditure.

Ground Relied upon by COA is not Clear

For its part, the COA maintains that it afforded Manankil, *et al.* due process. *First*, the COA is not obligated to afford the parties an opportunity to take part in the audit investigation prior to the issuance of an ND.[58] *Second*, the subject ND clearly identifies the persons liable for the disallowance, as well as their respective liabilities based on the extent of each one's participation.[59]

However, the COA did not *expressly* state any of the above-discussed grounds in its ND. Instead, it merely cited the reason "contrary to Article VIII, Sections 2 and 3 of the Lease Agreement/Amended Lease Agreement" in disallowing the 50% Release. *As it stands, whether a potential violation or breach of an existing private agreement makes the payment irregular, unnecessary, excessive, extravagant, illegal or unconscionable is not clear.*

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55 Paragraph 3.4, COA Circular No. 85-55-A (September 8, 1985).

56 Section 16.1.2, COA Circular No. 94-001 (January 20, 1994).

57 *Miralles v. Commission on Audit*, 818 Phil. 380, 392 (2017).

58 *Id.* at 498-501.

59 *Id.* at 502-503.

Inasmuch as it serves to notify a person charged with liability over a disallowed expenditure, the ND cannot be ambiguous as to the reasons justifying its issuance. The COA's *failure to specify the ground* relied upon for its disallowance raises serious concerns, *viz.*: *first*, it casts doubt over the COA's authority to disallow the expense in question, the grounds being jurisdictional; and *second*, it also deprives the persons found liable a fair opportunity to set up an effective case for their defense—a violation of their fundamental right to due process[60] amounting to grave abuse of discretion.

Later on, the COA Regional Director and COA Proper still did not cite a specific ground in upholding the disallowance. Notably, aside from being "contrary to the provisions of the contract," the COA also upheld the disallowance for being "contrary to law," *impliedly* categorizing the subject disbursement as "illegal" by definition.

Verily, the Court recognizes the wide latitude given to the COA in the discharge of its constitutional duty as the "guardian of public funds and properties."[61] *However, the COA must be deliberate and straightforward in its charges*. Its far-reaching jurisdiction cannot serve to justify its complacency in the performance of constitutional functions or to rectify due process violations.

Even if the Court considers COA's belated attempt to clarify its charges to have cured the defective ND,[62] the Court still finds for the petitioners.

Lease Agreement v. Insurance Contract.

At the onset, the Court must distinguish between the *Lease Agreement* and the *insurance contract.*

The *Lease Agreement's* subject was a parcel of land located within the CSEZ, upon which Grand Duty Free erected the original structure. While the parcel of land is a government property, the original structure

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[60] *Id.* at 398.
[61] *Id.*
[62] See *Development Bank of the Philippines v. COA*, G.R. No. 221706, March 13, 2018.

thereon—an improvement to the leased property—was owned by Grand Duty Free.

Under the *Lease Agreement*, Grand Duty Free was obligated to: (1) enter into an insurance contract to secure the original structure against all risks, and (2) designate the CDC as the beneficiary therein. In turn, Grand Duty Free entered into an *insurance contract* with the GSIS and paid all the premiums required under the policy. The *Lease Agreement* merely required its designation as beneficiary. However, the CDC was not a party to the *insurance contract*. The *Lease Agreement* further provided that in case of loss of or damage to the leased property, the CDC shall reconstruct or restore the original structure using the proceeds from the *insurance contract*.

When fire gutted the original structure, Grand Duty Free, as the insured, filed a claim upon the *insurance contract*. The GSIS, the insurer, remitted the proceeds to the CDC, as the designated beneficiary under the *Lease Agreement*. Thereafter, the CDC and Grand Duty Free preterminated the *Lease Agreement* and agreed to share in the insurance proceeds, 50-50. Pursuant to this, the CDC released 50% of the proceeds to Grand Duty Free.

The COA cites two main reasons for disallowing CDC's 50% Release: *first*, that it violated the Insurance Code, particularly Sections 53 and 18 thereof; and *second*, that the expenditure was contrary to the provisions of the Lease Agreement, particularly Section 2, Article VIII and Section 2, Article VI, thereof.

Insurance Code does not Apply.

The COA Proper cited the following Insurance Code provisions to support the 50% Release's disallowance:

> Sec. 18. No contract or policy of insurance on property shall be enforceable except for the benefit of some person having an insurable interest in the property insured.
>
> Sec. 53. The insurance proceeds shall be applied exclusively to the proper interest of the person in whose name or for whose benefit it is made unless otherwise specified in the policy.

Applying the above-cited provisions, the COA Proper ruled that the insurance contract was executed primarily to protect the CDC's—not Grand Duty Free's—insurable interest in the original structure. As the designated beneficiary having insurable interest in the property insured, the insurance proceeds shall be for the CDC's exclusive benefit. Thus, the 50-50 sharing scheme was contrary to law.

The Court disagrees with the COA Proper's reasoning.

That the disallowed amount in this case refers to a portion of insurance proceeds received from the GSIS does not *ipso facto* place the 50% Release within the coverage of the terms of the insurance contract and, by extension, the Insurance Code.

Certainly, whether or not a person designated to receive the insurance proceeds possesses the requisite insurable interest is a matter that will affect the *contract's enforceability* and the *beneficiary's suitability* to be constituted as such.[63] However, insurable interest is irrelevant to the manner by which the recipient chooses or is bound to use the proceeds after the fact.

In the present case, the COA seeks to disallow an amount that pertains not to the insurance proceeds *per se*, but to the subsequent disposition thereof.

Verily, the Insurance Code states that the proceeds shall be applied to the designated recipient's exclusive benefit. However, once the insurer releases the proceeds in full to the designated recipient, the obligations under a contract of insurance will have been fully performed and, thus, extinguished.[64] Upon such time, a contract of insurance's terms and the Insurance Code's provisions may no longer control the manner by which the proceeds are thereafter used or otherwise disposed of.

To recall, the CDC's 50% Release was pursuant to the terms and conditions attached to the Lease Agreement's *pretermination*. Thus, the payment and its possible disallowance must be evaluated based on these terms and conditions, not on the insurance contract or the Insurance Code. *This leads to the next issue for the Court's resolution: Did the 50% Release violate the Lease Agreement?*

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[63] See *Cha v. CA*, 343 Phil. 488, 493-494 (1997).
[64] CIVIL CODE, Article 1231(1).

According to the COA, the insurance proceeds exclusively belonged to CDC as the sole beneficiary. While it had initially been required to use these proceeds to rebuild the original structure, CDC was released from this obligation when Grand Duty Free defaulted (*i.e.*, refused to allow the CDC to proceed with reconstruction) and preterminated the Lease Agreement. In the first place, the primary purpose of designating CDC as the insurance's sole beneficiary was to protect its interest, particularly in CDC's rental income for the remainder of the lease term. Thus, Grand Duty Free had no right over the proceeds unless it will continue to lease the property for the remainder of the lease term.

This reasoning is circuitous and flawed.

Section 2, Article VIII of the Lease Agreement Imposed Reciprocal Obligations

It is undisputed that the GSIS released the full amount of the insurance proceeds to the CDC. However, the Court cannot ignore that the CDC's receipt of these proceeds *carried with it the concomitant obligation to rebuild the original structure.* In other words, the parties were *reciprocally obligated*: on the one hand, Grand Duty Free shall insure the original structure and designate CDC as the recipient of the proceeds and, on the other, CDC shall use these proceeds in rebuilding the original structure.

When the parties agreed to preterminate the lease, CDC was excused from performing its contractual obligation to reconstruct because Grand Duty Free no longer desired to pursue it's business in the CSEZ.

However, CDC's release from its former obligation was by no means gratuitous. *A fair and reasonable interpretation of the Lease Agreement and its subsequent pretermination demands that CDC remained reciprocally obligated upon the Lease Agreement's pretermination.* Thus, in place of its former obligation to undertake reconstruction, it had the duty to release to Grand Duty Free an amount equal to 50% of the insurance proceeds.

50-50 Sharing Scheme is Valid and Enforceable.

There is also no dispute that the Lease Agreement's pretermination was a new agreement. However, the COA argues that the pretermination *vis-à-vis* the 50-50 sharing scheme cannot supersede CDC's vested right over the total amount of the proceeds.

The Court disagrees with the COA.

When the parties expressly agreed to preterminate the Lease Agreement, they altered their original obligations' object and principal conditions and thereby extinguished the same. Thus, the parties shall be bound by the new agreement's terms and conditions, including the 50-50 sharing scheme.

The COA attempts to reduce the new terms' binding effect by arguing that the CDC Board's decision to preterminate the Lease Agreement was *ultra vires*.

This argument is specious.

EO 80 provides that the CDC's powers shall be vested in and exercised by its Board.[65] The CDC Board's authority to enter into a new contract preterminating the Lease Agreement originates from CDC's statutory power to make contracts and lease real property as the CSEZ's administrator.[66]

In the same vein, the Board's approval of the 50-50 sharing scheme was also within its recognized corporate power to "do and perform any and all things that may be necessary or proper"[67] to administer the CSEZ.

From the very start, CDC knew that the insurance proceeds were not completely at their disposal. Even the COA recognizes that CDC's receipt thereof was qualified by the concomitant obligation to rebuild the original structure. Thus, the CDC held the proceeds in trust, in view of

[65] Section 3, EO 80.
[66] Section 4 (k), PD 66 as provided in EO 80.
[67] *Id.*

its reciprocal obligation to reconstruct. *The CDC Board simply exercised prudence* when it refused to unjustly enrich the corporation and agreed to share the insurance proceeds with Grand Duty Free.

The COA further argues that the parties intended the proceeds to answer for the loss of the original structure *and* lost rental income due to pretermination. Thus, the Board's approval of the 50-50 sharing scheme financially disadvantaged CDC.

The Court disagrees with the COA's proposition. This is negated by the clear absence of any penal or escalation clause obligating Grand Duty Free to pay for lease rentals for the unexpired portion of the lease in the event of pretermination.

Parenthetically, the contract of insurance in the present case is a "fire insurance" obtained to secure the original structure against *loss by fire and lightning*.[68] The proceeds thereof cannot be construed to answer for CDC's loss of future rentals. Thus, the COA's comparison between the net proceeds and minimum guaranteed lease payments for the remaining lease term is irrelevant and misplaced.

All told, the Board Resolution preterminating the Lease Agreement and approving the 50-50 sharing scheme is a *legitimate exercise of the Board's business judgment.* The Court cannot interfere with sound corporate decisions when there is no evidence tainting the Board's good faith in its business dealings.[69]

The Court stresses that CDC and Grand Duty Free mutually agreed on the pretermination's terms and conditions. The Court must uphold the pretermination because it embodies the parties' mutual and amicable desistance from continuing their contractual relations. After all, the parties have the freedom to do so at their convenience, provided that their new terms do not contravene law, morals, good customs, public order, or public policy.[70]

Certainly, the CDC cannot be excused from the performance of its new obligation to release Grand Duty Free's share in the proceeds.

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[68] As evidenced by Fire Insurance Policy Nos. F-0152-05-CSFP and F-0152-A-05-CSFP. *Rollo*, pp. 267-268.

[69] See *Philippine Stock Exchange, Inc. v. The Hon. CA*, 346 Phil. 218, 234 (1997).

[70] CIVIL CODE, Article 1306.

The Government Suffered No Loss in the Transaction

As earlier discussed, the CDC merely held the insurance proceeds in trust, in view of its impending duty to rebuild the original structure. To recall, when fire razed the original structure on December 29, 2005, 10 years into the lease's 25-year term, Grand Duty Free remained to have full ownership over the property.

In addition, Grand Duty Free: (1) obtained the insurance to protect its property (the original structure, and not the land on which it stood) against damage caused by fire, and (2) paid all the required premiums. It is clear that the government did not contribute any capital to obtain the insurance.

In other words, the government collected from an insurance policy constituted over private property, the premium payments for which it did not even fund. Certainly, the government did not suffer any loss of capital from its partial collection.

WHEREFORE, the Court **GRANTS** the Second Motion for Reconsideration dated March 12, 2018; **SETS ASIDE** the Resolutions dated December 5, 2017 and February 6, 2018.

The Court **GRANTS** the petition for *certiorari*, and **NULLIFIES** and **SETS ASIDE** Notice of Disallowance No. 2008-10-03 dated October 17, 2008 for being issued with grave abuse of discretion.

No pronouncement on costs of suit.

SO ORDERED.

HENRI JEAN PAUL B. INTING
Associate Justice

WE CONCUR:

DIOSDADO M. PERALTA
Chief Justice

ESTELA M. PERLAS-BERNABE
Associate Justice

(On official leave)
MARVIC M.V.F. LEONEN
Associate Justice

ALFREDO BENJAMIN S. CAGUIOA
Associate Justice

ALEXANDER G. GESMUNDO
Associate Justice

RAMON PAUL L. HERNANDO
Associate Justice

ROSMARI D. CARANDANG
Associate Justice

AMY C. LAZARO-JAVIER
Associate Justice

RODIL V. ZALAMEDA
Associate Justice

MARIO V. LOPEZ
Associate Justice

EDGARDO L. DELOS SANTOS
Associate Justice

SAMUEL H. GAERLAN
Associate Justice

(On leave)
PRISCILLA J. BALTAZAR-PADILLA
Associate Justice

RICARDO R. ROSARIO
Associate Justice

CERTIFICATION

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

DIOSDADO M. PERALTA
Chief Justice