

IN THE SUPREME COURT OF GUAM

MAXIMO V. RONQUILLO and NELLIE P. RONQUILLO,
Plaintiffs-Appellees/Counterclaim Defendants-Appellees,

vs.

**KOREA AUTOMOBILE, FIRE, & MARINE INSURANCE
COMPANY, LTD., JANICE C. MANSFIELD aka JANICE
O'NEILL, and ERNEST A. MURPHY,**
Defendants-Appellants/Counterclaim Plaintiffs-Appellants.

OPINION

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Supreme Court Case No.: CVA01-004
Superior Court Case No.: CV1076-99

Appeal from the Superior Court of Guam
Argued and Submitted on September 12, 2001
Hagåtña, Guam

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BEFORE: PETER C. SIGUENZA, JR., Chief Justice; F. PHILIP CARBULLIDO, Associate Justice; BENJAMIN J.F. CRUZ, Justice Pro Tempore.

CARBULLIDO, J.:

[1] Maximo V. and Nellie P. Ronquillo (“Ronquillos”) sued Korea Automobile, Fire, and Marine Insurance Company (“Surety”) for quiet title and sought to enjoin Surety from foreclosing on a mortgage to certain real property. The mortgage was issued as security on an indemnity agreement that was issued pursuant to a construction performance bond. The issue is whether Surety’s responsibilities under the performance bond were triggered by the contractor’s defective work or breach of the construction contract. The trial court found against Surety and thereby quieted title to the disputed property in the Ronquillos. Surety appeals. We reverse.

I.

[2] This case arose from a defective construction claim. Phil-Guam Builders Corporation (“Phil-Guam”) entered into a contract with Janice C. Mansfield, also known as Janice O’Neill, and Ernest A. Murphy (“O’Neill and Murphy”) to construct a home in Santa Rita, Guam. The contract price for the construction of the home was \$191,500.00. In connection with the construction contract, and on behalf of Phil-Guam, a performance bond was issued by Surety. By an indemnity agreement, the Ronquillos, principal owners of Phil-Guam, agreed to indemnify Surety for any sums paid by Surety under the bond, and executed a mortgage of real property to Surety to secure the indemnity agreement. Construction proceeded on the home and an occupancy permit was issued on March 25, 1995.

[3] Shortly after O'Neill and Murphy moved into the home, the windows began to leak. O'Neill and Murphy notified Phil-Guam and Surety of the problem by a letter dated June 5, 1995. On June 8, 1995, Surety sent a letter to Phil-Guam indicating a potential claim and requesting that Phil-Guam correct the problem. On October 25, 1995, Surety again sent a letter to Phil-Guam requesting its cooperation in remedying the situation. On different occasions, Phil-Guam attempted to correct the problem but was not successful. In November 1995, the parties attended a pre-default hearing. By February 1996, Surety had retained the services of two different consultants who agreed that the cause of the problem was faulty installation by Phil-Guam. In July 1996, O'Neill and Murphy, pursuant to the terms of the construction contract, declared Phil-Guam in default. Surety hired another contractor to install new windows and fix the damage caused by the leakage. Surety paid \$124,779.00 to replace the windows and repair the damages. Surety sought to foreclose on the mortgage executed by Ronquillo, and in April of 1999, Surety recorded a notice of sale under mortgage of the subject real property at the Department of Land Management.

[4] To stop the sale under mortgage, the Ronquillos filed the underlying complaint to quiet title against Surety, and O'Neill and Murphy. Surety filed an answer and a counterclaim against the Ronquillos and the Bank of Guam for the amount paid for the repairs.¹ The trial court rendered judgment for the Ronquillos, holding that Surety had not acted in accordance with the contract provisions when stepping in to make the repairs. The trial court further held that the defective work did not constitute a default under

¹ According to the trial court's Decision and Order, the Bank of Guam held a mortgage on the property foreclosed by Surety. The trial court found that Bank of Guam's mortgage was second in time to Surety's and denied the Bank's request for a finding that its mortgage had priority over Surety's mortgage. The trial court also noted that the Bank's request was moot because judgment was rendered against Surety. This part of the trial court's decision was not made an issue in this appeal.

the contract triggering the obligations of Surety under the performance bond. This appeal followed.

II.

[5] This court has jurisdiction over an appeal from a final judgment. Title 7 GCA § 3107(b) (1994).

III.

[6] The primary issue is whether Surety was entitled to foreclose on the mortgage given by the Ronquillos to secure the indemnity agreement. In order to make this determination, we must consider whether Surety's responsibility was triggered under the terms of the performance bond. This requires consideration of whether Phil-Guam violated the terms thereof.

A. The Performance Bond

[7] We start by determining Surety's obligations under the performance bond. Most important to this case, under sections 6 and 6.1 of the performance bond, Surety is obligated for the correction of Phil-Guam's defective work and completion of the construction contract. In addition, section 1 of the performance bond provides that Surety and Phil-Guam are jointly and severally responsible for performance of the construction contract.

[8] The act which is alleged to have triggered Surety's obligation under the performance bond was the failure of Phil-Guam to properly install the windows in the home. The trial court made a factual finding that Phil-Guam failed to install the windows in a workmanlike manner, which amounted to defective work. Appellants' Excerpts of Record, p. 71 (Decision and Order, Jan. 30, 2001). On appeal, factual findings are reviewed under the clearly erroneous standard. *Apana v. Rosario*, 2000 Guam 7, ¶ 9. In such

reviews, much deference is given to the trial court. *Craftworld Interiors, Inc. v. King Enterprises, Inc.*, 2000 Guam 17, ¶ 8.

[9] The record contains evidence that supports the trial court’s factual finding of defective work. This evidence consists of letters from a representative of the window manufacturer, a construction contractor, and an architect who independently inspected the windows and concluded that the installation was defective. Appellants’ Excerpts of Record, pp. 98, 105, 110. These letters were admitted into evidence without objection from the Ronquillos. Transcript, vol. I, p. 6 (Bench Trial, Jan. 23, 2001). Thus, we hold the trial court’s finding is not clearly erroneous. We must next determine whether Phil-Guam’s defective work triggered Surety’s responsibility under the performance bond.

[10] Surety’s responsibility is determined by the performance bond, and as therein directed, to the construction contract. Principles of contract interpretation as applied to the facts are reviewed *de novo*. *Apana v. Rosario*, 2000 Guam 7, ¶ 9. In interpreting a contract, the language governs if clear and explicit and not involving absurdity. Title 18 GCA § 87104 (1992); *see Camacho v. Camacho*, 1997 Guam 5, ¶ 32. Generally, with a written contract, the intent of the parties is ascertained from the writing alone. Title 18 GCA § 87105 (1992), *Camacho*, 1997 Guam 5 at ¶ 33

[11] The performance bond, addresses defective work explicitly:

After the Owner has terminated the Contractor’s right to complete the Construction contract . . . the Surety is obligated without duplication for . . . [t]he responsibilities of the Contractor for **correction of defective work** and completion of the Construction contract
. . . .

Appellants’ Excerpts of Record, p. 30 (Performance Bond, §§ 6-6.1) (emphasis added). We find that Surety’s obligation to correct defective work after the contractor’s right to complete the contract has been

terminated is clear.

[12] The trial court distinguished between defective work and contractual default. The trial court found that although Phil-Guam had performed defective work and thereby breached the terms of the construction contract, this did not constitute a default of the construction contract requiring Surety to take action. We disagree. Under our interpretation of sections 6 and 6.1 of the performance bond, Surety was expressly liable for Phil-Guam's failure to repair defects and no finding of default of the construction contract was necessary. In any event, section 1 of the performance bond obligates Surety to perform the construction contract, which as is discussed later, explicitly requires Phil-Guam to repair defects after substantial completion. Thus, the failure of Phil-Guam to repair defects also amounted to a default of the construction contract, requiring Surety to step in.

B. Completion of the Construction Contract

[13] The Ronquillos argue that the construction contract was completed prior to any breach or default, thus relieving Surety of any obligation under the performance bond. However, the construction contract provides that the "Contractor shall promptly correct Work rejected by the Architect or failing to conform to the requirements of the Contract Documents, **whether observed before or after Substantial Completion. . .**" Appellants' Excerpts of Record, p. 25 (Construction Contract, Article 18.1) (emphasis added). Thus, Phil-Guam remained responsible for correcting defective work even after completion of the construction contract. Case law supports this interpretation. "[A surety's] promise that the project would be completed according to the terms and conditions of the construction contract means that [the surety] would be liable for defective work performed by the general contractor upon the general contractor's default." *Federal Ins. Co. v. Southwest Florida Ret. Ctr., Inc.*, 707 So.2d 1119, 1121 (Fla. 1998). The

surety's liability for the contractor's defective work "is not dependent upon whether the defect was discovered before or after substantial completion." *Id.* Thus, even if substantial completion occurred as indicated by the issuance of the occupancy permit, if the work was so defective that it did not comply with the terms of the construction contract, the breach of the contract would constitute a default under the performance bond.

[14] The Ronquillos argue that section 2 of the indemnity agreement is evidence of the parties' intent that the performance bond only secure performance, which they claim is substantial completion of the contract without regard to workmanship. However, under 18 GCA § 87105, the intent of the parties must be determined from the performance bond alone, which does not refer to the indemnity agreement. The performance bond clearly and explicitly evidences the intent that Surety step in to correct defective work and complete the construction contract. Thus, the language of the performance bond controls and this court may not look to the indemnity agreement to ascertain the intent of the parties as it pertains to their obligations under the performance bond. *See Camacho*, 1997 Guam 5 at ¶ 33 ("It is clear from the four sections of Title 18, cited above [18 GCA §§ 87104, 87105, 87110, 87111] that in interpreting a clause of a contract to determine the intent of the contracting parties, whenever possible, the express language of the contract should control."). We find that Surety was required to step in to correct defective work under the terms of the performance bond, notwithstanding Phil-Guam's completion of the construction contract, if Phil-Guam's right to correct the defects was properly terminated.

C. Termination of Contractual Rights

[15] The performance bond provides: "If there is no Owner default, the Surety's obligation shall arise after . . . [t]he Owner has declared a Contractor Default and formally terminated the Contractor's right to

complete the contract.” Appellants’ Excerpt of Record, p. 29 (Performance Bond, §§ 3, 3.2). Contractor default is defined by the performance bond as: “Failure of the Contractor, which has neither been remedied nor waived, to perform or otherwise comply with the terms of the Construction contract.” Appellants’ Excerpts of Record, p. 30 (Performance Bond, § 12.3).

[16] Turning to the O’Neill and Murphy declaration of default, it states:

On November 28, 1995 we had a pre-default hearing to resolve construction problems at our house. Nine months has expired since our pre-default meeting, and the contractor has communicated through his lack of response and lack of action that he has no interest in conscientiously correcting the construction problems.

This letter will serve to inform you that we are formally declaring Phil-Guam Builders Corporation in **DEFAULT** due to failure to repair the leaking windows and cracking walls. We hereby request the Surety to take the necessary action to permanently repair our home as expeditiously as possible.

Appellants’ Excerpts of Record, p. 118 (O’Neill and Murphy Default Declaration). The trial court found that this declaration did not formally terminate Phil-Guam’s right to complete the contract. We disagree.

[17] It was Phil-Guam’s right and obligation under article 18 of the construction contract to correct defective work even after substantial completion of the contract. While the default letter did not state explicitly that Phil-Guam’s right to repair the defects was terminated, the letter did state that Phil-Guam failed to repair the defects and had no interest in correcting the problems. Thus, the declaration indicates that O’Neill and Murphy, at the very least, considered the contract abandoned by Phil-Guam and that Surety was to proceed with the necessary repairs. The declaration also explicitly declared a default. With regard to such default declarations, “it is vital that the declaration be made in terms sufficiently clear, direct, and unequivocal to inform the surety that the principal has defaulted on its obligations and the surety must

immediately commence performing under the terms of its bond.” *L & A Contracting Co. v. S. Concrete Services, Inc.*, 17 F.3d 106, 111 (5th Cir. 1994). We find that the O’Neill and Murphy default declaration meets this standard and that it terminated Phil-Guam’s right to correct the defective work. The court cannot ignore the undisputed evidence that the owners and Surety repeatedly contacted Phil-Guam to repair the defects, that Phil-Guam made numerous unsuccessful repair attempts, and that default was declared after Phil-Guam failed to respond.

[18] We note that the trial court found that O’Neill and Murphy were not the correct parties to declare a default under the performance bond because the bond named Guam Savings & Loan as owner, and under section 3.2 of the bond, the “owner” must declare a contractor default and formally terminate the contractor’s right to complete the contract. We disagree.

[19] While the performance bond identifies only Guam Savings & Loan as owner, we find there is ambiguity as to the actual owner. The performance bond defines the construction contract as: “[t]he agreement between the Owner and the Contractor identified on the signature page, including all contract documents and changes thereto.” Appellant’s Excerpts of Record, p.30 (Performance Bond, § 12.2). Turning to the construction contract, the owners are listed as Jan Mansfield (O’Neill) and Ernest Murphy. Appellant’s Excerpts of Record, pp. 20, 27 (Construction Contract). The construction contract was signed by Mansfield and Murphy, not by Guam Savings & Loan. Thus, the language within the performance bond in part recognizes that the owners were Mansfield and Murphy.

[20] Furthermore, the purpose of the performance bond, as set forth in the request for bonding, was “[f]or the construction of a three story two bedroom residence to be located on Lot no. 13 Block no. 16, Santa Rita, Guam and belonging to Janice C. Mansfield and Ernest A. Murphy.” Appellees’ Supplemental

Excerpts of Record, index 1 (Request for Bonding). The performance bond was intended to guarantee construction of a home pursuant to the terms of the construction contract so that Murphy and O'Neill could receive the object of that contract. Thus, the performance bond was meant to benefit O'Neill and Murphy. Guam law provides third party beneficiaries the right to enforce a contract made for their benefit. "A contract, made expressly for the benefit of a third person, may be enforced by him at any time before the parties thereto rescind it." Title 18 GCA § 85204 (1992). We find that O'Neill and Murphy were the correct parties to declare a default under the terms of the performance bond.

D. Contractual Limitations Period

[21] The trial court found that Surety did not act in good faith when it sought to recover costs incurred in repairing damages from the leaky windows after the expiration of the contractual one year limitations period. We disagree. Article 18.1 of the construction contract provides in relevant part:

The Contractor shall promptly correct Work rejected by the Architect or failing to conform to the requirements of the Contract Documents, whether observed before or after Substantial Completion and whether or not fabricated, installed or completed, and shall correct any Work found to be not in accordance with the requirements of the Contract Documents within a period of one year from the date of Substantial Completion of the Contract

Appellants' Excerpts of Record, p. 25 (Construction Contract, Article 18.1). Article 18.2 provides:

Nothing contained in this Article 18 shall be construed to establish a period of limitation with respect to other obligations which the Contractor might have under the contract Documents. Establishment of the time period of one year as described in Paragraph 18.1 relates only to the specific obligation of the Contractor to correct the Work, and has no relationship to the time within which the obligation to comply with the Contract Documents may be sought to be enforced, nor to the time within which proceedings may be commenced to establish the Contractor's liability with respect to the Contractor's obligations other than specifically to correct the Work.

Appellant's Excerpts of Record, p. 25 (Construction Contract, Article 18.2). Article 18.2 clarifies the one year period and expressly provides that it is an obligation upon the contractor and does not affect the time within which obligations of the contractor may be enforced or proceedings commenced to establish the contractor's liability. Thus, article 18 is actually a warranty requiring Phil-Guam to correct defective work even after substantial completion.

[22] Case law on such warranty provisions supports this position. “[A]n express warranty against defects for a limited period of time does not act as a limitation upon the obligation to perform the contract in a workmanlike manner.” *Tonkin v. Bob Eldridge Const. Co.*, 808 S.W.2d 849, 853 (Mo.App. 1991). “[T]he twelve-month guarantee should not be interpreted as a limitation upon the contractor's liability for defective work . . . a provision requiring corrections of defects appearing within a year is actually ‘an added guarantee, inserted in the contract to extend rather than limit the contractor's liability for faulty construction. As such, it does not prescribe the owner's exclusive remedy, and it in no way impairs the contractor's general obligation to perform his contract in a proper, workmanlike manner.’” *Norair Eng'g Corp. v. Saint Joseph's Hosp. Inc.*, 249 S.E.2d 642, 647 (Ga.App. 1978) (quoting *Burton-Dixie Corp. v. Timothy McCarthy Const. Co.*, 436 F.2d 405, 410-11 (5th Cir. 1971)). In the instant case, we find that article 18 is not a contractual time limitations period to bring an action against Phil-Guam.

[23] Under the undisputed facts, Phil-Guam was notified of the leaky windows on June 5, 1995. The occupancy permit was issued less than three months prior, on March 25, 1995. Thus, the defect was discovered and Phil-Guam was notified well within the twelve month limit set forth in article 18.1. Phil-Guam had the responsibility and the right to make the repairs within twelve months of substantial completion, which in this case was signified by issuance of the occupancy permit. Article 18 prescribes

Phil-Guam's duty to make the repairs for defective workmanship detected within twelve months of substantial completion. It does not limit the time in which Phil-Guam faces liability for failing to make the repairs within the twelve months. We note that the performance bond does contain a limitations period, which the Ronquillos argue bars the claim against them. The provision states in part:

Any proceeding, legal or equitable, under this Bond may be instituted in any court of competent jurisdiction . . . shall be instituted within one year after Contractor default or within one year after the Contractor ceased working or within one year after the surety refuses or fails to perform its obligation under this Bond, which ever occurs first.

Appellants' Excerpts of Record, p. 30 (Performance Bond, § 9). As it relates to the facts of this case, section 9 provides that the owner was required to bring legal action against Surety within a year from when the contractor defaulted or ceased working, whichever occurred first, if Surety refused to perform. In this case, Surety performed after default was declared and the owners had no need to bring action against Surety. Moreover, Surety's counter-claim against Phil-Guam was based upon the indemnity agreement. Thus, section 9 is irrelevant to this case.

E. Statute of Limitations

[24] The trial court found that 5 GCA § 32501(d) limited Surety's responsibility to a period of one year following issuance of the occupancy permit. We disagree. This section states:

No bonding company which is bonding a contractor constructing a new home shall be responsible for any of the warranties set out in this section for breaches which occur more than one (1) year after the date the certificate of occupancy is issued for the home by the Department.

Title 5 GCA § 32501(d) (1996). Section 32501 sets out certain statutory implied warranties which are

to be distinguished from expressed contractual warranties.² The one year limit in section 32501(d) pertains to breaches of the implied warranties and is not a statute of limitations restricting the time within which a suit is required to be filed.

[25] Moreover, we interpret a breach of an implied warranty under section 32501(d) to include the discovery of a defect in construction. If the defect or breach occurs one year after substantial completion, the bonding company faces no responsibility. To find as the trial court suggests would mean that a contractor could be notified of a defect immediately after substantial completion but continue ineffective repair work for a year, thus relieving itself and the bonding company of any liability and leaving the owner with no protection.

[26] In this case, the record shows substantial completion on March 25, 1995, upon the issuance of the occupancy permit, and that Phil-Guam was notified of the defective windows in June 1995. Thus, under

² Section 32501 provides in pertinent part:

(a) A new home has the following implied warranties:

(1) That the home was built in a workmanlike manner of suitable new materials of at least average quality, and that any exceptions thereto were communicated to the purchaser thereof in a separate writing signed by the purchaser before he occupied the home. Compliance with this subsection (1) shall not excuse compliance with any other warranty.

(2) That the home was built according to plans and specifications filed with Department of Public Works (the "Department"), and that the home fully complies with all laws, the Building Code and all rules and regulations relating thereto. The failure of a building inspection to detect noncompliance with plans, laws, or rules and regulations, the Building Code, or specifications shall not be a defense to a claim under this warranty.

(3) If the home was purchased from a developer who supplied both the lot and the home to the purchaser and did not build on a lot supplied by the purchaser, there is a warranty that the home will not flood for a period of five (5) years, in the absence of any negligence by the homeowner.

(4) In addition to the foregoing warranties, the home is warranted against all defects of construction, materials, and workmanship for eighteen (18) months.

....

5 GCA § 32501(d), Surety's potential liability attached because the defect was discovered within a year of substantial completion.

F. Salvage Value

[27] In the event this court were to hold for Surety, the Ronquillos requested that this court offset the salvage value of the replaced windows from the costs incurred in the repairs. However, aside from the testimony of O'Neill: "I think it was \$30,000.00 – thirty-some thousand dollars," Transcript vol. II, p. 32 (Bench Trial, Jan. 24, 2001), there was no evidence presented by the Ronquillos as to the actual salvage value of the replaced windows. The Ronquillos failed to call any witnesses or provide evidence to contest the reasonableness of the amount spent by Surety on the repairs. Aside from noting O'Neill's testimony, the trial court made no factual finding as to the salvage value of the windows. Thus, we are unable to make any offset of the value of the windows from the amounts claimed by Surety. At argument in this appeal, Surety waived its claim to the \$320 inspection fee charged to the Ronquillos. This amount shall be deducted from the total claimed by Surety.

G. Attorney's Fees

[28] Surety requests attorney's fees pursuant to section 3 of the indemnity agreement. Section 3 expressly provides that the Ronquillos pay attorney's fees in connection with any legal action brought against them under the indemnity agreement. Appellants' Excerpts of Record, p. 16 (Indemnity Agreement, § 3). Because we hold in favor of Surety on its counter-claim, which was based upon the indemnity agreement, we find that Surety is entitled to attorney's fees including fees incurred in prosecuting this appeal. *See Citizen's Sec. Bank (Guam), Inc., v. Bidaure*, 1997 Guam 3, ¶¶ 22-23 (finding attorneys fees justified by the express language in a guaranty and including attorney's fees on appeal).

IV.

[29] Phil-Guam breached the terms of the construction contract by not building a residence of workmanlike quality. This breach amounted to a default of the construction contract. Under the performance bond, Surety's responsibility extended to correction of defective work of the contractor. We find that the requirements of the performance bond were met in the declaration of default by the owners and the assumption by Surety of Phil-Guam's duty to repair the defects. We hold that Surety is entitled to judgment in the amount claimed, less \$320 for the unjustified inspection fee, plus pre-judgment interest as allowed by the indemnity agreement, and attorney's fees

[30] The judgment of the trial court in favor of the Ronquillos is **REVERSED**. The case is **REMANDED** to the trial court for entry of judgment in favor of Surety, calculation of damages and attorneys fees, and for further proceedings on the foreclosure of the mortgage consistent with this opinion.

BENJAMIN J. F. CRUZ
Justice *Pro Tempore*

F. PHILIP CARBULLIDO
Associate Justice

PETER C. SIGUENZA, JR.
Chief Justice