

REPUBLIC OF THE PHILIPPINES
GOVERNMENT PROCUREMENT
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NPM No. 044-2004

March 30, 2004

Mr. EDGARDO MANDA
General Manager
Manila International Airport Authority
MIA Road, Pasay City
Metro Manila

Re : Retention Money as a Form of Warranty under Republic Act No. 9184 ("R.A. 9184") and its Implementing Rules and Regulations Part A ("IRR-A")

Dear Mr. Manda :

This refers to your letter dated January 29, 2004, which we received on February 2, 2004, requesting for clarification on these issues:

a) Whether or not warranty retention money may be imposed to cover for the warranty of the following items:

- (1) Gasoline for Manila International Airport Authority ("MIAA") vehicles;
- (2) Construction/Electrical/Electronic/Mechanical materials procured in cases of emergency and in small volume;
- (3) Office supplies such as papers, folders, books, paper clips, tissue paper, ink cartridges, toner etc.,
- (4) Chemicals for building maintenance;
- (5) Spare parts for immediate replacement; and
- (6) Printing of office forms, tickets, etc.

b) Whether or not the commencement of the warranty period is upon delivery or final acceptance by the MIAA of the subject goods.

This request was made in connection with the complaints raised by suppliers regarding the retention of ten percent (10%) of MIAA's procured supplies in compliance with Section 62 of R.A. 9184, otherwise known as the "Government Procurement Reform Act" ("GPRA") and Section 62.1 of the IRR-A.

Retention Money or Special Bank Guarantee Required to Cover Warranty for the Procurement of Goods

To protect the proprietary interest of the Government, the crafters of R.A. 9184 and its IRR-A deem it necessary to insert an innovative provision that will provide for guarantee and immediate indemnity in case the goods or the construction works procured are found to be defective or of substandard quality. Thus, the GPRA and its IRR-A contain special provisions on warranty in the procurement of goods and infrastructure projects which provide for an upfront or forward assurance that the supplier, manufacturer, or distributor warrants the goods from hidden defects and the procuring entity against eviction therefrom, whereby the happening of any, works as a signal for the procuring entity to call on the retention money or bank guarantee. For the procurement of goods, Section 62. 1 of the IRR-A explicitly provides:

For the procurement of goods, in order to assure that manufacturing defects shall be corrected by the supplier, manufacturer or distributor, as the case may be, a warranty shall be required from the contract awardee for a minimum period of three (3) months, in the case of supplies, and one (1) year, in the case of equipment, after performance of the contract. The obligation for the warranty shall be covered by either retention money in an amount equivalent to at least ten percent (10%) of every progress payment, or a special bank guarantee equivalent to at least ten percent (10%) of the total contract price. The said amounts shall only be released after the lapse of the warranty period: *Provided, however,* That the goods supplied are free from patent and latent defects and all the conditions imposed under the contract have been fully met. (Underscoring supplied)

By virtue of this provision, procuring entities are now mandated to retain a part of the contract price, or require a bank guarantee from its suppliers, manufacturers or distributors in the procurement of goods. This provision is generic in application and provides for no exception such that even procurement of goods in small amounts and quantity including those acquired through the alternative methods of procurement are subject to this requirement. It must be noted that the above-quoted section has no specific price threshold as to when warranty for goods may be applicable, likewise, it does not restrict the application of warranty exclusively to goods procured under competitive bidding.

Accordingly, when MIAA retained ten percent (10%) of the contract price for the supplies it procured, it was just exercising its legal right within the bounds of the GPRA and its IRR-A. We therefore see no irregularity that would justify and substantiate the complaints of the suppliers. Undoubtedly, there is valid and lawful reason for MIAA to

impose the retention money equivalent to ten percent (10%) of the contract price, to cover for warranty of the goods procured.

However, to properly guide you in the application of said provision and to avoid further complaints from suppliers in the future, we want to emphasize the prominent features of Section 62.1 of the IRR-A, to wit:

First, warranty under said section applies only to the procurement of goods, which refer to all items, supplies, materials and general support services, except consulting services and infrastructure projects, which may be needed in the transaction of public businesses or in the pursuit of any government undertaking, project or activity, whether in the nature of equipment, furniture, stationary, materials for construction, or personal property of any kind, including non-personal or contractual services.

Second, the IRR-A provides that warranty period for goods is for a minimum period of three (3) months for supplies and one (1) year for equipment, which will commence after performance of the contract. This connotes that the procuring entity may impose a longer warranty period depending on the nature of goods, but it cannot shorten the said specified periods;

Third, the warranty for goods shall be covered by either a retention money or a special bank guarantee. No other arrangements or credit instruments are allowed;

Fourth, the amount of retention money should be equivalent to at least ten percent (10%) of every progress payment and, in case of special bank guarantee, it shall be equivalent to at least ten percent (10%) of the total contract price. This denotes that the procuring entity may impose a higher percentage amount of the progress payment or contract price to cover for the warranty but not lower than the percentage provided by the IRR-A ; and

Lastly, the retention money or bank guarantee shall only be released after the lapse of warranty period, provided that the goods supplied are free from latent and patent defects and satisfies the conditions of the contract.

Commencement of the Warranty Period under Section 62.1 of the IRR-A of R.A. 9184

Section 62.1 of the IRR-A specifies when the warranty period shall commence, thus:

“For the procurement of goods, in order to assure that manufacturing defects shall be corrected by the supplier, manufacturer or distributor, as the case may be, a warranty shall be required from the contract awardee for a minimum period of three (3) months, in the case of supplies, and one (1) year, in the case of equipment, **after performance of the contract.**”

Based on the above-cited provision, the warranty period of three (3) months for supplies and one (1) month for equipment shall begin after the performance of the

contract. In other words, the reckoning point for the commencement of warranty period in the procurement of goods is not on the date of actual delivery of goods procured or final acceptance of the procuring entity concerned, as you suggest, but it is on the date of the consummation of the contract. However, in order to determine the instance when a contract for procurement of goods is consummated, we have to refer to the specific provisions of the Civil Code on the Contract of Sale, which have supplementary application to this type of government contract.

Under the Law on Sales, a contract of sale is consummated upon compliance of the buyer and seller with their reciprocal obligations, which consists of delivery and transfer of determinate thing, on the part of the seller, and payment therefor of a price certain in money or its equivalent, on the part of the buyer.¹ Accordingly, in the procurement of goods by the government, a supplier, manufacturer or distributor, stands as a seller who is obliged to transfer ownership of the goods to the procuring entity concerned, which is the fundamental aim of the contract.² Under the law, ownership of the goods is usually transferred upon delivery, as stated by Article 1496 of the Civil Code which provides:

Art 1496. The ownership of the thing sold is acquired by the vendee from the moment it is delivered to him in any of the ways specified in articles 1497 to 1501, or in any other manner signifying an agreement that the possession is transferred from the vendor to the vendee.

On the other hand, the procuring entity, as a buyer, is reciprocally bound under the law to accept and pay the price of the goods delivered.³ However, the law accords the buyer the right to a reasonable opportunity to examine the goods to ascertain whether they are in conformity with the contract⁴ before it accepts the same.⁵

In fine, a government contract for the procurement of goods is deemed consummated after the goods have been delivered by the manufacturer, supplier or distributor and the procuring entity has accepted and paid the same.⁶ Accordingly, it is only upon the concurrence of these two reciprocal and bilateral acts that the warranty period under Section 62.1 of the IRR-A commences and the retention money or bank guarantee becomes enforceable. In sum, after delivery of the goods procured, the procuring entity is bound to accept the goods, if it finds the goods in conformity with the contract, and pay its price with the right to retain a part thereof or require a special bank

¹ Article 1458 of the Civil Code.

² Paras, Civil Code of the Philippines, Volume V (1995) citing 3 *Castan* 12-13

³ Article 1582 of the Civil Code.

⁴ Article 1584 of the Civil Code.

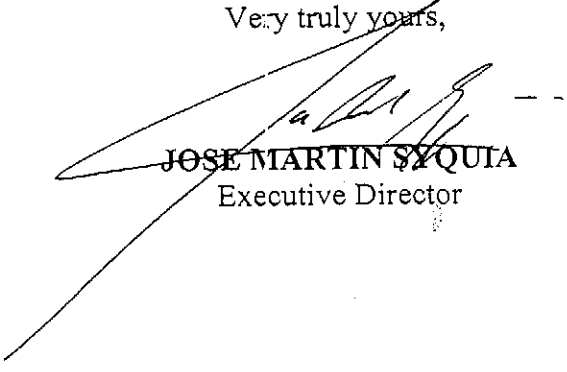
⁵ It must be noted that in the absence of express or implied agreement of the parties, acceptance of the goods by the buyer, shall not discharge the seller from liability in damages or other legal remedy for breach of any promise or warranty in the contract of sale (Article 1586 of the Civil Code) and the buyer is allowed to set up the breach of the warranty as a set-off or counterclaim for the price (Paras, Civil Code of the Philippines, Volume V (1995), p. 228, citing *William v. Perrota*, 95 *Conn.* 529).

⁶ It may be agreed upon by the parties that delivery shall be by installments, pursuant to Article 1583 of the Civil Code. If this is the case, there shall be partial performance of the contract through delivery by installments on the part of the seller, and progressive payment on the part of the buyer. In this arrangement, the warranty period for the goods delivered by installments shall commence after these have been delivered and partially paid. Take note that the retention money is equivalent to ten percent (10%) of every progress payment, however, if the procuring entity opt to require a special bank guarantee instead, such must be ten percent (10%) of the total contract price as provided under Section 62.1 of the IRR-A of R.A. 9184.

guarantee of ten percent (10%) of the contract price to cover for the warranty. From thereon, the warranty period begins to run.

Anent all the foregoing, we trust that your queries have been sufficiently addressed. Please bear in mind that this opinion is being rendered on the basis of the facts and particular circumstances as represented. It may not be necessarily applicable upon a different set of facts or circumstances.

Very truly yours,

A large, stylized handwritten signature in black ink, written over the typed name and title.

JOSE MARTIN SYQUIA
Executive Director