

REPUBLIC OF THE PHILIPPINES
GOVERNMENT PROCUREMENT POLICY BOARD
Technical Support Office
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NPM No. 054-2004

April 20, 2004

MR. RODOLFO L. SERRANO
Proprietor
EJR Engineering & Consultancy
Navotas, Metro Manila

Re: Queries on Republic Act No. 9184 and its Implementing Rules and Regulations Part A

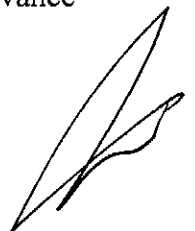
Dear Mr. Serrano:

This refers to your letter dated January 30, 2004, addressed to Honorable Secretary Emilia T. Boncodin as Chairperson of the Government Procurement Policy Board ("GPPB"), which was referred to our office on February 5, 2004 requesting for clarification on some matters regarding Republic Act No. 9184 ("R.A. 9184") and its Implementing Rules and Regulations Part A (IRR-A). In your letter, you raised some concerns summarized as follows:

1. Are procuring entities legally authorized to demand a counter part insurance bond in an amount double of what it has paid as an advance payment on the project?
2. Can procuring entities require that the bank certification should include the statement: *"that the credit line shall be release only when the Project had been completed and authorized by the procuring entity"*? What is the intention of the law with regard to the credit line as required under Section 23.6 (f) of the IRR-A of R.A. 9184?
3. What is the rationale for the imposition of liquidated damages in government contracts?

Advance Payment under Annex "E" of the IRR-A of R.A. 9184

Under the Contract Implementation Guidelines for the procurement of Infrastructure Projects of the IRR-A of R.A. 9184, Annex "E", the procuring entity may make advance payment to contractors as provided in Section 4 (1) thereof, to wit:



The procuring entity shall upon a written request of the contractor which shall be submitted as a contract document, make an advance payment to the contractor in an amount equal to fifteen percent (15%) of the total contract price, to be made in lump sum or, at the most, two installments according to a schedule specified on the Instruction to Bidders and other relevant Tender Documents.

Advance payment made on the contract is a form of financial assistance that the Government extends to the contractor, upon his request, before he commences work on the project contracted for as working capital for particular infrastructure projects, whether major, urgent or otherwise, as necessitated by the complexity of present-day Government contract administration. Such financial help is calculated to encourage contractors to comply faithfully with their contractual obligations and to forestall any delay in the accomplishment of the work under the contract¹.

However, as a form of security for the advance payment made by the procuring entity, the contractor is required to submit an irrevocable standby letter of credit of equivalent value from a financial bank, a bank guarantee or a surety bond. Annex "E" of the IRR-A of R.A. 9184, Section 4 (2) provides:

The advance payment shall be made only upon the submission to and acceptance by the procuring entity of an irrevocable standby letter of credit of equivalent value from a commercial bank, a bank guarantee or a surety bond callable upon demand, issued by a surety or insurance company duly licensed by the Insurance Commission and confirmed by the procuring entity. (Emphasis supplied)

It is clear from the above-quoted provision that the irrevocable standby letter of credit, bank guarantee or surety bond which a contractor must submit as a condition precedent for advance payment should be equivalent to the value of such advance payment made by the procuring entity considering that such stands as a security for the re-payment of money upfront on the contract price.

In view of the foregoing, and taking into consideration the purpose of advance payment, which is to provide financial help to contractors to expedite the completion of a particular government infrastructure project, we see no logical basis for a procuring entity to require that the security for the advance payment to a contractor concerned be double the value thereof. Evidently, this requirement is more onerous for the contractors as it adds difficulty for them in availing of the benefits advance payment will provide.

Thus, pursuant to the underlying rationale of the provisions of Annex "E" of the IRR-A of R.A. 9184 on advance payment, we recommend that a procuring entity should avoid prescribing a higher amount for the letter of credit, bank guarantee or surety bond that stands as a security for the advance payment made. This requirement shall be in contravention with the law since it goes beyond the maximum amount of security set by R.A. 9184 and its IRR-A, Annex "E", No. 4 (2).

¹ Bartolome C. Fernandez, A Treatise on Government Contracts under Philippine Law, 2001 Ed., p. 115

Eligibility Check for the procurement of goods and infrastructure projects

Prospective bidders are required to comply with the minimum eligibility criteria as provided under the IRR-A of R.A. 9184. One of the financial documents that should be submitted in order to comply with the eligibility requirements is provided under Section 23.6 (f) of the IRR-A of R.A. 9184, to wit:

The prospective bidder's computation for its Net Financial Contracting Capacity (NFCC) which shall be in accordance with Section 23.11 of this IRR-A; or **a commitment from a licensed bank to extend to it a credit line if awarded the contract to be bid**, or a cash deposit certificate, in an amount not lower than set by the procuring entity in the Bidding Documents, which shall be at least equal to ten percent (10%) of the approved budget for the contract for the contract to be bid. (emphasis supplied)

The submission of a commitment from a licensed bank to extend a credit line to the prospective bidder establishes its financial capacity to absorb the additional obligations it may incur in connection with the contract to be bid, thus, assuring the procuring entity that in case the contract has been awarded to such bidder, the bidder shall be able to comply faithfully with its contractual obligations. The commitment from a licensed bank to extend a credit line serves as a guarantee for the procuring entity since it indicates a bank's willingness to extend credit to the bidder in case the bidder is in need of any financial assistance during contract implementation so as not to disrupt the completion of the project.

For this reason, the bank's commitment to extend a credit line in favor of the contractor should be existent and available until the completion of the project so that the contractor could draw cash from the credit line, if necessary as to ensure faithful and complete performance of the work as specified in the contract documents.

Recovery of Liquidated Damages

Liquidated damages, as a form of indemnification under the Civil Code, may be recovered in case of breach by a party of any of the stipulation, agreement or covenant in the contract. The same concept is applied under Annex "E" of the IRR-A of R.A. 9184, such that when the supplier fails to complete the works required within the contract time, he will be held liable for liquidated damages. Section 8 (1) thereof provides:

Where the contractor refuses or fails to satisfactorily complete the work within the specified contract time, plus any time extension duly granted and is hereby in default under the contract, the contractor shall pay the procuring entity for liquidated damages, and not by way of penalty, an amount to be determined in accordance with the following formula until the work is completed and accepted or taken over by the procuring entity: (Emphasis supplied)

The liquidated damages that may be imposed by the procuring entity upon the contractor does not depend on the damage incurred by the procuring entity. In fact, the procuring entity need not prove actual damage in order to collect such liquidated damages as provided by Section 8 (3) of Annex "E" of the IRR-A of R.A. 9184, to wit:

To be entitled to such liquidated damages, the procuring entity does not have to prove that it has incurred actual damages. Such amount shall be deducted from any money due or which may become due the contractor under the contract and/or collect such liquidated damages from the retention money or other securities posted by the contractor whichever is convenient to the procuring entity. (Emphasis supplied)

It must not be forgotten that liquidated damages for delay incurred by the contractor in the completion of the work under a Government infrastructure contract is a regulatory imposition which has to be complied with. Such provision is read to all government contracts for the protection of the procuring entity and as an assurance that it is immediately compensated without further proof for the damages it suffers in case the contractor delays to continue the works through his fault.

Thus, considering that liquidated damages is just a form of indemnity in contracts sanctioned by law, which has gained wide acceptance in the commercial world and in the area of government procurement, we see no inequity or unfairness for the imposition of such.

With the foregoing elucidations, we trust that our opinion has provided your office with the needed information relevant to government procurement.

This opinion is being rendered on the basis of the facts and particular circumstances as represented. It may not necessarily be applicable upon a different set of facts or circumstances.

Very truly yours,



JOSE MARTIN C. SYQUIA
Executive Director