

# **CIAP DOCUMENT 102**

## **UNIFORM GENERAL CONDITIONS OF CONTRACT FOR PRIVATE CONSTRUCTION ANNOTATIONS WITH CASE SYNOPSES AND JURISPRUDENCE**

This document offers descriptions and explanations on the provisions in **CIAP Document 102—the Uniform General Conditions of Contract for Private Construction in the Philippines**, citing relevant jurisprudences on the practical application of the laws and construction industry practices, with synopses of cases decided by the Supreme Court.

The purpose of this document is to familiarize the readers with the key provisions in construction contracts, highlighting the respective rights and obligations of the contracting parties and providing the procedures, guidelines, and the criteria to be used in situations that normally arise or may possibly happen during project implementation. Each section contains the gist of the provisions offered therein underscoring the importance of each of them and citing relevant jurisprudence to guide the readers on how to ascertain, prevent, and manage risks and issues in construction projects. The case briefs are presented to give the readers a grasp of the circumstances surrounding the issues and to give them insights on the practical application of the laws, the industry practice, and the provisions in CIAP Document 102, in the interpretation of ambiguities of the contract and filling in the omission of provisions which are ordinarily established.

## CIAP DOCUMENT 102

### UNIFORM GENERAL CONDITIONS OF CONTRACT FOR PRIVATE CONSTRUCTION

This document specifies general conditions of contract between a private Owner and Contractor applicable to the construction of any type of structure or works as contemplated in Republic Act No. 4566 otherwise known as the Contractors' License Law.

CIAP Document 102 contains conditions or stipulations ordinarily established in construction contracts in the Philippines, which reflect the usages and customs in the Philippine construction industry. It is envisaged for a *traditional contract* whereby the contractor is not responsible for the design, meaning, the Project Owner hire Consultants, who can be an Engineer, an Architect, or Construction Manager or Project Manager, to prepare the contract documents such as the plans, specifications, bill of quantities, the construction agreement, and others, and bids out the project to pre-qualified Contractors. It is intended to have suppletory application to private construction contracts to resolve apparent conflicts in the provisions of contract documents or to be used as general conditions in the absence of one.

#### Section I Definitions and Documents

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##### Article 1 Definitions

This provision contains the customary definition of the terms used in the Contract documents.

Words that are capitalized or begin with a capital letter refer to a specific term, name, expression or document which shall have no other meaning other than the meaning as provided for in this article, and which shall be used and referred to as such in all of the Contract documents.

##### Article 2 Execution, Correlation, Meaning of Terms, and Intent of Documents

The purpose of this article is to provide the correlation, meaning, and intent of the contract documents pertaining to all labor, materials, and equipment necessary for the proper execution of the Work and the rules in the interpretation of the provisions of Contract documents in cases where there is an ambiguity, conflict, error, or omission in any of them.

This provision highlights the duties and responsibilities of the Owner and the Contractor with regards to the accuracy of all the drawings, specifications, and all documents comprising the Contract. Any

inconsistency or omission in any of the Contract documents should be properly addressed, clarified and corrected in a timely manner to insure the efficient and timely execution of the works. It underscores the implied duty of *good faith and fair dealing* expected upon the parties in the exercise of their duties and responsibilities under the Contract. Since this document contemplates a *traditional* or *build contract* where all the Contract documents are provided by the Owner, the Contractor has the duty to report to the Owner any error or discrepancy or omission in the Contract documents, and the Owner to resolve in a timely manner taking due regard of the construction schedule and Contract Completion Time.

The principle of *good faith and fair dealing* is often applied by the Courts in ascertaining the facts and circumstances surrounding the issues brought before them for decision. The Supreme Court defined “good faith” as:

*“an intangible and abstract quality with no technical meaning or statutory definition, and it encompasses, among other things, an honest belief, the absence of malice and the absence of design to defraud or to seek an unconscionable advantage. It implies honesty of intention, and freedom from knowledge of circumstances which ought to put the holder upon inquiry. The essence of good faith lies in an honest belief in the validity of one’s right, ignorance of a superior claim and absence of intention to overreach another.”*

Where due to errors, omission, or discrepancy in the Drawings, Specifications, or any of the Contract documents extra work, would be necessary, the Owner is required to issue a Change Order indicating the corresponding adjustments of Contract Time and Contract Price. This should be read in conjunction with Articles 20.7 [Changes in the Work] and 21.04 [Extension of Time].

## **Section II    Laws, Regulations, Site Conditions, Permits & Taxes**

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This section delineates the duties and responsibilities of the Owner and the Contractor in doing the preliminary works necessary for the project to ensure compliance with all laws that are binding upon or affect the parties to the Contract and to the Work, such as the provision of utilities for construction (water, electricity, gas, and communication), survey of site conditions prior to commencement of the works, and securing and payment of construction permits, licenses and taxes.

It is expected that the Contractor has complied with the requirement for bidding which is to visit the site before the bidding and assess the

physical conditions based on the survey results furnished by the Owner, such that its estimate or bid would have already included the costs of the facilities and other contingencies and incidental expenses deemed necessary. The Owner is liable for any damage suffered or cost incurred by the Contractor due to errors in the data furnished to it. In case of variations in the physical or subsurface conditions from those shown in the Drawings or in the Specifications or in any of the Contract Documents, and if such would entail change in the work, whether as deductive or additive work, the Owner shall issue a Change Order covering such change and the Contractor shall be entitled to adjustments in Completion Time and Contract Price as provided for under Articles 20.06 [*Increased or Decreased Quantities of Work*], 20.07[B] [*Change of Sub-surface Conditions*], and 21.04 [*Extension of Time*].

This section delineates the responsibility of the parties in securing and paying construction permits, licenses, and taxes, and balances the parties' risks and accountabilities in case of delay, default, or neglect in performance. The duty of the Contractor is to assist the Owner in securing the permits and licenses necessary for the Work, but it is the Owner who shall pay for the costs.

### **Section III Equipment and Materials**

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This section sets-out the requirements of the Contract as to the quality of materials and equipment necessary for the Work, ensuring strict compliance with the Specifications and all statutory and regulatory laws that are in force and applicable during the period of construction.

Samples of all materials, equipment, fixtures, appliance and fittings necessary for the Work shall be approved by the Owner, such that no materials and equipment shall be used or installed without passing the tests required in the Contract [*Article 10.03, Testing Samples of Materials*] and without the expressed approval of the Owner. Such requirement is also applicable for substitute materials and equipment where written notice of approval by the Owner is required. The Owner's action/approval on the samples shall be made within seven (7) working days after submission by the Contractor. Said samples shall be available at the site for inspection by the Owner.

The Contractor shall be responsible for materials and equipment which were used or installed without the approval of the Owner; and if such were found to be not conforming with the Specifications, under Article 20.03, they shall be considered defective. The Owner

may, as provided for under Article 20.04, examine the work done and require tests to ensure compliance by the Contractor with the Specifications. In *Deiparine vs. CA and Trinidad* <sup>[1]</sup>, it was held that though the Contract documents do not require concrete stress test, the Owner has the right to require a test to verify the structural soundness of the building constructed, in view of the Contractor's disregard of the Owner's instruction to get approval of the samples of the cement mixture prior to pouring and the inconsistencies in the results of the cylinder tests. The Supreme Court ruled that it was rational for the Owner to require such test as it was the only means by which it could ascertain the Contractor's faithful compliance with the Specifications and the integrity of the building constructed. The structure failed in the concrete core test, thus, justifying Owner's rescission of the Contract.

## **Section IV Premises and Temporary Structures**

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This section defines the responsibilities of the Contractor in maintaining the safety and sanitation of the work premises and in providing temporary facilities for storage of materials and apparatus, temporary office, and housing for workers with basic utilities for water, electricity and lighting, telephone, and sanitary facilities.

All temporary facilities, signages and structures must be approved by and must be done in the manner acceptable to the Owner. Strict compliance with Republic Act No. 11058 (*An Act Strengthening Compliance with Occupational Safety and Health Standards and Providing Penalties for Violations Thereof*) and its Implementing Rules and Regulations (IRR), should be the main consideration in this section as it provides the guidelines for ensuring safety and health in the work environment and in preventing loss or damage to lives and properties during construction. This should be read in conjunction with Article 30 [*Contractor's Responsibility for Accidents and Damages*].

The removal of these temporary facilities and structures is provided in Article 20.09 [*Cleaning up at Completion of Work*]. Under this article, the Contractor is required to remove all these temporary facilities and structures. The Owner may opt to keep any of these temporary facilities and structures, subject to appropriate compensation and as stipulated in the Contract.

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<sup>[1]</sup> *Deiparine vs. CA and Trinidad*, G.R. No. 96643, April 23, 1993

## **Section V Protection of Work and Property**

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This section defines the obligations of the Contractor to protect the Work and the Owner's property and any existing and adjacent properties, utilities, vegetation and waterways or drainage. The Contractor shall be liable for all damages which may result from its act or neglect.

This shall be read in conjunction with Article 30 [*Contractor's Responsibility for Accidents and Damages*] and Section II on the requirement for survey of site condition.

## **Section VI Labor, Work and Payments**

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The purpose of this section is to ensure that appropriate and efficient methods are used to ensure completion of the Work of the required quality within the completion time, and that the Contractor is paid for work accomplished.

### **Article 19 Labor**

Under this article, the Contractor is required to employ only qualified and competent workers for the project to ensure the quality of the Work.

### **Article 20 Work**

The purpose of this article is to ensure that the Contractor is paid for Work completed and for the Owner to retain a portion of the Contract Price, when the retained amount and the Performance Bond, are not sufficient to complete the Work without additional cost to the Owner.

Presented in detail under this article are the conditions affecting the scope of Work, the quality of the Work, and the effects on Contract Price and Completion Time if there are changes in the Work.

On the scope of the Work:

This provides that any change in the Work shall be covered by a Change Order which shall indicate the costs involved and the corresponding adjustments in Contract Price and Completion Time, if necessary. If the Work is increased by such changes, a proportionate additional Performance Bond is required. Whether the changes are for the deletion, addition or alteration of work, the aggregate value of the such changes should not exceed twenty-five percent (25%) of the original Contract Price of the particular pay item and shall be determined by the Owner using any or more of the following ways:

- a) By lump sum acceptable to the Contractor;
- b) By unit prices either stipulated in the Contract or subsequently agreed upon, provided the aggregate value of changes does not exceed 25% of the original Contract Price of the particular pay item;
- c) By actual direct cost plus value added tax, if any, plus fifteen percent (15%) for Contractor's profit and overhead. In this case, the Contractor shall keep and present, in such form as the Owner may direct, a correct account of the direct cost together with vouchers and other supporting documents.

Overruns exceeding 25% shall be covered by a Supplemental Contract in which the Contractor shall not be obliged to execute the changes using the unit rate specified in its Bid, a Supplemental Contract being treated as one separate from and independent of the Contract. If the Contractor executes the changes without demanding the execution of a Supplemental Contract, the value of the changes shall be determined based on item (b) above.

For deductive change order initiated by the Owner for the purpose of transferring certain work items or part of the scope of work to another Contractor or for the Owner to supply certain construction materials, the Contractor shall be entitled to fifteen percent (15%) of the amount deducted in the change order to recover overhead expenses and profit.

Adjustment of prices due to escalation or reduction of costs of executing the work and peace and order problem, is covered by Article 20.16 and its sub-articles. The adjustment of prices shall be determined using a parametric formula agreed upon by the Owner and the Contractor. If the project is delayed by more than 15% and such delay is not excused, the rate to be used for the work affected by such delay should be the rate applicable during the period it should have been accomplished.

On the quality of the Work:

Article 20.04 provides the procedure for the inspection of the Work, stipulating the responsibility of the Owner to inspect and examine ongoing works including works which were covered up or already completed but were purportedly done not in accordance with the Drawings and Specifications, and assigning to the Contractor all the costs of examination and of satisfactory reconstruction of works found to be defective. A Supplemental Agreement is required for special test or inspection instructed by the Owner to be performed



after the date of substantial completion [*Article 20.14, Special Test and Inspection*].

If the Owner accepts defective or non-conforming works, instead of requiring its removal and replacement, such shall be covered by a Change Order as provided for in Article 20.15 [*Acceptance of Non-Conforming Work*] reflecting the corresponding reduction in the Contract Price by an amount not exceeding the value of unfinished work as determined in the Breakdown of Work and Corresponding Value.

If the works were found to be done in accordance with the Drawings and Specifications, the Contractor shall be entitled to the actual cost of labor and materials involved in the examination plus fifteen percent (15%) and shall be granted a suitable extension of time if completion of the work has been delayed on account of such examination and the additional work involved.

#### **Article 20.10 Use of Completed Portions of Work**

This article provides the conditions for the Owner in taking possession of and use of completed or partially completed portion of the Work prior to overall completion. Such partial possession is deemed practical completion of that portion of the Work, covered by Articles 20.11 [*Substantial Completion and its Effect*], 20.12 [*Period of Making Good of Known Defects or Faults*], 20.13 [*Making Good of Known Defects or Faults*], 20.14 [*Special Test and Inspection*] and 20.15 [*Acceptance of Non-Conforming Work*]. The Owner shall issue a Certificate of Completion for that portion of the Work taken possession of. The Owner is required to release to the Contractor the retention for that portion of the Work and the defects liability period begins to run on that portion. Such, however, shall not be deemed an acceptance of the remaining works, neither shall it be deemed a waiver by the Owner of its right to claim damages for delay in the completion of the Work.

The Contractor is entitled to extra cost or extension of time or both if such partial possession of the Work increases the cost or delays the completion of the uncompleted works.

#### **Article 20.11 Substantial Completion and Its Effect**

Under this article the Contractor is paid for Work completed although the Owner retains a portion of the Contract price, if the Performance Bond and the retention are not sufficient to complete the Work without additional cost to the Owner.



Unless the Contract provides otherwise, there is substantial completion when the Contractor completes 95% of the Work, provided that the remaining work and the performance of the work necessary to complete the Work shall not prevent the normal use of the completed portion. The Supreme Court has applied the 95% threshold in determining what constitutes substantial completion in the absence of an agreement to the contrary.

Substantial completion is a milestone in construction which sets the limit for the imposition of liquidated damages and triggers other events or obligations as provided for in this document, viz:

- Inspection and Tests on completed works [*Article 20.04*];
- Punchlist shall be issued within 30 days from date of substantial completion [*Article 20.11(C)*];
- Retention shall be released within 60 days from date of substantial completion upon posting of Contractor's Guarantee Bond [*Article 20.11(C)*];
- Works ordered by the Owner to be performed after the date of substantial completion shall be covered by a supplemental agreement [*Article 20.14*].

The Owner shall be deemed to have recognized substantial completion of the Work through:

- the approval of the Contractor's billing for completing at least 95% of the Work; or
- the issuance of a Certificate of Substantial Completion or equivalent document; the date of said document, however, shall not be controlling if substantial completion is shown to have been made at an earlier date, unless the Contractor accepts the certificate without taking exceptions thereto in writing within fifteen (15) days from receipt, conditioned upon successful test-run of the Facility. Delay in the test run through no fault of the Contractor shall automatically extend the Completion Time for a period equal to the period of delay.

Once the Contractor achieves 95% project completion, it is excused from the payment of further liquidated damages. The Contractor must prove by substantial evidence that it actually achieved 95% completion of the project. The rules<sup>[2]</sup> are intended to balance the allocation and burden of costs between the Contractor and the project Owner so that the Contractor still achieves a return for its completed work, and the project Owner will not incur further costs.

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<sup>[2]</sup> *Article 20 [Work]*

**Article 21 Time of Completion of Work**

The purpose of this article is to ensure that the Contract is completed within the original or extended Completion Time due to changes both directed and constructive.

The Time of Completion of the Work starts and ends on the date stipulated in the Contract, in the absence of which, from the date the Contractor commences the Work and ends on the stipulated date of completion of the Work, or by a specific date.

When the time for completion of the Work is contingent upon the date when the Contractor actually commences the Work, the commencement date is normally indicated in the Notice to Proceed (NTP) issued by the Owner as within seven (7) days or more days from receipt of the NTP or on the fixed date indicated in the NTP. The commencement date is significant in reckoning the Completion Time or in computing liquidated damages in case there is delay in the execution or completion of the Work. Likewise, there are obligations of the Owner and the Contractor which are to be performed reckoned from the commencement date of the Contract, such as Article 32.01 [Advance Payment] and Section II [Laws, Regulations, Site Conditions, Permits and Taxes]. If the Contract does not provide for the issuance of a Notice to Proceed, the Contractor should get consent from the Owner for it to commence the Work on a date it so specified.

Article 21.03 [Schedule of Construction Work] providing for acceleration of work in case of slippage provides that, if the delay is due to the fault of the Contractor, the additional cost for the acceleration of work shall be borne by the Contractor, but if the acceleration of work is for the benefit or convenience of the Owner or due to its fault or delay, then, it shall be the Owner who shall be responsible for the cost thereof. The acceleration work should be covered by a Change Order as extra work.

**Article 21.04 Extension of Time**

This article enumerates the causes or events that obstruct or delay the execution or completion of the Work and which may or may not allow an adjustment of Contract Completion Time.

For delay caused by events not due to the fault or neglect of the Contractor, the Owner shall determine the reasonable adjustment of Completion Time corresponding to such delay within fifteen (15) days from receipt of the Contractor's request. If the delay is authorized by

the Owner or caused by the act, neglect, delay or fault of the Owner, the adjustment is based on the period of delay caused by such event/factor, and the Contractor may be entitled to additional costs (See Article 20.08 [*Claims for Extra Cost*]). This provision should be interpreted in conjunction with Articles 26 [*Termination and Suspension*] and 29.06 [*Liquidated Damages*].

In *DPWH v. FSI*<sup>[3]</sup>, the Supreme Court affirmed the finding of CIAC that the delay of FSI was caused by DPWH for which it was awarded extended rental costs of various equipment and standby rental cost and overhead costs during the period those equipment went idle. In addition, it was relieved of the liability for liquidated damages, as the delay was caused by DPWH which failed to the right-of-way and to turn-over to FSI possession of the site free of obstructions.

## **Article 22      Payments**

This article provides the conditions relative to payments, including the release of retention.

The Breakdown of Work and Corresponding Value submitted by the Contractor upon commencement of the Work and as approved by the Owner, shall be the basis for all the Requests for Payment and for determining the value of uncompleted work or corrective works. The Request for Payment shall be computed from the work completed on all items listed in the Breakdown of Work and Corresponding Value, less a retention of 10% of the progress payment to the Contractor. The Owner is authorized to deduct from any payment due the Contractor the cost of defective works not remedied, the amount of unpaid claims by Sub-contractors and suppliers of materials and labor, and the amount which has accrued as liquidated damages. The Owner shall evaluate, certify, and pay the amount of the Contractor's accomplishment within thirty (30) days after receipt of the Contractor's Request for Payment. Owner's delay in the payment of the amount due shall entitle the Contractor to payment of interest at a rate prevailing on due date and who may exercise its right as provided for under Article 26(b).

The conditions for the release of Final Payment to the Contractor is provided in this article. This release renders the Owner free from any unpaid labor and unpaid claims of Sub-Contractors and suppliers, including payment of all taxes and obligations due in connection with the Contract. The Owner may require the Contractor to submit a sworn statement with proof of full payment to Sub-Contractors,

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<sup>[3]</sup> *Department of Public Works and Highways vs. Foundation Specialists, Inc.*, G.R. No. 191591, June 17, 2015

suppliers, and appropriate government agencies. If there are still unpaid claims, the Contractor may be required to furnish the Owner an indemnity bond as provided for in Articles 31.04 [*Contractor's Performance and Payment Bonds*] and 33.01 [*Liens*]. The Contractor's acceptance of Final Payment shall constitute a waiver of all its claims against the Owner, subject to the exceptions in Article 22.09 [*Acceptance and Final Payment*].

### **Article 22.11 Release of Retention**

The 10 percent retention is a portion of the contract price which the Owner deducts from the contractor's billings, as security for the execution of corrective work or completion of work – if any – becomes necessary. This amount is to be released one year after the completion of the project, minus the cost of corrective and/or completion work undertaken.<sup>[4]</sup>

The Owner's obligation to release the retention money arises after the conditions for its release have been complied with.<sup>[5]</sup>

## **Section VII Contractor-Separate Contractor-Subcontractors Relationship**

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This section provides the conditions for the Owner to engage a Separate Contractor to do works outside of the Contractor's scope of work, and the conditions for the Contractor's engagement of a Sub-Contractor, and the relationship amongst them.

These provisions are important to make clear to the parties their respective obligations in respect of the Work commissioned to them by the Owner, as well as their respective accountabilities in case of nonfulfillment. Such provisions should also be covered in the Owner's contract with a Separate Contractor and in the Contractor's contract with its Sub-Contractor.

In this section, the Owner is responsible for the coordination of the work of the Separate Contractor with the work of the Contractor. The Contractor is not liable for any damage caused by the Separate Contractor. On the other hand, the Contractor shall be responsible for the acts and omissions of its Sub-Contractor. The Owner may or may not allow subcontracting. The Owner's consent, however, shall

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<sup>[4]</sup> *H.L. Carlos Construction, Inc. v. Marina Properties Corporation, Jesus K. Typoco, Sr. and Tan Yu*, G.R. No. 147614, January 29, 2004; *Empire East Land Holdings, Inc. v. Capitol Industrial Construction Groups, Inc.*, G.R. No. 168074, September 26, 2008

<sup>[5]</sup> *Empire East Land Holdings Inc. v. Capitol Industrial Construction Groups, Inc.*, G.R. No. 168074, September 26, 2008

not create any contractual relation between the Sub-Contractor and the Owner. Article 33.03 [*Subcontracting*] provides the conditions for subcontracting of works.

## **Section VIII Suspension of Work and Termination of Contract**

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### **Article 26 Contractor's Right to Suspend Work or Terminate Contract**

The Contractor may suspend the Work or terminate the Contract.

The Contractor is required to give fifteen (15)-days written notice to the Owner of its decision to suspend or terminate the Contract for any of the grounds specified in this article. For suspension of work, the Contractor shall be entitled to an equitable adjustment of Completion Time and/or Contract Price under any of the circumstances herein provided.

### **Article 27 Owner's Right to Suspend the Work**

This provision allows the Owner to suspend the Work with or without cause.

A written notice to the Contractor is required.

For suspension without cause, the notice of suspension shall indicate the date the work shall be resumed. The period of suspension shall be not more than the aggregate period of fifteen (15) days, unless the Contractor agrees to an additional period.

For suspension with cause, the Owner shall issue written order to the Contractor to stop the work or any portion thereof until the cause thereof has been eliminated.

Suspension of work due to the act, neglect, delay or fault of the Owner or any other Contractor employed by the Owner or those beyond the control or fault of the Contractor, shall entitle the Contractor to an adjustment of Completion Time and Contract Price. These causes are described in Article 27.02 as follows:

- unsuitable weather or other conditions considered unfavorable for the prosecution of the work;
- necessity for adjusting the Drawings to suit site conditions found during construction, or in case of a change in Drawings and Specifications;
- failure of the Owner to supply Owner-supplied/furnished materials on time, where such failure is due to causes beyond the reasonable control of the Owner;

- delay by the Owner in obtaining a right-of-way, where such obligation is assumed by the Owner under the Contract, and the delay is not due to the fault or negligence by the Owner;
- force majeure or fortuitous event;
- peace and order problems; or
- any condition similar to the above beyond the control of the Owner.

For unsuitable weather conditions, the Contractor shall be entitled to an adjustment of Completion Time and Contract Price only for the period in excess of that taken into account in the Bid Documents.

## **Article 28 Owner's Right to Terminate Contract**

The Owner has the right to terminate the Contract with or without cause. This provision should be read together with Articles 29.02, 29.03, 29.04, 29.05, and 29.06.

The Owner may terminate the Contract for cause even without prior notice to the Contractor by reason of the economic status of the Contractor as described in Article 28.01.

The Owner may for cause also terminate the Contract upon fifteen (15)-day written notice to the Contractor and to its Surety upon occurrence of any event caused by the Contractor's act, delay, fault or neglect. The Owner has the right to exclude the Contractor from the site and take possession of the Work and all of the Contractor's tools, appliances, equipment, machinery, and materials left at the site. The Owner may take over and finish the Work and withhold any payment due the Contractor until the Work is finished.

The Owner may terminate the Contract without cause upon fifteen (15)-day written notice to the Contractor. This is known as *termination for the convenience of the Owner*. In such case, the Contractor shall be paid for all work accomplished and any expense sustained as a consequence of the termination plus reasonable termination costs.

In *G.R. No. 96643*<sup>[6]</sup>, the Supreme Court defined the right of rescission of contracts as provided for in Articles 1381 and 1191 of the Civil Code. Article 1381 enumerates what are "rescissible contracts". Under Article 1385, it is provided that *he who demands rescission should return whatever he may be obliged to restore*. Evidently, this provision does not include construction contracts.

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<sup>[6]</sup> *Deiparine vs. CA and Trinidad, G.R. No. 96643, April 23, 1993*

Construction contract falls squarely under the coverage of Article 1191<sup>[7]</sup> providing for the right of rescission under the law on obligations. The Supreme Court said:

*Article 1191, unlike Article 1385, is not predicated on economic prejudice to one of the parties but on breach of faith by one of them that violates the reciprocity between them. Article 1725<sup>[8]</sup>, on the other hand, contemplates a voluntary withdrawal by the owner without fault on the part of the contractor, who is therefore entitled to indemnity, and even damages, for the work he has already commenced.*

In *Angel V. Talampas, Jr. v. Moldex Realty, Inc.*, G.R. No. 170134<sup>[9]</sup>, the Supreme Court pegged the cost of opportunity lost due to the Owner's unilateral termination of the Contract at 20% of the value of unfinished work. It was ruled that the "cost of opportunity lost must represent only the profits that the Contractor failed to obtain due to the contract's early termination".

## **Article 29      Owner's Right to Proceed with the Work after Reduction in Contractor's Scope of Work; Partial Takeover from Contractor**

The Owner has the right to carry out the work, without terminating the Contract, by reason of Contractor's failure to perform its obligations under any of the circumstance described in Article 29.01. Written notice shall be given to the Contractor and the Owner is required to issue a Change Order covering that portion of the Work taken over as deductive works.

Such taking over of the Work shall not prevent the Owner from recovering damages against the Contractor and its sureties, which shall include liquidated damages and additional costs incurred in completing the Work. The Owner is required to assess the value of the work completed by the Contractor and the value of all usable materials taken over, which shall be deducted from any amount found to be due as damages from the Contractor.

<sup>[7]</sup> Art. 1191. *The power to rescind obligations is implied in reciprocal ones, in case one of the obligors should not comply with what is incumbent upon him.*

*The injured party may choose between the fulfillment and the rescission of the obligation, with the payment of damages in either case. He may also seek rescission, even after he has chosen fulfillment, if the latter should become impossible.*

*The court shall decree the rescission claimed, unless there be just cause authorizing the fixing of a period.*

*This is understood to be without prejudice to the rights of third persons who have acquired the thing, in accordance with Articles 1385 and 1388 and the Mortgage Law.*

<sup>[8]</sup> Art. 1725. *The owner may withdraw at will from the construction of the work, although it may have been commenced, indemnifying the contractor for all the latter's expenses, work, and the usefulness which the owner may obtain therefrom, and damages.*

<sup>[9]</sup> *Angel V. Talampas, Jr. v. Moldex Realty, Inc.*, G.R. No. 170134, June 17, 2015



## Article 29.06 Liquidated Damages

The Contractor is liable to pay the Owner liquidated damages by reason of delay in the completion of the Work within the Contract Completion Time, including the time adjustment duly granted.

The Supreme Court defined liquidated damages as: “the amount that the parties agree to be paid in case of a breach, which shall answer for damages suffered by the owner due to delays in the completion of the project.”<sup>[10]</sup> “As long as the contractor fails to finish the works within the period agreed upon without justifiable reason and after the owner makes a demand, then liability for damages as a consequence of such default arises.”<sup>[11]</sup> They are in the nature of penalties. A penal clause is an accessory undertaking to assume greater liability in case of a breach. It is attached to the obligation in order to ensure performance.”<sup>[12]</sup>

Liquidated damages accrues from the first day of delay in completing the project until the date of substantial completion, but in no case shall the total sum exceed ten percent (10%) of the total contract price. The amount of liquidated damages for delay shall be reduced in proportion to the value of the portions of the Work which have been certified as complete or occupied or used by the Owner prior to the overall completion of the Work. Such amount of liquidated damages shall be deducted from any money due or which may become due the Contractor or from the retention money or other securities posted by the Contractor, whichever is convenient to the Owner.

## Section IX Responsibilities and Liabilities of the Contractor and the Owner

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This section embodies the purpose of Republic Act No. 11058 (*An Act Strengthening Compliance with Occupational Safety and Health Standards and Providing Penalties for Violations Thereof*) on ensuring the safety and health in the work environment and in preventing loss or damage to lives and properties during construction. It delineates the responsibilities and liabilities of the Contractor and the Owner by requiring both of them to secure and maintain (a) insurance coverage as will protect them from claims for injury or death or damage to property which may arise from the implementation of the Contract, and (b) the bonds that will guarantee faithful performance of the

<sup>[10]</sup> *H.L. Carlos Construction, Inc. v. Marina Properties Corporation*, 466 Phil. 182, 199-200 (2004)

<sup>[11]</sup> *Atlantic Erectors, Inc. vs. Herbal Cove Realty Corporation*, G.R. No. 170732, October 11, 2012

<sup>[12]</sup> *H.L. Carlos Construction, Inc. v. Marina Properties Corporation*, 466 Phil. 182, 199-200 (2004)

Work. The mandatory conditions for the bonds provided in Article 31.07 shall form part of the bonds and as such, shall be deemed accepted by the surety issuing the bonds.

**Article 32.01** requires Owner to give the Contractor an Advance Payment (also referred to as down payment), to help with the start-up of construction, such as mobilization and procurement of materials, conditioned upon the Contractor's posting of an Advance Payment Bond or surety bond to guarantee its repayment. The amount of advance payment is a percentage of the contract price agreed upon by the parties which shall be recouped pro rata from payment of approved progress billings.

**Article 32.04** allows the Contractor to request the Owner to furnish the Contractor reasonable evidence that it is ready and able to fulfill its obligations under the Contract, and unless such reasonable evidence is provided, the Contractor may not be required to execute the Contract or to commence or continue the Work.

### **Article 33.01 Liens**

The purpose of this article is to ensure that the Work is free of any legal liens prior to the release of the Final Payment to the Contractor. The Owner may require the Contractor to execute sworn statement and submit proof of payment of claims of sub-contractor and suppliers and settlement of its obligations with government agencies in regard to taxes due in connection with the Contract, the employees' contributions, and withholding tax on the employees' wages, as provided for in Article 22.09 [*Acceptance and Final Payment*].

### **Article 33.02 Assignment**

This article provides, without exception, that the Contractor is not allowed to assign to another party any part or the whole of the Contract. If the Owner discovers that such assignment was made without its consent, the Owner may remove from the Contractor's scope of work that part which was assigned and give it to another contractor or terminate the Contract.

### **Article 33.03 Subcontracting**

Subcontracting is allowed subject to the prior consent of the Owner. As conditions for its approval, the Owner may require the Contractor to submit copy of the subcontract and that the subcontract should require the same bonds and insurances required of the Contractor and furnish the Owner copies thereof. The Owner's consent to the

engagement of a Sub-Contractor, however, shall not, by itself, create any contractual relation between the Sub-Contractor and the Owner, as stipulated in Section VII [*Contractor-Separate Contractor-Subcontractors Relationship*].

#### **Article 33.04 Disputes**

This provision requires the Owner and the Contractor to settle their disputes amicably. Any dispute not so settled shall be submitted for arbitration by the Construction Industry Arbitration Commission (CIAC) which, under Executive Order No. 1008, has an original and exclusive jurisdiction to settle construction disputes (See Article 33.05 [*Settlement of Disputes*]).

### **Section X Owner's Representative**

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The Owner's representative is a person appointed by the Owner to act for and on its behalf in all matters affecting the Contract and to ensure that the Contract is properly implemented. The Owner's representative may be the Architect, Engineer or Construction/Project Manager. In this section, the Owner's representative has full and unqualified authority, unless the Owner issued a written notice to the Contractor stating the limits of such authority granted.

In complex or large scale projects where the Owner hires an Architect or an Engineer or a Construction or Project Manager, a distinction and delineation of their duties and responsibilities shall be provided in the Contract to ensure that any or all of the issues that may arise from the implementation of the Contract will be properly addressed and resolved without delay.

In *G.R. Nos. 176439 and 176718*<sup>[13]</sup>, the Architect was authorized under the Contract to act on the Contractor's request for time extension and to determine the period of extension he deems reasonable. The Supreme Court, in view of the conflicting findings of the Construction Industry Arbitration Commission (CIAC) and the Court of Appeals on the extent of Contractor's delay in the project, adopted the computation of the Architect, citing the practice in the construction industry in this regard, and the provision in the Contract

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<sup>[13]</sup> *The Church of Jesus Christ of Latter Day Saints v. BTL Construction Corporation, G.R. No. 176439, and BTL Construction Corporation v. The Manila Mission of the Church of Jesus Christ of Latter Day Saints and BPI-MS Insurance Corporation, G.R. No. 176718, January 15, 2014*

specifically providing the Architect the authority to act/grant requests for time extension.

## **Section XI Schedule of Time Limits**

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This section summarizes the prescribed time limits for the execution of the Contract conditions as provided in this document.

## **CASE SYNOPSES**

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### **LIQUIDATED DAMAGES**

**Empire East Land Holdings Inc. v. Capitol Industrial Construction Groups, Inc., G.R. No. 168074, September 26, 2008**

As justification for its claim for liquidated damages against the Contractor, the Owner alleged that the Contractor was in default in the performance of its obligations at the start and for the entire duration of the construction due to insufficient manpower and lack of technical know-how. On the other hand, the Contractor argued that the delay in the completion of the project was attributed to the Owner's fault, viz., (a) delayed issuance of building permit; (b) additional works ordered by the Owner; (c) delayed payment of progress billings; (d) delayed delivery of owner-supplied construction materials; and (e) limitation of monthly accomplishment. Both the CIAC and the CA found these to be the causes of the Contractor's failure to complete the project on time.

The Supreme Court held:

*Liquidated damages are those that the parties agree to be paid in case of a breach. As worded, the amount agreed upon answers for damages suffered by the owner due to delays in the completion of the project. Under Philippine laws, they are in the nature of penalties. They are attached to the obligation in order to ensure performance. As a pre-condition to such award, however, there must be proof of the fact of delay in the performance of the obligation.*

As the Contractor is not guilty of breach of its obligation under the Contract, it cannot be held liable for liquidated damages.

**Atlantic Erectors, Inc. v. Herbal Cove Realty Corporation, SC G.R. No. 170732, October 11, 2012, 684 SCRA 55**

At issue here is whether by the Owner's termination of the Contract the Contractor was prevented it from completing the project, thereby releasing it from liability for liquidated damages.

It is not disputed that the Contractor reneged on its obligation to complete the project on schedule despite the extensions granted by the Owner. The Contractor did not seek additional time after the expiration of the extended period despite its claim of the existence of circumstances that entitle it to an extension of time, which it, however, failed to document. Although there was a commitment from the Contractor to complete the project, its proposed date of completion was way beyond the extended completion date agreed upon. The Contractor argued further that the Owner's termination of the contract prevented it from fulfilling its commitment to complete the project.

The Supreme Court held:

*Respondent's (Herbal Cove's) entitlement to liquidated damages is distinct from its right to terminate the contract. Petitioner's (Atlantic Erector's) liability for liquidated damages is not inconsistent with respondent's takeover of the project. What is decisive of such entitlement is the fact of delay in the completion of the works. Stated in simple terms, as long as the contractor fails to finish the works within the period agreed upon by the parties without justifiable reason and after the owner makes a demand, then liability for damages as a consequence of such default arises.*

The Supreme Court further noted that while the contractor cited grounds which fairly entitled it to additional time to complete the works, it never sent to the owner a request for extension of time to finish the work. Assuming these reasons to be valid, still the contractor is not excused from making this request, and should bear the consequences for the delay for it deprived the owner of the right to determine the length of extension to be given to it and, consequently adjust the period to finish the work.

The rights to liquidated damages and to terminate the contract are distinct remedies available to the Owner under the Contract. What is decisive of the Owner's entitlement to liquidated damages is the fact of delay in the completion of the works. The Contractor's accomplishment as of the last billing was only 62.57%. Thus, liquidated damages in the maximum amount of 10% of the Contract price was awarded to the Owner against the Contractor.

## **EFFECTS OF SUBSTANTIAL COMPLETION ON THE CLAIM FOR LIQUIDATED DAMAGES**

**Werr Corporation International v. Highlands Prime, Inc., G.R. No. 187543, February 8, 2017; Highlands Prime, Inc. v. Werr Corporation International, G.R. No. 187580, February 8, 2017, 805 Phil. 415**

Issues: Whether delay should be computed until actual termination of the contract or until substantial completion of the project.

The project was not completed on the initial completion date, hence, several extensions were granted, but still, the project was not completed on the final extension granted. The Contractor's accomplishment after the expiration of the extended completion time was only at 93.18%, thus, the Owner terminated the Contract.

The Supreme Court held:

*The contracting parties are free to stipulate as to the terms and conditions of the contract for as long as they are not contrary to law, morals, good customs, public order or public policy. Corollary to this rule is that laws are deemed written in every contract. Deemed incorporated into every contract are the general provisions on obligations and interpretation of contracts found in the Civil Code.*

While the Contract provides for liquidated damages of 1/10 of 1% of the contract price for every day of delay, it does not, however, provide for the period until when such liquidated damages shall run. In this instant case, the Supreme Court said that such omission may be supplemented by the provisions of the Civil Code (Arts. 1234 and 1376), the industry practice, and the CIAP Document 102 which have supplementary effect on private construction contracts, provided that the Contractor successfully proved by substantial evidence that it actually achieved 95% completion. The Contractor, however, failed to present evidence to show what it had accomplished from the time of the last billing up to the time the contract was terminated, and also failed to prove that it is a practice in the construction industry to project the date of substantial completion of a project and to compute the period of delay based on the rate in past progress billings.

*The rules are intended to balance the allocation and burden of costs between the contractor and the project owner, so that the contractor still achieves a return for its completed work and the project owner will not incur further costs. To compute the period of delay when substantial compliance is not yet achieved but merely on the assumption that it will eventually be achieved would result in an iniquitous situation where the project owner will bear the risks and additional costs for the period excused from liquidated damages.*

Thus, the Contractor cannot be excused from the payment of liquidated damages for it failed to meet the condition precedent, that is, that it actually achieved 95% completion rate.

**Filinvest Land, Inc. v. The Honorable Court of Appeals, Philippine American General Insurance Company and Pacific Equipment Corporation, G.R. No. 138980, September 20, 2005, 470 SCRA 57**

Issues: Whether or not the liquidated damages agreed upon by the parties should be reduced considering that: (a) time is of the essence of the contract; (b) the



liquidated damages was fixed by the parties to serve not only as penalty in case the Contractor fails to fulfill its obligation on time, but also as indemnity for actual and anticipated damages which the Owner may suffer by reason of such failure; and (c) the total liquidated damages equivalent to 32% of the total contract price was freely and voluntarily agreed upon by the parties.

The Contractor admitted that it failed to complete the contracted work despite the three extensions granted by the Owner because of inclement weather and Owner's alleged refusal to accept and pay its accomplished work and change order. The Owner took over the project and held the Contractor liable for damages which it had incurred and will incur to finish the project in the amount of ₱15,000 per day of delay as stipulated in the Contract. According to the Owner, such provision in the Contract is intended to recover from the Contractor actual anticipated and liquidated damages, and it is not just merely for penalizing breach of the contract. It argued that had the project been completed on time, it could have sold the lots sooner and earned its projected income that would have been used for its other projects.

The Supreme Court held:

*A penal clause is an accessory undertaking to assume greater liability in case of breach. It is attached to an obligation in order to insure performance and has a double function: (1) to provide for liquidated damages, and (2) to strengthen the coercive force of the obligation by the threat of greater responsibility in the event of breach.*

Article 1226 of the Civil Code provides:

*In obligations with a penal clause, the penalty shall substitute the indemnity for damages and the payment of interests in case of noncompliance, if there is no stipulation to the contrary. Nevertheless, damages shall be paid if the obligor refuses to pay the penalty or is guilty of fraud in the fulfillment of the obligation.*

The penalty may be enforced only when it is demandable in accordance with the provisions of this Code.

The Supreme Court said:

*A distinction between a penalty clause imposed essentially as penalty in case of breach and a penalty clause imposed as indemnity for damages should be made in cases where there has been neither partial nor irregular compliance with the terms of the contract. In cases where there has been partial or irregular compliance, as in this case, there will be no substantial difference between a penalty and liquidated damages insofar as legal results are concerned. Thus, there is no justification for the Civil Code to make an apparent distinction between a penalty and liquidated damages because the settled rule is that there is no difference between penalty and liquidated damages insofar as legal results are concerned and that either*



*may be recovered without the necessity of proving actual damages and both may be reduced when proper.*

*As a general rule, courts are not at liberty to ignore the freedom of the parties to agree on such terms and conditions as they see fit as long as they are not contrary to law, morals, good customs, public order or public policy. Nevertheless, courts may equitably reduce a stipulated penalty in the contract in two instances: (1) if the principal obligation has been partly or irregularly complied; and (2) even if there has been no compliance if the penalty is iniquitous or unconscionable [Article 1229, Civil Code].*

*The question of whether a penalty is reasonable or iniquitous can be partly subjective and partly objective as its resolution would depend on such factors as, but not necessarily confined to, the type, extent and purpose of the penalty, the nature of the obligation, the mode of breach and its consequences, the supervening realities, the standing and relationship of the parties, and the like, the application of which, by and large, is addressed to the sound discretion of the court.*

The penalty charge of ₱15,000/day which totals to an amount equivalent to 32% of the contract price was unconscionable as the construction was already not far from completion at 94.53% accomplishment rate. There was no evidence presented to prove that the delay was due to the negligence of, or that there was bad faith on the part of, the Contractor. It was held that the 94.53% completion at the time of termination of the contract is a substantial compliance in good faith which renders unconscionable the application of the full amount of liquidated damages as penalty for delay. Likewise, the Owner's right to indemnity was cancelled as it failed to do what was incumbent upon it when it failed to pay the Contractor for work accomplished. The Owner's claim for liquidated damages was dismissed.

**Urban Consolidated Constructors Philippines v. The Insular Life Assurance Co., Inc., G.R. No. 180824, August 28, 2009**

The construction was beset by several delays. As such, the parties entered into a second contract increasing the contract price and extending the deadline for completion of the project. The Owner, likewise, agreed to extend financial assistance to the Contractor by paying directly the suppliers of construction materials. Despite such, however, the Contractor still failed to meet the target completion date. Hence, the Owner took over the project.

The Contractor alleged that the delay was due to the Owner's delay in the approval and payment of monthly billings; delivery of materials; and execution of a formal written construction agreement. The project was already 97% complete when the Owner took over, which at that time, the Contractor was already delayed by 294 days.

The Supreme Court held:

There was no bad faith on the part of the Contractor as it had in fact completed 97% of the project. The delay in the delivery of materials cannot be attributed to the Owner as the payment of materials directly by the Owner is only an accommodation to ensure the timely completion of the project, but the obligation to procure and have the materials delivered on time remains with the Contractor. It was held that the total amount of ₱11,432,190.00 as liquidated damages (1/10 of 1% of the contract price or ₱38,885.00 per day for 294 days of delay) is unconscionable.

*As a general rule, courts are not at liberty to ignore the freedom of the parties to agree on such terms and conditions as they see fit as long as they are not contrary to law, morals, and good custom, public policy or public order. Nevertheless, (t)he judge shall equitably reduce the penalty when the principal obligation has been partly or irregularly complied with by the debtor. Even if there has been no performance, the penalty may also be reduced by the courts if it is iniquitous or unconscionable. [Art. 1229, Civil Code]*

The amount of liquidated damages was reduced from ₱38,885.00 to ₱10,000.00 per day of delay for a total of ₱2,940,000.00, and was further reduced to ₱1,940,000.00 due to the Owner's failure to release the retention money and the payment for change orders which could have been used by the Contractor to purchase construction materials and expedite the completion of the project.

**Transcept Construction and Management Professionals, Inc. v. Teresa C. Aguilar, G.R. No. 177556, December 8, 2010, 637 SCRA 574**

The Contractor failed to complete the works on time. The Owner hired an accredited testing laboratory to assess the Contractor's quality of work and accomplishment rate, and it was discovered that there were substandard works and that substandard materials were used in the project. The parties then agreed to execute a second contract to cover the necessary corrective works and to extend the deadline for completion of the project. Despite such, however, the Contractor still failed to finish the project within the extended time indicated in the second contract. At that time, the Contractor's accomplishment was determined at 98.16%.

The Supreme Court held:

The Owner is not entitled to liquidated damages since the Contractor already accomplished more than 95% required under CIAP Document 102 [Art. 20.11(A)(a)] which is considered substantial completion of the project, and instead, awarded the cost of the remaining works in accordance with Article 1234 of the Civil Code – *“If the obligation had been substantially performed in good faith, the obligor may recover as though there had been a strict and complete fulfillment, less damages suffered by the obligee”*.

## PROLONGATION COSTS

**Department of Public Works and Highways vs. Foundation Specialists, Inc., G.R. No. 191591, June 17, 2015**

The Contractor demanded from the Owner the payment of extended rental costs of various equipment, standby rental cost, and overhead costs which it incurred during the period of delay caused by the Owner's failure to remove all obstructions and secure road right-of-way along the stretch of construction.

The Supreme Court held:

The Owner's denial of the Contractor's claims for extended rental and overhead costs was not justified absent any document to prove that such claims are prohibited. The Owner failed to present the modified Contract provision which allegedly contain such prohibition. Moreover, such modified Contract provision was not even mentioned in the Owner's letters to the Contractor granting the latter's requests for time extension. Thus, it was concluded that no such modified version existed, and that the Owner had no basis to deny Contractor's claims for extended rental and overhead costs, which the CIAC and the Court of Appeals have exhaustively deliberated upon. Hence, the award to the Contractor of the costs of standby rental cost and overhead costs were affirmed, but the award of the extended rental costs of various equipment was ordered to be recomputed by the CIAC to cover only the period such various equipment were idle due to the Owner's delay.

## PRICE ESCALATION

**Hanjin Heavy Industries and Construction Co., Ltd. v. Dynamic Planners and Construction Corp., G.R. Nos. 149408 & 170144, April 30, 2008**

Among the issues resolved in this case is the legality of the award of price escalation in favor of the Sub-Contractor.

The Sub-Contractor accomplished only 84% of the subcontracted works on the scheduled project completion date. The Contractor advised the Sub-Contractor that no payment shall be forthcoming after that date. When the project was at 94% completion, the Sub-Contractor allegedly abandoned the project, hence, the Contractor took over. The Sub-Contractor argued that it did not abandon the project as it was already nearing completion, but it admitted that it suspended the work on account of the Contractor's act of withholding the release of the down payment and non-payment of its progress billings, which caused delay in the project and rendered its timely completion impossible. The Sub-Contractor then demanded for payment of its claims against the Contractor, which include its claim for price escalation.

The Contractor admitted that the Sub-Contractor is entitled to escalation cost for the local portion of the project, but it argued that it should be computed using the 52

formulas and price indexes from the National Statistics Office and the National Statistical Coordination Board, or at 35% of the price index only.

The Supreme Court held:

The Contractor failed to present any of the supposed 52 formulas and price indexes which it claimed would give a more precise price escalation amount, and it also failed to support its assertion that it should only be at 35% of the price index. The Subcontract Agreement provides that the Sub-Contractor is entitled to both price adjustment and price escalation. Thus, the award of the Court of Appeals which was pegged on the local portion of the contract price which is 65% of the Sub-Contractor's billings and accomplishments prior to the Contractor's takeover, multiplied by 100% price index was affirmed.

## **LABOR AND MATERIAL COST ESCALATION**

**H.L. Carlos Construction, Inc. vs. Marina Properties Corporation, G.R. No. 147614, January 29, 2004**

The parties executed an Amended Contract extending the contract period plus a grace period of 30 days. The Contractor failed to complete the works within the stipulated completion period and abandoned the project. The Owner, thus, contracted out the remaining works to another entity and demanded from the Contractor the damages it incurred. The Contractor, on the other hand, claimed for payment of its unpaid billings, change orders and extra work, labor and material price escalation, release of retention, and the value of materials left at site. On the Contractor's claim for cost escalation, the Owner averred that the Contractor is not entitled to any price increase since it was delayed in the completion of the project, and entitling it to such claim would be to reward it for its breach of contractual obligation.

The Supreme Court held:

The Contract prohibited claims for cost escalation except on the labor component of the work.

The Contractor failed to present evidence, such as an official economic data, that would show the increases in material costs during the period covered in its claim. Further, its unpaid billings for change orders and extra work were not subject to increases since they were not included in the agreed contract price and the materials for these additional works are to be purchased only when the work was contracted or agreed upon. Thus, the Contractor is not entitled to material cost escalation.

The labor cost escalation clause in the Contract shall cover government mandated wage adjustment during the period of construction. The Contractor is entitled to labor cost escalation even after the expiration of the extended completion period since the Owner allowed it to continue with the works, and since the Owner accepted and paid

the Contractor's accomplishments, labor cost escalation has already been earned and should be paid for.

## **CLAIM FOR ADDITIONAL COSTS DUE TO ACCELERATION OF WORK**

**R-II Builders, Inc. v. Mivan Builders, Inc., G.R. Nos. 152545 & 165687, November 15, 2005**

On Contractor's request, the Sub-Contractor fast-tracked the completion of a number of buildings comprising the project and thereafter demanded payment for additional costs incurred therefor consisting of increased costs of labor, materials, and equipment. The Contractor did not contest the Sub-Contractor's computation but denied liability arguing that the order for acceleration of work came from the Owner and that the procedural requirement of a timely submission of cost impact has not been complied with.

The Supreme Court held:

The Contractor is very much aware that such acceleration of work necessarily entails additional costs, thus, its silence about the lack of explicit agreement on who should bear such additional costs contradicts the principles of fair dealing which should be the norm of all transactions (*Art. 19, Civil Code*). On the other hand, the Sub-Contractor's similar silence cannot be presumed that it agreed to bear the increased costs as such would result in unjust enrichment which the law abhors (*Art. 2142, Civil Code*). The Sub-Contractor's compliance with the Contractor's request for early completion was in effect a binding modificatory novation of the Contract. The reasonable inference on the parties' silence on who should bear the costs involved was that the parties had impliedly agreed to charge the increased costs to the Sub-Contract as a Change Order. The Contractor did not offer any compelling reason to reverse the ruling of the Construction Industry Arbitration Commission (CIAC) on this claim. Thus, the Court affirmed the CIAC's ruling and award of additional costs incurred for early completion of portion of the project covering the increased costs of labor, materials, and equipment, which were held to be not only legally tenable, but equitable considerations also support it.

## **CLAIM AGAINST THE BONDS UPON TERMINATION OF THE CONTRACT DUE TO DELAYS IN THE PROJECT**

**J Plus Asia Development Corporation v. Utility Assurance Corporation, G.R. No. 199650, June 26, 2013**

The Contractor in this case incurred tremendous delay in executing the works for the project. Under the Contract, the project is supposed to be completed in December 2008 but the Contractor has completed only 31.39% of the works as of 14 November

2008 as per the joint evaluation conducted by the parties. The Contractor did not ask for an extension of time to complete the project. The Owner thus terminated the Contract, and demanded from the Contractor the payment of liquidated damages and the return of the unrecouped down payment and overpayment. The Owner also made a claim against the Performance Bond to recover the damages it suffered caused by such delay. The Contractor, on the other hand, contends that the Performance Bond merely guaranteed the 20% down payment and not the entire obligation under the Contract, and that since its accomplishment already exceeded such amount, its obligation under the bond had been fully extinguished.

The Supreme Court held:

*Default or mora on the part of the debtor is the delay in the fulfillment of the prestation by reason of a cause imputable to the former. It is the nonfulfillment of an obligation with respect to time. It is a general rule that one who contracts to complete certain work within a certain time is liable for the damage for not completing it within such time, unless the delay is excused or waived.*

While the Contract contemplates delay in the completion of the project, such, however, does not defeat the Owner's right to claim for damages or the Contractor's liability under the Performance Bond. The Contract stipulates that the Owner shall be entitled to confiscate the performance bond to compensate for all the damages it suffered due to delay in the completion of the Project by more than thirty (30) days. Such stipulation depicts the nature of a penalty clause, which is recognized by law as "an accessory undertaking to assume greater liability on the part of the obligor in case of breach of an obligation. It functions to strengthen the coercive force of obligation and to provide, in effect, for what could be the liquidated damages resulting from such a breach. The obligor would then be bound to pay the stipulated indemnity without the necessity of proof on the existence and on the measure of damages caused by the breach. It is well-settled that so long as such stipulation does not contravene law, morals, or public order, it is strictly binding upon the obligor". The Surety was ordered to pay the Owner the full amount of the Performance Bond with interest.

**Philippine Charter Insurance Corporation vs. Central Colleges of the Philippines and Dynamic Planners and Construction Corporation, G.R. No. 180631-33, February 22, 2012**

The Owner terminated the Contract for failure of the Contractor to complete the project on time. The Contractor's accomplishment at the time of termination was only at 57.33%. The Owner claimed against the Performance Bond and the Surety Bond for the unrecouped down-payment. The Surety denied its liability under the bonds it issued arguing that the reglementary period within which to file a claim against the bonds had already expired. It contends that the claim should have been filed ten days from the occurrence of the default.



The Supreme Court held:

*The civil law concept of delay or default commences from the time the obligor demands, judicially or extrajudicially, the fulfillment of the obligation from the obligee. In legal parlance, demand is the assertion of a legal or procedural right. It is the obligor's culpable delay, not merely the time element, which gives the obligee the right to seek the performance of the obligation.*

In this case, the default commenced when the Owner informed the Contractor and the Surety in writing prior to expiration of the bonds of the breach in the contract and its plan to claim against the bonds. Upon such notice, the Surety's liability had already attached pursuant to Article 2047 of the Civil Code, thus, it is duty bound to perform what it has guaranteed under the Performance and Surety Bonds, all of which are callable on demand. The Surety and the Contractor were ordered to jointly and severally pay the Owner the total amount of the Surety and Performance Bonds.

## **RELEASE OF RETENTION UPON TERMINATION OF THE CONTRACT**

**The President of the Church of Jesus Christ of Latter Day Saints v. BTL Construction Corporation, G.R. No. 176439, January 15, 2014; BTL Construction Corporation v. The President of the Manila Mission of the Church of Jesus Christ of Latter Day Saints and BPI-MS Insurance Corporation, G.R. No. 176718, January 15, 2014**

In issue is the Contractor's entitlement to the release of retention upon the termination of the Contract.

Due to the Contractor's financial difficulties and losses, and upon the request of the Contractor, the Owner and the Contractor executed a deed of assignment in favor of the Contractor's suppliers for the project so that they may collect directly from the Owner. A few months thereafter, the Contractor ceased its operations for lack of funds to pay for the cost of labor and other items necessary to complete the project. Consequently, the Owner terminated the Contract and engaged the services of another contractor to complete the project. The Contractor claimed for payment of its work accomplishment and the release of retention. The Owner, however, refused to release the retention since they have already agreed that such amount will answer for the payment to the Contractor's suppliers.

The Supreme Court held:

*The nature of the 10% retention money is that it is a portion of the contract price withheld from the contractor to function as a security for any corrective work to be performed on the infrastructure covered by a construction contract. As such, the 10% retention money should not be treated as a separate and distinct liability as it merely forms part of the contract price.*



While the retention will be eventually released to the Contractor, such amount should be automatically deducted from the Contractor's billings. Thus, the award to the Contractor of the unpaid balance of the contract price inclusive of the 10% retention.