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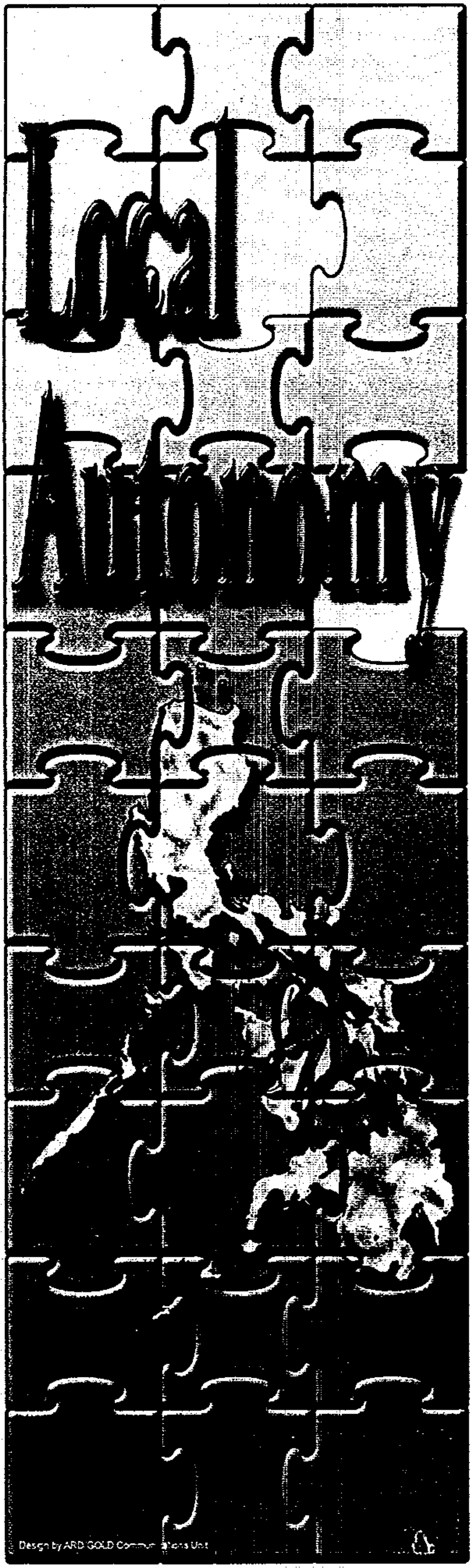

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Financing Local Infrastructure Projects Through Joint Ventures

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The *Local Autonomy* series is a publication of the GOLD Project which aims to provide information and insights and to contribute to the discourse and debate on the devolution brought about by the Local Government Code of 1991. These papers are not fixed policy pronouncements, but are intended to provide a forum for policy dialogue.

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Financing Local Infrastructure Projects Through Joint Ventures[1]

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The use of joint ventures as vehicles for private participation in government infrastructure projects has gained acceptance over the last three years owing in large part to the successful implementation of the Metro Manila Skyway Project, a joint venture between the Philippine National Construction Corporation and various foreign companies. However, notwithstanding the precedent set by the Skyway and other toll road projects, the private sector remains cautious in structuring their transaction with the government as joint ventures. Private investors fear that the absence of a specific legal framework governing joint ventures will subject their transactions with government to potential legal difficulties.

Indeed, there is no one law where the legal framework for joint ventures may be found. This paper attempts to construct that legal framework through a survey of laws applicable to joint ventures, as well as to each specific undertaking commonly assumed by government under joint venture contracts.

The objective of the paper is two-fold. First, it seeks to compile in a single document the possible approval and other substantial and procedural requirements applicable to projects undertaken through joint venture arrangements. Second, it hopes to provide both the government and the private sector basis for assessing the legal risks involved in using joint ventures as transaction structures for their projects with government. The ideas in this paper are developed around the context of local government infrastructure projects.

This paper is divided into four parts. The first part describes the concept of a joint venture and discusses certain characteristics of a joint venture that every investor, whether government or private, must consider in deciding the structure of its investment. The second part argues the existence of the authority of local governments to enter into joint ventures. The third part enumerates certain restrictions on such authority that must be observed to ensure the validity of joint venture contracts with local governments. The last part identifies specific undertakings usually assumed by local governments under joint venture contracts that may require additional approvals or impose additional restrictions.

I. Concept of a Joint Venture

The Supreme Court, citing Black's Law Dictionary, defines a joint venture as follows: "[A]n association of persons or companies jointly undertaking some commercial enterprise; generally all contribute assets and share risks. It requires a community of interest in the performance of the subject matter, a right to direct and govern the policy in connection therewith, and duty, which may be altered by agreement to share both in profit and losses." *Kilosbayan Incorporated vs. Guingona Jr.*, 232 SCRA 110 (1994). Three elements of a joint venture may be culled from the above definition:

(i) a common interest in the performance of the obligation and in the management of the enterprise;

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(ii) a mutual contribution of money, contractual rights, labor, or other properties; and,

(iii) a sharing in the risks involved.

The elements of a joint venture are the same as those of a partnership, a nominate contract and a business form specifically governed by Articles 1767 to 1867 of Republic Act (*"R.A."*) No. 386 as amended or the Civil Code of the Philippines (the *"Civil Code"*). Because of the similarity in the elements of a joint venture and a partnership, the Supreme Court has ruled that a joint venture is a form of partnership and should thus be governed by the laws on partnership:

> The legal concept of a joint venture is of common law origin. It has no precise legal definition, but it has been generally understood to mean an organization formed for some temporary purpose. (Gates v. Megargel, 266 Fed. 811 [1920]) It is in fact hardly distinguishable from the partnership, since their elements are similar — community of interest in the business, sharing of profits and losses, and a mutual right of control. (Blackner v. McDermott, 176 F. 2d. 498, [1949]; Carboneau v. Peterson, 95 P. 2d., 1043 [1939]; Buckley v. Chadwick, 45 Cal. 2d. 183, 288 P. 2d. 12 289 P. 2d. 242 [1955]). The main distinction cited by most opinions in common law jurisdictions is that the partnership contemplates a general business with some degree of continuity, while the joint venture is formed for the execution of a single transaction, and is thus of a temporary nature. (Tufts v. Mann. 116 Cal. App. 170, 2 P. 2d. 500 [1931]; Harmon v. Martin, 395 Ill. 595, 71 NE 2d. 74 [1947]; Gates v. Megargel 266 Fed. 811 [1920]). This observation is not entirely accurate in this jurisdiction, since under the Civil Code, a partnership may be particular or universal, and a particular partnership may have for its object a specific undertaking. (Art. 1783, Civil Code). It would seem therefore that under Philippine law, a joint venture is a form of partnership and should thus be governed by the law of partnerships. The Supreme Court has however recognized a distinction between these two business forms, and has held that although a corporation cannot enter into a partnership contract, it may however engage in a joint venture with others. (At p. 12, Tuazon v. Bolaños, 95 Phil. 906 [1954]) (Campos and Lopez — Campos Comments, Notes and Selected Cases, Corporation Code 1981).

Aurbach vs. Saniwares, G.R. No. 75875 (December 15, 1989).

Like a partnership, a joint venture is fundamentally contractual. As such, a joint venture affords the parties a great degree of flexibility in ordering their relations and in fixing the conditions under which they shall operate as a business organization.

As a general rule, no special form is required for a contract of partnership. The contract may be made orally or in writing. The only exception is where immovable property or real rights are contributed thereto, in which case a public instrument shall be necessary. *Civil Code, Art. 1771.* Under Article 1772 of the Civil Code, every contract of partnership with capital of three thousand pesos or more must appear in a public instrument and registered with the Securities and Exchange Commission (SEC). However, failure to comply with the registration requirement does not affect the validity of the contract or prevent the formation of the partnership or joint venture. Registration has become a necessity only as a practical matter because government agencies require registration as a precondition for issuance of business licenses.

A joint venture, as is a partnership, is endowed by law with juridical personality separate and distinct from each of the joint venturers. As a juridical person, a joint venture may enter into contracts, acquire property of all kinds in its own name, incur obligations and bring civil and criminal actions. *Civil Code, Art. 46.* The separate juridical personality of a joint venture attaches from the moment of execution of the contract, unless there is a contrary stipulation in such contract. *Civil Code, Art. 1784.*

As a business relationship, a joint venture is characterized by the principle of *delectus personae* wherein personal attributes of each party are deemed important consideration for the consent of the other party to the contract. A joint venture is a relationship created and maintained on the basis of trust and confidence. Accordingly, a joint venturer may not allow another person to take his place without the consent of all the other parties to the contract. Under Article 1813 of the Civil Code, while a partner may convey the whole of its interest in a partnership without causing a dissolution, the person to whom he has assigned his interest cannot interfere in the management or administration of the partnership business or affairs, or require any information or account of partnership transactions, or inspect the partnership books. The assignee is entitled only to receive the profits to which the assigning partner would otherwise be entitled. Likewise, the inability of one partner to continue in the partnership because of death, insolvency, civil interdiction or retirement would cause a dissolution of the partnership. Finally, as each partner is considered a fiduciary of the other, it has the obligation to observe the utmost good faith, fairness, honesty and integrity in its dealings with the other with respect to partnership affairs.

A joint venture also creates a contract of mutual agency between the parties. Under Article 1818 of the Civil Code, every partner is an agent of the partnership for the purpose of its business, and the act of every partner, including the execution in the partnership name of any instrument, for apparently carrying on the usual business of the partnership, binds the partnership. Parties to a contract of partnership may limit the authority of the partners to bind the partnership by providing for the appointment of a managing partner, or requiring a minimum number of votes for transactions of the partnership. However, contractual limitations on authority of any partner are not binding upon third parties without actual knowledge of such limitations. *Civil Code, Article 1818.* Stated otherwise, notwithstanding that a contract of partnership specifically denies a partner the authority to act for the partnership, contracts entered into by such partner with third persons who have no actual knowledge of the lack of authority of such partner may bind the partnership. Third persons have no duty to make inquiries as to the acting partner's authority.

The foregoing attributes of a joint venture should be considered by any investor – government or private sector alike – in deciding the appropriate structure for its investment projects. Specifically, the impact of certain features of a joint venture on the commercial objectives of the investor or on the requirements of the project should be carefully considered.

Perhaps one major consideration against the use of a contractual joint venture as a business vehicle is the potential for a joint venturer to become liable for the obligations of the joint venture beyond the amount of its intended investment. Under Article 1816 of the Civil Code, all partners are liable *pro rata* with all their property and after all the partnership assets have been exhausted for contracts entered into in the name and for the account of the partnership. Thus, unlike a corporate structure where stockholders enjoy limited liability, parties in a joint venture contract may be held personally liable by the creditors of the joint venture beyond the amount of their investments. There are, however, ways of assimilating the limited liability feature of a corporation in a joint venture arrangement. One way is to form an incorporated joint venture which will have all the legal attributes of a corporation including the limited liability feature. Another way is for joint venturers to individually form a single-purpose corporation which, in turn, enters into the joint venture contract. Under this structure, the liability of the parties to the joint venture contract will be limited to their investments in the single-purpose corporation.

Investors may also find a contractual joint venture unattractive as a vehicle for their investments because it has no inherent right of succession. The right of succession is a legal attribute inherent in a corporation that allows it, as a separate and distinct juridical personality, to continue with its business despite death or retirement of its shareholders. As already discussed, the death, retirement, withdrawal, or civil interdiction of any partner may cause the dissolution of a partnership. This may become an important consideration when the parties try to get financing for their project. Creditors will usually like to be assured of the continued existence of the entity they are lending to.

However, while the right of succession is not inherent in a contractual joint venture, the same may be specifically provided for in the contract. Partners may stipulate that those who shall remain after the withdrawal of any one of them shall have the right to continue the business of the partnership.

Joint venture partners may also address concerns over the survival of a joint venture as a separate juridical person by incorporating the same.

Finally, certain investors may prefer a more centralized management of their business, which is not possible in a contractual joint venture because under the law, management agreements between the partners are not necessarily binding on third persons. A way around this limitation is to make a very narrow definition of the business purpose of the joint venture. Under the law, a partner is considered an agent of the partnership only for the purpose of its business. Another solution is to form a joint venture corporation where decision-making will be centralized in the board of directors.

It is apparent from the above discussion that most risks and concerns present in a contractual joint venture may be addressed through an incorporated joint venture. Incorporation of the joint venture, however, would move the vehicle from the realm of partnership law to the realm of corporation law. Certain attributes, especially those arising from the principle of *delectus personae,* may be lost if the joint venture takes the corporate form. For instance Philippine corporation law requires free transferability of shares of stock with very narrow exceptions. Nonetheless, within these narrow exceptions, parties in a joint venture contract may find assurance against indiscriminate changes in their joint venture partners.

Thus, most joint venturers forming a corporation incorporate in their agreement and in the articles of incorporation of the joint venture corporation a provision which grants both parties a pre-emptive right over additional issuance of shares by the corporation or a right of first refusal on the transfer or sale of shares by the other party. Joint venturers may also include in their articles of incorporation a "piggy-back" provision. A "piggy-back" is a provision which allows the minority shareholder to ride-on any intended sale of shares by the majority shareholder by enjoining the majority shareholder to buy all of its shares (who is now burdened with the responsibility of selling all the shares to a third party) or which prohibits the majority shareholder from accepting any offer made by any third party to buy its shares unless such third party also offers to buy the shares of the minority on the same terms and conditions as the offer made to the majority shareholder. As may be inferred, piggy-back provisions are designed to protect minority shareholders who usually do not have enough capital to buy the shares of the majority shareholder and, thus, prevent them from exercising their pre-emptive rights or rights of first refusal.

II. Authority of Local Governments to Enter into Joint Ventures

It used to be that local government units, such as provinces, cities, municipalities and *barangays,* are regarded as subordinate branches of the government of the State. *Ruperto G. Martin, Public Corporations (1985) at 105.* As mere creations of the legislature, local government units are said to have very limited powers: They can exercise only such powers as are expressly granted to them and those which are necessarily implied or incidental to the exercise thereof. *City of Ozamiz v. Lumapas*, G.R. No. L-30727 (July 15, 1975).

These basic precepts are under challenge. The adoption of the 1987 Constitution, that raises to a constitutional right the right of provinces, cities, municipalities, and barangays to exist as political and territorial subdivisions of the Philippines and expressly declares local autonomy as a state policy, has ushered a more liberal view of the scope of power of local governments. Under the liberal view, local governments have the authority to do any act or to engage in any undertaking not otherwise prohibited by law pursuant to the fundamental grant of local autonomy and in furtherance of the general welfare of the community. *Alberto C. Agra, Local Autonomy and Government, Ateneo Center for Continuing Legal Education (1999) at 4-5.* This notion stands in sharp contrast with the centralist view, under which local governments may exercise only those powers expressly delegated to them and those necessarily implied therefrom. *Id.*

Republic Act No. 7160, otherwise known as the Local Government Code of 1991 or the LGC, supports a more liberal interpretation of the powers of local governments. Section 5 of that law states that any provision on a power of a local government unit shall be liberally interpreted in its favor, and any fair and reasonable doubt as to the existence of such power shall be interpreted in favor of the local government unit concerned.

Whether under the liberal or centralist view of local autonomy, or the liberal or strict interpretation of the powers of local governments under the LGC, local governments have the authority to enter into joint ventures.

Section 15 of the LGC acknowledges the dual nature of local government units. It states that every local government unit is a body politic and corporate and as such shall exercise powers as a political subdivision of the national government and as a corporate entity representing the inhabitants of the territory. As a body corporate, every local government unit is expressly granted the power to enter into contracts and to exercise such other powers as are granted to corporations, subject to the limitations provided in the LGC and other laws. *LGC, Sec. 22(a)(5) and (6).*

The power to contract has itself been held broad enough as to authorize local governments to enter into joint ventures. *Reports on the Provincial Public Utilities Department-Provincial Electric System Province of Bohol (June 1999) at 9 <u>citing</u> the legal opinion of the Provincial Attorney of Bohol dated August 7, 1998.* On the other hand, the powers, rights and privileges of private corporations are embodied in the Corporation Code of the Philippines ("Corporation Code"). And in at least one case, the Supreme Court ruled that private corporations may enter into joint ventures with other entities provided the nature of that venture is in line with the business authorized by its charter. *J.M. Tuason & Co., Inc. v. Bolaños*, 95 Phil 106 (1954).

The authority of local government units to enter into joint ventures does not rest solely on the general contracting authority and corporate powers of the local government units.

The LGC contains various provisions allowing the local government units to tap private resources in the performance of certain governmental and proprietary functions. Section 3 (l) of the LGC expressly provides that the participation of the private sector in local governance, particularly in the delivery of basic services, shall be encouraged to ensure the viability of local autonomy as an alternative strategy for sustainable development.

In Opinion No. 79, Series of 1994, the Department of Justice (DOJ) upheld the authority of Philippine National Construction Corporation (PNCC) to enter into joint ventures on the basis of a whereas clause in the PNCC franchise which states that PNCC may have to "tap private resources and enterprises which will at the same time allow the government to redirect its own resources to other infrastructure projects." The language used in the LGC encouraging private sector participation in the delivery of basic services is even more explicit and provides stronger basis for the authority of local governments to enter into joint ventures for such purpose.

On the other hand, Section 22(d) of the LGC guarantees local government units "full autonomy in the exercise of their proprietary functions and in the management of their economic enterprises, subject to the limitations provided in the LGC and other applicable laws." Powers which local governments exercise in their proprietary capacity are those which are meant to promote the local necessities and conveniences of the communities they serve. *City of Manila v. Intermediate Appellate Court*, G.R. No. 71159 (November 15, 1989); *Torio v. Fontanilla*, 85 SCRA 599 (1978). On the other hand, the term "economic enterprises" has been defined in Memorandum Circular No. 90-104 issued by the Department of Interior and Local Governments (DILG) on December 3, 1990 to prescribe policies and guidelines for the privatization of basic services and management of economic enterprises as "income generating ventures of local governments" and include public markets, slaughterhouses, garbage collection and disposal, water supply, road construction, repair and maintenance, and health services.

The guarantee of full autonomy in the local governments' exercise of their proprietary functions assures local governments the flexibility to choose the means by which they shall discharge such functions, whether alone or in joint venture with the private sector.

Furthermore, Section 17(j) empowers local government units, by ordinance, to sell, lease, encumber, or otherwise dispose of public economic enterprises owned by them in their proprietary capacity. A joint venture is a form of partial privatization, with the local governments retaining certain equity interest. Entry into joint venture arrangements may thus be considered as part of the larger power of local governments to sell, alienate, encumber the public economic enterprises which they own in their proprietary capacity.

Finally, Section 35 of the LGC expressly grants the local government units the authority to enter into joint ventures and other cooperative arrangements with people's and nongovernmental organizations for various purposes ranging from delivery of basic services to enhancement of the economic and social well-being of the people.

> Sec. 35. *Linkages with People's and Non-governmental Organizations.* - A local government unit may enter into joint ventures and such other cooperative arrangements with people's and nongovernmental organizations to engage in the delivery of certain basic services, capability-building and livelihood projects, and to develop local enterprises designed to improve productivity and income, diversify agriculture, spur rural industrialization, promote ecological balance, and enhance the economic and social well-being of the people.

Rule XIII, Article 62 of the Implementing Rules and Regulations of the LGC extends the application of Section 35 of the LGC to joint ventures with the private sector in general, and clarifies that joint venture is a scheme that may be used to tap private resources quite apart from financing under the Build-Operate and Transfer scheme under Republic Act No. 6597, as amended by Republic Act No. 7718. Thus:

> Art. 62. *Role of People's Organizations, Nongovernmental Organizations (NGOs) and the Private Sector.* - LGUs shall promote the establishment and operation of

people's organizations, NGOs and the private sector, to make them active partners in the pursuit of local autonomy. For this purpose, people's organizations, NGOs, and the private sector shall be directly involved in the following plans, programs, projects, or activities of the LGUs:

(a) Local special bodies;

(b) Delivery of basic services and facilities;

(c) Joint ventures and cooperative programs and undertakings;

(d) Financial and other forms of assistance;

(e) Preferential treatment for organizations and cooperatives of marginal fishermen;

(f) Preferential treatment for cooperatives development; and

(g) Financing, construction, maintenance, operation, and management of infrastructure projects.

The LGC contains provisions that support, in both broad and specific language, the authority of local governments to enter into joint ventures. Considering the interpretation given to such provisions by the administrative agencies of the government, whose opinions are entitled to great weight and respect, the existence of the local government's power to enter into joint ventures, at least for certain purposes, appears beyond doubt.

III. Requirements and Restrictions Applicable to Local Government Joint Ventures

A joint venture is a contract. Like any contract, a joint venture, to be valid, must have the consent of the contracting parties, a lawful object or subject matter, and a lawful cause or consideration. *Civil Code, Arts. 1318 and 1409.*

And like any private contracting party, the Government is given the full liberty to enter into any stipulations, terms, or conditions, as it may deem convenient or desirable. *Civil Code, Art. 1306.* The only limitation is that such stipulations, terms, and conditions must not violate laws, morals, good customs, public order, or public policy. *Id.* The laws that the terms of a contract must not contravene are those which expressly declare their obligatory character, or which are prohibitive, or which express fundamental principles of justice, or which impose essential requisites without which the contract cannot exist. *4 Tolentino, Commentaries and Jurisprudence on the Civil Code of the Philippines 416 (1986).* On the other hand, a contract may be said to violate morals and good customs if the terms thereof infringe generally accepted principles of morality which have received some kind of social and practical confirmation. *Id. at 418.* Finally, a contract will be declared void as against public policy if it is contrary to law, or if it contravenes some established interest of society, or is inconsistent with sound policy and good morals, or tends clearly to undermine the security of individual rights. *Id. At 420.*

A private party contracting with the Government bears the burden of ensuring that its contract with the Government complies with all applicable legal requirements, whether they relate to substance, form, or procedure. Persons dealing with the Government and its officials and agents must take notice of their authority and are charged with knowledge of the limitations on their powers. Not even the doctrine of estoppel lies to validate contracts entered into by the Government and its officials and agents in excess of their authority and contrary to prescribed conditions and procedures. As held by the Supreme Court in relation to municipal corporations:

> The doctrine of estoppel can not be applied as against a municipal corporation which it has no power to make, or which it is authorized to make only under prescribed conditions, within prescribed limitations, or in a prescribed mode

> or manner, although the corporation has accepted the benefits thereof and the other party has fully performed his part of the agreement, or has expended large sums in preparation for performance. *San Diego v. Municipality of Naujan,* 107 Phil. 118 (1960); *Favis v. Municipality of Sabangan,* 27 SCRA 92 (1969).

The object of this part of the paper is to enumerate and discuss the specific requirements for validity of local government joint ventures, as well as the restrictions to the local governments' authority to enter into joint ventures. These requirements and restrictions may be generally categorized into three types: (i) those relating to the project; (ii) those generally applicable to contracts entered into by local governments, and (iii) those arising from the special nature of a joint venture contract.

A. *Requirements and Restrictions Relating to the Joint Venture Project*

1. Object of the Joint Venture

The authority to enter into contracts, as well as to exercise such other powers as are granted to corporations, is given to local government units in their capacity as corporations. *LGC, Sec. 22.* Like any other private corporations, local government units may exercise such inherent powers only in furtherance of their declared objects or purposes. In the context of joint ventures, this means that local government units may form only those joint ventures whose object or purpose is in line with the object or purpose of local government units. This principle at once circumscribes the power of local government units to enter into joint ventures, both in respect of the nature of the object or the specific undertaking of the joint venture, and the territorial coverage of the joint venture.

(a) *Nature of the Undertaking*

Local government units have dual functions. First, they serve as instrumentality of the state in carrying out the functions of government. Second, they act as an agency of the community in the administration of local affairs, performing acts not strictly governmental but proprietary or ministrant. In performing either function, local government units are guided by one fundamental objective, that is, the promotion of the general welfare of their respective constituencies. Section 16 of the LGC sets forth the breadth and scope of local government powers as they relate to the promotion of the general welfare:

> Section 16. *General Welfare*. Every local government unit shall exercise the powers expressly granted, those necessarily implied therefrom, as well as powers necessary, appropriate or incidental for its efficient and effective governance, and those which are essential to the promotion of the general welfare. Within their respective territorial jurisdictions, local government units shall ensure and support, among other things, the preservation and enrichment of culture, promote health and safety, enhance the right of the people to a balanced ecology, encourage and support the development of appropriate and self-reliant scientific and technological capabilities, improve public morals, enhance economic prosperity, and social justice, promote full employment among their residents, maintain peace and order, and preserve the comfort and convenience of their inhabitants.

Under the quoted provision, local governments may perform just about any power that will benefit their constituencies, including the construction and operation of infrastructure facilities. Thus, in at least one case, the Supreme Court ruled that the general welfare clause authorizes local governments units to engage in activities not purely governmental in character, but proprietary as well, such as the operation of a telecommunications service. *Philippine Long Distance Telephone Company vs. City of Davao, et al.*, G.R. No. L-23080 (October 30, 1965).

In the area of infrastructure development, the authority given to local government units is even explicit and specific. Section 17 of the LGC gives the local government units both the power and responsibility to provide their respective communities certain basic services and facilities. It authorizes local government units to exercise such power as is "necessary, appropriate or incidental" to the efficient and effective provision of such basic services and facilities.

The basic services and facilities that local government units are expressly authorized and required to provide vary according to their level at the hierarchy of the local governmental structure. *Barangays*, the smallest local government units, are given the least powers. In the field of infrastructure development, their express authority cover (i) the maintenance of *barangay* roads, bridges, and water supply facilities, (ii) the construction and operation of satellite or public market, where viable, and (iii) the provision of services and facilities related to general hygiene and sanitation, beautification, and solid waste collection. *LGC, Sec. 17(b)(1)*.

Municipalities are given much broader powers, including the provision of the following services and facilities: (i) solid waste disposal system or environmental management system and services or facilities related to general hygiene and sanitation; (ii) municipal roads and bridges, communal irrigation, small water impounding projects, fish ports, artesian wells, spring development, rainwater collectors, and water supply systems, and other infrastructure facilities intended primarily to service the needs of the residents of the municipality; (iii) public markets, slaughterhouses and other municipal enterprises; (iv) public cemetery; and, (v) tourism facilities and other tourist attractions. *LGC, Sec. 17(b)(2)*.

Provinces, on the other hand, are empowered to engage in various infrastructure projects, including the following: (i) mini-hydroelectric power projects for local purposes; (ii) provincial roads and bridges, inter-municipal waterworks, drainage and sewerage, flood control and irrigation systems, reclamation projects and other infrastructure facilities intended to service the needs of the residents of the provinces; (iii) programs and projects for low cost housing and other mass dwellings, except those funded by the Social Security System, Government Service Insurance System, and the Home Development Mutual Fund; (iv) inter-municipal telecommunications services, subject to national policy guidelines; and (v) tourism development and promotion programs. *LGC, Sec. 17(b)(3)*.

Finally, cities are given all the powers given to municipalities and provinces, and in addition, the authority to provide adequate communication and transportation facilities, and support for education, police, and fire services and facilities. *LGC, Sec. 17(b)(4)*.

The enumeration of services and facilities that local government units are authorized to provide under Section 17 of the LGC is not exclusive. This is evident from Section 17 of the LGC itself, which expressly states that local government units may provide basic services and facilities, including, but not limited to, those expressly enumerated therein. In fact, local government units may provide any facility or service that may not come within the enumeration of Section 17 of the LGC so long as it is of such a nature as would promote the general welfare of their respective constituencies. *Philippine Long Distance Telephone Company vs. City of Davao, et al.*, G.R. No. L-23080 (October 30, 1965).

(b) ***Territorial Coverage***

Perhaps the more serious limitation affecting local government units relates to the territorial reach of their powers, rather than to the nature of the activities that they are authorized to undertake. It is a general rule that municipal corporations cannot, without legal authorization, exercise its powers beyond its own corporate limits. *Martin, supra at 23.* Section 16 of the LGC accordingly limits the authority of local government units to exercise powers to promote general welfare "within their respective territorial jurisdictions." Section 17 of the LGC, on the other hand, authorizes municipalities, provinces, and cities to build only such infrastructure facilities as would service the needs of their residents. Nonetheless, if a wide area coverage is necessary for a joint venture undertaking to achieve the desirable economies of scale, private parties may contract with the local government units with the widest area jurisdiction, *i.e.*, provinces, or they may urge various local government units to jointly undertake infrastructure projects. Under Section 33 of the LGC, local government units may, through appropriate ordinances, group themselves, consolidate, or coordinate their efforts, services, and resources for purposes commonly beneficial to them. In support of such undertakings, the local governments units involved may, upon approval by the *sanggunian* concerned after a public hearing conducted for the purpose, contribute funds, real estate, equipment, and other kinds of property and appoint or assign personnel under such terms and conditions as may be agreed upon by the participating local units through memoranda of agreement.

2. **Constitutional Limitations**

The general welfare clause is broad enough to authorize local government units to undertake, either alone or in joint venture with the private sector, any conceivable infrastructure projects. However, local government units should not engage in activities adequately and competently undertaken by the private sector. Otherwise, they will be violating the declared policy under the 1987 Constitution of encouraging private initiative in economic development. *1987 Constitution, Art. II, Sec. 20.*

3. **Inclusion in the Local Development Plan**

Finally, the project or activity that will be undertaken by the joint venture between a local government unit and the private sector must be included in the local development plan of the local government unit concerned.

Under Section 106 of the LGC, each local government unit is required to draft, through the initiative of its local development council, a comprehensive multi-sectoral development plan. Essentially, this plan sets the direction of social and economic developments within the local government unit. Local development plans of local government units are considered in the formulation of national development plans, in order to optimize the use of government resources and to avoid duplication in the use of fiscal and physical resources. *LGC, Sec. 305.* Local development plans also form an integral part of national and local budgeting process. They are considered in the formulation of budgets of national line agencies and offices. *Id.* Local governments, on the other hand, are required to formulate local budgets that "operationalize approved local development plans." *Id.* Local development plans must be approved by the *sanggunians* of the local government units. Local development plans of component cities and municipalities must be submitted to the provincial legislative bodies for review. *LGC, Sec. 56.* This review, however, is limited; it is meant to ensure only that component cities and municipalities are acting within the scope of their authority. *Id.*

Considering the role of local development plans in the budget process, it is important for any project or activity that will be undertaken by local governments in joint venture with the private sector to be included in such plans. Otherwise, no appropriation may be made to fund whatever financial obligation the local governments may assume under the joint venture. Neither can local governments avail themselves of credit facilities to fund their share in the venture. Under Section 296 of the LGC, local government units may create indebtedness and avail of credit facilities to finance local infrastructure projects only in accordance with the approved local development plans and public investment programs.

B. *Requirements and Restrictions Generally Applicable to Local Government Contracts*

1. Object of the Joint Venture

Government contracts must be executed by public officials with the proper authority to do so. Since government like any other corporation is an artificial person, it can only act or bind itself through its duly authorized agents. Under the rules on agency, an agent who acts beyond the scope of his or her authority shall not bind the principal. Public officials, therefore, who enter into government contracts without the requisite authority to do so, do not bind the government.

For local governments, the relevant contracting authority is found in Section 51 of the Administrative Code of 1987. It reads: "Contracts executed in behalf of the political subdivisions and corporate agencies or instrumentalities shall be approved by their respective governing boards or councils and executed by their respective executive heads."

The chief executive of a *barangay* is the *punong barangay*; of the municipality, the municipal mayor; the city, the city mayor; and of the province, the provincial governor. The authority of these local chief executives to negotiate, enter into and sign all bonds, contracts and obligations in behalf of their respective local government units is expressly stated in the enumeration of their specific powers under the LGC. *See LGC, Sections 389 (2); 444 (vi); 455 (vi); 465 (vi).*

2. General Review and Approval Process

A government contract is not perfected until such contract has passed the appropriate review and approval process prescribed by law and other relevant rules and regulations. The review and approval process generally required for all types of contracts entered into by local governments is described below.

(a) ***Sanggunian Approval***

In general, all contracts entered into by local government units require the approval of their respective *sanggunians*. Pursuant to Section 51 of the Administrative Code of 1987, contracts executed in behalf of political subdivisions require the approval of their respective governing boards or councils. Specifically, Section 22 (c) of the LGC states that unless otherwise provided therein, no contract may be entered into by the local chief executive without prior authorization of the *sanggunian* concerned. Thus, it has been ruled by the DILG in one opinion that council authorization is a condition precedent to the validity of the contract of a local government unit. *DILG Opinion No. 156-1993.* Under the LGC, the governing board or council for the *barangay* is the *sanggunian barangay*; for the municipality, the *sanggunian bayan*; for the city, the *sanggunian panglungsod*; and for the province, the *sanggunian panlalawigan*.

As a general rule, no specific form of *sanggunian* approval is required for local government contracts. Hence, in giving such approval, the local councils may proceed either by way of a resolution or ordinance. Certain types of contract, however, require authorization from local legislative bodies in the form of an ordinance. One such type of contract is a contract for the sale, lease, encumbrance or other disposition of public economic enterprises owned by local government units in their proprietary capacity. *LGS, Sec. 17 (j).* It is common for local government units to contribute infrastructure facilities they own in their proprietary capacity in exchange for a share in the joint venture entity. If such disposition is embodied in the joint venture contract, the *sanggunian* authorization for the contract must be in the form of an ordinance.

(b) ***Posting Requirement***

It must also be noted that Section 22 (c) of the LGC requires the posting of a legible copy of the contract at a conspicuous place in the provincial capitol or the city, municipal, or *barangay* hall. The apparent intent of this posting requirement is to ensure transparency in the affairs of the local government.

(c) ***Review by Higher Sanggunian***

Barangay ordinances must be submitted to the city and/or municipal councils for review. *LGC, Sec. 57(a).* The review power of cities and municipalities is limited to ensuring that the *barangay* ordinance is not inconsistent with laws and ordinances. *Id.*

Except for ordinances and resolutions approving the development plans and public investment programs formulated by the city or municipal development councils and those authorizing annual or supplemental appropriations, ordinances enacted by the *sangguniang panglungsod* or the *sangguniang bayan* are not subject to the same review process required for *barangay* ordinances. *IRR, Art. 59 (2), (3).* Ordinances enacted by the *sangguniang panlalawigan* are likewise not subject to a similar review process.

(d) ***COA Review***

Local government contracts are also submitted to the Commission on Audit (COA) for review.

As a general rule, the COA undertakes review of government contracts not as a prerequisite for their perfection, but only for the purpose of passing upon the validity and enforceability of such contracts. Under Section 2, Article IX-D of the 1987 Constitution, the COA has the power, authority, and duty to examine, audit, and settle all accounts pertaining to the revenue and receipts of, and expenditures or uses of funds and property, owned or held in trust by, or pertaining to, the government or any of its subdivisions, agencies or instrumentalities, including government-owned and controlled corporations with original charters. The COA's auditing power includes promulgating accounting and auditing rules and regulations for the prevention and disallowance of irregular, unnecessary, excessive, extravagant, or unconscionable expenditures, or uses of government funds and properties. *1987 Constitution, Art. IX-D, Sec. 2(2).*

In pursuit of such powers, the COA promulgated rules which require government agencies including local governments to submit contracts to the COA for its review. One of the functions entrusted to the COA under the Government Auditing Code is to review and evaluate contracts, and inspect and appraise infrastructure projects. *Presidential Decree No. 1445, Sec. 18 (4); Executive Order No. 292, s. 1987, Book V, Title I, Subtitle B, Chap. 3, Sec. 7(6).* Furthermore, in the course of its inspection, the COA is empowered to require submission of the original or certified true copy of a contract, deed, or other relevant and supporting documents under which any collection of, or payment from, government funds may be made. *Presidential Decree No. 1445, Sec. 39; Executive Order No. 292, s. 1987, Book V, Title I, Subtitle B, Chap. 4, Sec. 23.*

This review power of the COA becomes more significant if one considers the adjudicating power of the COA to decide and settle money claims filed by any private contracting party against the government. In other words, a favorable review by the COA serves as an assurance that the contract has substantially complied with all the substantial and procedural requirements prescribed by existing laws and regulations and, therefore, its validity, insofar as the COA is concerned, should not be a contentious issue in any prosecution of money claim arising from the contract.

Thus, upon review of the contract, the auditor makes of record his evaluation and recommendations. His evaluation would note the defects and/or deficiencies found whether as to substance or form. He then submits his recommendation which usually consist of proposed corrective measures in order to remedy or minimize any defects found. If, however, in his judgment, the defects are so fatal as to render the contract void, then the auditor may strike down the contract as void and a complete nullity, hence, inexistent and utterly bereft of any legal force and effect. *Fernandez, Jr., Treatise on Government Contracts (1996) at 55.*

(e) ***Presidential Approval***

Finally, under a memorandum issued by the President on 25 August 1998, all contracts in the amount of fifty million pesos and above to be entered into by all departments, bureaus, offices, agencies of the government including government owned and/or controlled corporation and their subsidiaries must first be submitted to the Office of the President for approval. A subsequent memorandum dated 25 January 1999 expressly makes the requirement applicable to local government contracts.

3. Terms of Contract Not Grossly Disadvantageous to Government

Under the Anti-Graft and Corrupt Practices Act, the act of entering into any contract or transaction which is manifestly and grossly disadvantageous to the government is declared a corrupt practice and therefore illegal *per se*. *Republic Act No. 3019, Sec. 3 (g).* A government contract with terms grossly disadvantageous to the government is void for being contrary to law.

However, the charge that a contract is manifestly and grossly disadvantageous to the government is not easily proved. Public officials enjoy the presumption of regularity in the performance of public duties, and so long as it is shown that the terms of the contract were agreed after a thorough study of the facts by the public official concerned, no finding of gross and manifest advantage will be made on the ground alone that the private party stands to profit from the transaction. Thus, the Supreme Court, in the case of *Tatad vs. Garcia*, ruled in favor of the validity of the "Revised and Restated Agreement to Build, Lease and Transfer a Light Rail Transit System for EDSA" dated April 22, 1992, and the "Supplemental Agreement to the 22 April 1992 Revised and Restated Agreement To Build, Lease and Transfer a Light Rail Transit System for EDSA" dated May 6, 1993 after considering that:

> The terms of the agreements were arrived at after a painstaking study by DOTC. The determination by the proper administrative agencies and officials who have acquired expertise, specialized skills and knowledge in the performance of their functions should be accorded respect, absent any showing of grave abuse of discretion (Felipe Ysmael, Jr. & Co. v Deputy Executive Secretary, 190 SCRA 673 [1990]; Board of Medical Education v. Alfonso, 176 SCRA 304 [1989]).
>
> Government officials are presumed to perform their functions with regularity and strong evidence is necessary to rebut this presumption. Petitioners have not presented evidence on the reasonable rentals to be paid by the parties to each other. The matter of valuation is an esoteric field which is better left to the experts and which this Court is not eager to undertake.
>
> That the grantee of a government contract will profit therefrom and to that extent the government is deprived of the profits if it engages in the business itself, is not worthy of being raised as an issue. In all cases where a party enters into a contract with the government, he does so, not out of charity and not to lose money, but to gain pecuniarily.

Tatad vs. Garcia, G.R. No. 114222 (April 6, 1995).

4. Capacity of Private Contracting Party

In general, any person, be it an individual or corporation, not suffering from any legal disability by reason of age, insanity or civil interdiction, has the capacity to contract with local governments. Certain persons, however, cannot enter into joint ventures with local governments by reason of their position as, or their association with, public officials.

Certain statutory restrictions which seek to strengthen the accountability of public officials also inhibit them from acquiring or holding any prohibited interest in government contracts. Section 7(a), of Republic Act No. 6713, otherwise known as the "Code of Conduct and Ethical Standards for Public Officials and Employees", prohibits public officials and employees from directly or indirectly having any financial or material interest in any transaction which requires the approval of their office. A financial or material interest is defined by Section 1(a), Rule X of the implementing rules and regulations of R.A. 6713 as a pecuniary or proprietary interest by which a person will gain or lose something. Furthermore, under the Anti-Graft and Corrupt Practices Act, the act of having, directly or indirectly, a financial or pecuniary interest in any contract or transaction in which the public officer is prohibited by the Constitution or by any law from having any interest is likewise declared a corrupt practice and therefore illegal per se. *Republic Act No. 3019, Section 3(h).*

Moreover, Section 89 of the LGC declares it unlawful for any local government official or employee from engaging in any business transaction (i) with the local government unit in which he is an official or employee or over which he has the power of supervision, or (ii) with any of its authorized boards, officials, agents, or attorneys, whereby money is to be paid, or property or any other thing of value is to be transferred, directly or indirectly, out of the resources of the local government unit to such person or firm. Specifically, local public officials are prohibited from engaging in the following activities:

(i) holding such interests in any cockpit or other games licensed by a government unit;

(ii) purchasing any real estate or other property forfeited in favor of such local government unit for unpaid taxes or assessment, or by virtue of a legal process at the instance of the said local government unit;

(iii) being a surety for any person contracting or doing business with the local government unit for which a surety is required; and

(iv) possessing or using any public property of the local government unit for private purposes.

Violation of these provisions will subject the local official and any person or persons dealing with him to criminal liability. *LGC, Sec. 514.* More importantly, there is a risk that the contract will be considered void for being contrary to law. Article 1409 of the Civil Code declares as inexistent and void from the beginning any contract whose cause, object or purpose is contrary to law, morals, good customs, public order or public policy.

It must be noted that there exists a divergence of views on the effect of such prohibited interests to the validity of the contract. It has been opined by some that the above prohibited acts do not actually render the contract null and void. Since the evident intent of the above prohibitions is to prevent public officials from taking advantage of their positions to the detriment of the government and the public in general, then these prohibitions are actually directed to the public official concerned and not to the contract. As opined by the Secretary of Justice, such contracts will only be held void if the public official entering into these contracts is found later on to be a controlling stockholder or officer who is directly involved in the management of such enterprise. However, if such official is merely a stockholder with no opportunity to direct or control the affairs of the corporation, then contract shall be held valid though such official may be held criminally or administratively liable. The conservative view, on the other hand, holds that mere presence of such prohibited interest has the effect of immediately nullifying the contract. Such view, considers the mere presence of such prohibited interest as offensive to public policy.

C. Restrictions Arising from the Special Nature of a Joint Venture Contract

1. Public Bidding

It is a settled rule in this jurisdiction that contracts entered into by government without public bidding, *when such is required by law,* is void. In various cases, our Supreme Court has considered laws requiring public bidding as impressed with public policy and therefore of obligatory character. This policy is borne out of the recognized benefits of public bidding. Thus:

i. It allows the government to secure the lowest possible price for the project. *Caltex Philippines, Inc. vs. Delgado Brothers, Inc., G.R. No. L-5439 (December 29, 1954).*

ii. It curtails favoritism, fraud and corruption in the award of the contract, which is always a danger if the power to select prospective contractors were left to the unbridled discretion of government officials. *Fernandez, Jr., A Treatise on Government Contracts, (1996) at 64.*

iii. It avoids or precludes suspicion of anomalies in the execution or even renewal of the contract. *Matute vs. Hernandez, G.R. No. 46028 (August 8, 1938).*

iv. It places all prospective bidders on equal footing so as to afford them equal opportunities in securing the awards of public contracts. *San Diego vs. Municipality of Naujan, G.R. No. L-9920 (February 29, 1960); Malaga vs. Penachos, G.R. No. 86695 (September 3, 1992).*

Not all contracts, however, are subject to bidding. Certainly, there is no such express legal requirement for joint ventures. However, because government joint ventures almost always have the construction and operation of infrastructure facilities as their object or subject matter, doubts are raised as to the characterization of a joint venture as a contract. The issue is whether a joint venture for a development project should be considered as a build-operate-and-transfer (BOT) contract or any of its variants, or at the very least, a "contract for infrastructure projects." A BOT contract and a contract for infrastructure projects are subject to bidding under separate laws.

(a) ***BOT and Similar Contracts***

In Opinion No. 79 dated June 2, 1994, the DOJ upheld the position taken by the Office of the Government Corporate Counsel ("OGCC") in Opinion No. 224 dated November 8, 1993 (the "OGCC Opinion") that the PNCC may undertake the construction and operation of toll facilities pursuant to its franchise in joint venture with private companies without the necessity of public bidding. The OGCC, whose opinion was relied upon by the DOJ, reasoned out its conclusion by first tracing the authority of PNCC to enter into joint ventures with local or foreign entities in the construction and development of the expressways. It said:

> We believe that PNCC may enter into joint venture agreements or "partnership" with local or foreign entities in the construction and development of the desired Expressways. This is recognized in the PNCC franchise as reflected in the whereas clause of P.D. No. 1113 which states that in its undertaking, PNCC may have to "tap private resources and enterprises which will at the same time allow the government to redirect its own resources to other infrastructure projects" (3rd Whereas Clause, P.D. 1113), and joint venture scheme is one of the means of effectively tapping private resources and enterprises.

Furthermore, the authority of PNCC, like other government corporations to enter into joint venture agreements with private entities is recognized under Memorandum Order No. 226 dated November 28, 1989, which provides for guidelines governing investments by government corporations in joint venture agreements with private entities.

Having settled the authority of PNCC to enter into joint venture agreements, the OGCC then looked into the nature of joint ventures. It characterized joint ventures as akin to partnerships in the conclusion of which the personal attributes of the parties are paramount. The OGCC thus concluded that the choice of prospective partners in a joint venture agreement cannot, because of the principle of *delectus personae,* be the subject of public bidding. The OGCC stated:

> We agree with you that the choice of prospective "partners" largely depend on the consent of PNCC under the principle of *delectus personae* where in partnership relations, no one can become a member of the partnership association without the consent of all the partners (Article 1804, Civil Code). The principle, however, can only be applied by analogy as the contemplated joint venture agreements do not exactly qualify as partnerships under the Civil Code.

One issue that was not addressed in either the OGCC Opinion or the DOJ Opinion is how the joint venture agreement contemplated therein would differ from BOT or any of its variants which are governed by Republic Act No. 6957, as amended by Republic Act No. 7718 (the "BOT Law"). The distinction is important for purposes of taking out joint venture agreements from the coverage of the BOT Law which imposes the requirement of public bidding.

The BOT arrangement and other schemes recognized under the BOT Law are defined therein as follows:

i. Build-and-transfer (BT) – A contractual arrangement whereby the project proponent undertakes the financing and construction of a given infrastructure or development facility and after its completion turns it over to the government agency or local government unit concerned, which shall pay the proponent on an agreed schedule its total investment expended on the project, plus a reasonable rate of return thereon. This arrangement may be employed in the construction of any infrastructure or development projects, including critical facilities which, for security or strategic reasons, must be operated directly by the government.

ii. Build-lease-and-transfer (BLT) – A contractual arrangement whereby a project proponent is authorized to finance and construct an infrastructure or development facility and upon its completion turns it over to the government agency or local government unit concerned on a lease arrangement for a fixed period, after which ownership of the facility is automatically transferred to the government agency or local government unit concerned.

iii. Build-operate-and-transfer (BOT) - A contractual arrangement whereby the project proponent undertakes the construction, including financing, of a given infrastructure facility, and the operation and maintenance thereof. The project proponent operates the facility over a fixed term during which it is allowed to charge facility users appropriate tolls, fees, rentals, and charges not exceeding those proposed in its bid or as negotiated and incorporated in the contract to enable the project proponent to recover its investment, and operating and maintenance expenses in the project. The project proponent transfers the facility to the government agency or local government unit concerned at the end of the fixed term that shall not exceed fifty (50) years. This shall include a supply-and-operate situation which is a contractual arrangement whereby the supplier of equipment and machinery for a given infrastructure facility, if the interest of the government so requires, operates the facility providing in the process technology transfer and training to Filipino nationals.

iv. Build-own-and-operate (BOO) – A contractual arrangement whereby a project proponent is authorized to finance, construct, own, operate and maintain an infrastructure or development facility from which the proponent is allowed to recover its total investment, operating and maintenance costs plus a reasonable return thereon by collecting tolls, fees, rentals or other charges from facility users. Under this project, the proponent who owns the assets of the facility may assign its operation and maintenance to a facility operator.

v. Build-transfer-and-operate (BTO) – A contractual arrangement whereby the public sector contracts out the building of an infrastructure facility to a private entity such that the contractor builds the facility on a turn-key basis, assuming cost overruns, delays, and specified performance risks. Once the facility is commissioned satisfactorily, title is trasnferred to the implementing agency. The private entity, however, operates the facility on behalf of the implementing agency under an agreement.

vi. Contract-add-and-operate (CAO) – A contractual arrangement whereby the project proponent adds to an existing infrastructure facility which it is renting from the Government and operates the expanded project over an agreed franchise period. There may or may not be a transfer arrangement with regard to the added facility provided by the project proponent.

vii. Develop-operate-and-transfer (DOT) – A contractual arrangement whereby favorable conditions external to a new infrastructure project which is to be built by a private project proponent are integrated into the arrangement by giving that entity the right to develop adjoining property, and thus, enjoy some of the benefits the investment creates such as higher property or rent values.

viii. Rehabilitate-operate-and-transfer (ROT) – A contractual arrangement whereby an existing facility is turned over to the private sector to refurbish, operate and maintain for a franchise period, at the expiry of which the legal title to the facility is turned over to the government. The term is also used to describe the purchase of an existing facility from abroad, importing, refurbishing, erecting and consuming it within the host country.

ix. Rehabilitate-own-and-operate (ROO) – A contractual arrangement whereby an existing facility is turned over to the private sector to refurbish and operate with no time limitation imposed on ownership. As long as the operator is not in violation of its franchise, it can continue to operate the facility in perpetuity.

An examination of the contractual arrangements referred to in the BOT law reveals two distinguishing characteristics. First, in all these arrangements, the construction and/or operation of a project, prior to its turnover to the concerned government agency, is a *wholly private affair*. Under the law, the participation of the government agencies concerned in the construction and/or operation of a project under these arrangements goes no farther than ensuring that design and performance specifications initially agreed upon are complied with. It is true that in most BOT projects, the government agencies assume certain undertakings to support the project, such as the delivery of the site or rights of way or other materials (*e.g.* steam or fuel or water for power projects), but these undertakings are not such as would influence private sector management of the project. These undertakings do not put into test the very rationale of the OGCC in exempting joint ventures from public bidding, which is the compatibility of the joint venture partners, or their trust or confidence on each other, that allows them to successfully undertake a project jointly. It would seem, therefore, that to differentiate a joint venture agreement from the contractual arrangements under the BOT Law, it is necessary to grant the government agency the right to participate, at the very least, in the decision-making on all aspects of the construction and/or operation of the project.

Second, under the contractual arrangements contemplated by the BOT Law, the project proponent recovers its investments from either payments made by the government agencies concerned as in a BT or a BLT arrangement or from tolls, fees or charges that it is allowed to collect from facility users as in a BOT or a BOO arrangement. In an ordinary joint venture agreement, however, the partners contribute capital and/or labor and share in the distribution of profits.

Substantial distinctions exist between a joint venture contract and a BOT and its variants. These distinctions provide basis for the view that the BOT Law, including the requirement of public bidding, does not apply to a joint venture.

(b) ***Contracts for Infrastructure Projects***

Executive Order No. 292, otherwise known as the Administrative Code of 1987, states that "[a]s a general rule, contracts for infrastructure projects shall be awarded after open public bidding to bidders who submit the lowest responsive/evaluated bids." *Executive Order 292, Book III, Chapter 13, Section 62.* The procedure for bidding infrastructure projects is set out in more detail in Presidential Decree No. 1594 "prescribing policies, guidelines, rules and regulations for infrastructure contracts."

The requirement of bidding for contracts for infrastructure projects is found in the chapter of the Administrative Code that appears addressed solely to national government agencies. In addition, the LGC has expressly repealed PD 1594 "insofar as it governs locally funded projects." Nonetheless, there is basis for the view that the award of local infrastructure projects is still subject to public bidding.

Section 17 (d) of the Local Government Code mandates that the designs, plans, specifications, testing of materials, and the procurement of equipment and materials for the provision of basic services shall be undertaken by the local government unit concerned based on "national policies, standards and guidelines." Thus, the COA, in promulgating the rules and regulations on the supply and property management of local governments, adopts as a general policy the acquisition of supplies or property through public bidding. Acquisition through public bidding applies to all supplies and materials including those acquired for the prosecution of infrastructure projects whether funded locally or nationally, or through foreign assistance or local donations. *COA Circular No. 92-386, sections 6 and 27.* The words "supplies" and "property" are further defined to include "everything, except real property, which may be needed in the transaction of public business or in the pursuit of any undertaking, project, or activity, whether in the nature of equipment, furniture, stationery, materials for construction or personal property of any sort, including non-personal or contractual services such as the repair and maintenance of equipment and furniture, as well as trucking, hauling, janitorial, security and related services."

The requirement of public bidding for local infrastructure projects is also implied from Section 37 of the LGC. Section 37 mandates the formation of prequalification, bids and awards committee in every province, city, and municipality which shall have the primary responsibility of conducting the "prequalification of contractors, bidding, evaluation of bids, and the recommendation of awards concerning local infrastructure projects."

The question is whether a joint venture for the construction and operation of an infrastructure facility, such as waterworks systems, etc., is subject to bidding under the pertinent provisions of the LGC and the rules of the COA.

There is basis for the view that a joint venture, even though formed for the purpose of constructing and operating an infrastructure facility, is not an infrastructure contract as such term is used in the LGC and the rules of the COA. A joint venture agreement differs from an ordinary infrastructure contract. In an ordinary contract for infrastructure projects, the government contracts the services of a private contractor to construct the project. As owner of the project, the government retains absolute control over the project with the power to terminate the project at will, *Civil Code, Art. 1725*, which power may be exercised when disagreements arise as to the details of the execution of the contract. Again, joint decision-making, which appear to be the essence of a partnership, is absent. To summarize, there is basis for the view that no bidding is required for a joint venture contract. There is no law requiring the bidding of such type of contract. A joint venture contract does not qualify as a BOT or a contract for infrastructure development and is therefore not subject to the requirements (including bidding) applicable to these two types of contract. As will be shown in Chapter IV of this paper, however, specific undertakings assumed by the local governments under the joint venture contract may require bidding.

Also, while no express provision of law requires bidding of joint venture contracts, some national government agencies and local government units have nonetheless gone through public bidding in the choice of their joint venture partners in the interest of transparency, a public policy embodied in administrative issuances.

Memorandum Circular No. 90-104 was issued by the DILG to prescribe policies and guidelines for the privatization of the delivery of basic services and the management of economic enterprises owned by local government units. One of the guidelines prescribed in the memorandum circular is transparency in all privatization transactions. Thus, even in the absence of a clear and express requirement for public bidding, local governments may resort to bidding in the interest of transparency.

Certain private sector participants and government agencies have already taken the lead on this. The private proponent for the Subic Clark Expressways expressed its preference for bidding out the joint venture contract to achieve a favorable public perception or transparency. DOJ Opinion No. 79, series of 1994. The Baguio Water District had bidded out the joint venture contract for the construction, rehabilitation and operation of its waterworks system.

2. **Approvals Particularly Applicable to Joint Ventures**

(a) **Approvals for BOT Contracts Not Applicable**

Certain types of local government contracts are subject to additional review and approval requirements. Of particular concern, mainly because of its similarity to a joint venture contract, is the BOT agreement or its variants.

Under Section 302 of the LGC, local government units may enter into contracts with any duly prequalified individual contractor, for the financing, construction, operation, and maintenance of any financially viable infrastructure facilities under BOT and similar arrangements, subject to the applicable provisions of the BOT Law, its implementing rules and regulations (the "BOT Rules") and the provisions of the LGC.

Projects proposed to be implemented by the local government units under the BOT scheme or any of its variants must be submitted to and confirmed by the following:

(i) For projects costing up to P20 million, the municipal development council;

(ii) For projects costing above P20 million up to P50 million, the provincial development council;

(iii) For those costing up to P50 million, the city development council;

(iv) For those costing above P50 million up to P200 million, the regional development council, or in the case of Metro Manila projects, the Metro Manila Development Council (MMDC);

(v) For those costing above P200 million, by the Investment Coordination Committee (ICC) of the National Economic and Development Authority Board. *BOT Rules, Sec. 2.7(b), BOT Law, Sec. 4.*

The above requisite approvals must be applied for and secured by the concerned local government unit prior to the call for bids for the project. *BOT Rules, Sec. 2.3.*

Furthermore, local government units must, prior to the schedule of submission of bids, submit the draft contract to the ICC for clearance on a non-objection basis. *BOT Rules, Sec. 2.9.* If the draft contract includes government undertakings within the scope of an earlier ICC approval, the submission will only be for the information of the ICC. *Id.* However, should it include additional government undertakings over and above the original scope, then the draft contract will be reviewed by the ICC. *Id.* Failure on the part of the local government unit to submit the contract, or if submitted, to comply with the requirements of the ICC shall render the award or the contract invalid. *Id.*

Projects undertaken under a BOO scheme or through other similar arrangements not specifically defined in the BOT Law and Rules require the approval of the President of the Philippines.

Within the local government units themselves, local development projects to be implemented under the BOT scheme and its variants are subject to a unique approval process. Under Section 302 of the LGC, a local government unit intending to implement a BOT project must take the following steps:

(i) The mayor or governor shall send a formal written instruction to the local engineer to prepare plans and specifications for the proposed BOT project;

(ii) The plans and specifications are then submitted to the *sanggunian* for its approval;

(iii) The project is then bidded out and awarded to the lowest complying bidder after publication of the plans and specifications for at least two (2) weeks in a newspaper of general circulation in the locality; and finally,

(iv) BOT Contracts are reviewed by the local legal officer to determine their legality, validity, enforceability, and even correctness of form.

A provincial attorney has already opined that a joint venture is but a variant of a BOT contract. *Reports on the Provincial Public Utilities Department-Provincial Electric System Province of Bohol (June 1999) at 9 citing the legal opinion of the Provincial Attorney of Bohol dated August 7, 1998.* As has been discussed elsewhere, however, a substantial distinction exists between a BOT and a joint venture contract that would make the approval requirements imposed on BOT contracts inapplicable to joint venture agreements.

3. COP Approval

Joint venture contracts require the approval of the Committee on Privatization (COP) created under Proclamation No. 50, series of 1986. Under Executive Order No. 12 issued on August 14, 1998 by President Joseph Ejercito Estrada, any disposition related activities (*i. e.*, sale, lease, management contract, joint venture schemes, BOT and its variants) by national government agencies, government owned and controlled corporation or local government units shall not be undertaken without the prior approval of the COP in accordance with the disposition guidelines provided by the COP and other existing rules and regulations on disposition of assets.

However, under Section 4 of the Rules and Regulations issued by the COP last January 13, 1999, privatization transactions of local government units are specifically exempted from the requirement of COP approval. Nevertheless, they continue to be governed by the disposition/privatization guidelines of the COP and other applicable laws, rules and regulations on privatization or asset disposition. *Implementing Rules and Regulations of Executive Order No. 12, Secs. 1 and 4 (January 13, 1999).*

4. **Other Approvals**

Certain specific undertakings assumed by local governments under joint venture contracts may attract other approval requirements. These approvals will be discussed in more detail in Chapter IV of this paper.

Summary of Requirements and Restrictions

There are three types of requirements and restrictions applicable to local government joint ventures, namely: (i) those relating to the joint venture project; (ii) those generally applicable to local government contracts; and (iii) those arising from the special nature of a joint venture contract. The first category of restrictions relates to the object of the joint venture, i.e., the specific undertaking that is the subject matter of the contract. In general, such undertaking should be within the express or implied power of the local government unit concerned. In addition, the joint venture may operate only within the territorial boundaries of the local government unit concerned, unless it has grouped together with other local government units. The project must also be included in the local government's development plan.

Like any local government contract, a joint venture must be executed by the local chief executive with the prior authorization of the sanggunian concerned. The requirement of review by a higher sanggunian or by other national government agencies like the COA should likewise be observed. Furthermore, pursuant to the memorandum issued by the President, where the contract involves an amount in excess of fifty million pesos, the contract must be submitted to the President for approval. Other principles generally applicable to government contracts must likewise be observed. These include the requirement that the terms of the contract should not be grossly disadvantageous to the government, and that the private contracting party should not be subject to any special disqualifications.

Finally, certain requirements and restrictions may arise owing to the special nature of a joint venture contract. Public bidding is not required for the joint venture per se, although certain specific undertakings assumed by the local governments may, as will be shown in Chapter IV, make bidding applicable. These specific undertakings may also attract other approval requirements, apart from the approval of the COP required for joint venture contracts.

IV. Specific Undertakings of Local Governments

There is no single law that lays down the rules governing the use of joint venture as a transaction structure for infrastructure projects. This circumstance has discouraged some private investors from packaging their transactions with government as joint ventures; they fear that the lack of set rules will open their projects with government to protracted legal challenge. Still other investors have seen this circumstance as affording the government the flexibility to package their transactions outside the ambit of the BOT Law, the approval and evaluation process under which has proved to be an interminably long one. Relying on general principles of contract law and armed with nothing but an opinion from the DOJ on the nature of a joint venture, some private sector participants and government infrastructure agencies have concluded joint ventures for infrastructure projects, sidestepping bidding and other approval requirements under the BOT Law. There may be legal basis for the view that a joint venture is not a variant of the BOT contract, and therefore, not governed by the BOT Law. This does not necessarily mean, however, that bidding for the project can be dispensed with entirely, or that less approvals and consents would be required than when the project is governed by the BOT Law. The specific undertakings assumed by the government under the joint venture contract have to be carefully examined and properly characterized to ascertain whether bidding is still necessary. These specific undertakings will also dictate the approvals that must be obtained for the project.

The use of joint venture as a transaction structure also offers some practical advantage. The lack of set rules governing joint ventures allows the parties the flexibility to divide up responsibilities for the project, with the government assuming responsibilities that it can execute through financing under concessional rates and with tax and other fiscal incentives. For private investors, the government's equity interest in the venture may translate to a firm commitment not to make adverse change in laws and rules, but it may also pave the way for greater government intervention in the project.

This part of the paper identifies the specific undertakings usually assumed by the government in infrastructure projects and sets out the approvals required for those specific undertakings, and the advantages and disadvantages of the government assuming such undertakings.

a. *Equity Investments*

Most infrastructure joint ventures that have been entered into by the government are structured as equity joint ventures, with the parties agreeing to incorporate a joint venture corporation and to contribute a specified sum to the capital stock. This choice of structure may be due to the familiarity of both government and the private sector to the corporation as a form of business organization, as well as to the advantage that the limited liability feature of a corporation offers to investors.

1. Limitations on Authority to Incorporate

However, based on two opinions issued by the DILG, local governments cannot form corporations whether through an ordinance or under the Corporation Code.

Under DILG Opinion No. 97-1995, the department has ruled that local governments are not empowered to create private corporations or development enterprises by ordinance. Under the Constitution, only Congress may create government-owned or controlled corporations by special charters in the interest of common good and subject to the test of economic viability. *1987 Constitution, Art. XII, Sec. 16.* Since local governments cannot exercise a power expressly reserved by the Constitution to Congress, they cannot form private corporations through an ordinance.

Furthermore, in a later opinion, DILG has ruled that local governments cannot incorporate a private corporation under the Corporation Code of the Philippines. *DILG Opinion 80, s. 1997.* It cites as reason Section 10 of the Corporation Code which only qualifies natural persons to incorporate a private corporation. A local government being an artificial person is legally disqualified to become an incorporator and such disqualification extends to its local officials who merely act as agents of the local government.

These two DILG opinions, however, do not absolutely prevent the local governments from structuring their joint ventures with the private sector as equity joint ventures. While local governments may not incorporate a corporation either by special ordinance or by general law, they may invest funds in existing corporations. The authority of local governments to invest funds in another corporation is acknowledged by the DILG in its Opinion No. 80, series of 1997, thus:

> A local government unit like that of a province is empowered under this Code to exercise such other powers as are granted to corporations, subject to limitations provided in this Code and other laws (Sec. 22, RA 7160). This is in consonance with the principle of law that local government units (LGUs) shall be given the full autonomy to enjoy in the exercise of their proprietary functions, including the management of their economic enterprises, but still subject to the same limitations setforth above. Among the powers granted to corporations are provided for under Sections 36-45 of the Corporation Code (B.P. Blg. 68) in that the same may invest corporate funds in another corporation or business or for any other purpose and to exercise such other powers as may be essential or necessary to carry out its purpose or purposes as stated in its articles of incorporation.

2. **Limitations on Disbursement Authority**

If the local government commits to make a financial investment in the joint venture corporation, the joint venture contract must, as a general rule, be covered by a certificate of availability of funds; otherwise, the contract will be void. Under the LGC, local governments cannot disburse funds except in pursuance of an appropriation made by law. To enforce this restriction on the local government's disbursement power, the COA requires that the certificate of availability of funds shall be attached and made an integral part of every government contract, except for the following: (i) contracts for personal service; (ii) contracts for the procurement of supplies for current consumption or to be carried in stock not exceeding the estimated consumption for three months, or (iii) banking transactions of government-owned or controlled banks. This certificate shall be executed by the proper accounting official of the agency concerned and shall attest to the officer entering into the obligation that (i) funds have been duly appropriated for the purpose and (ii) the amount necessary to cover the proposed contract for the current fiscal (calendar) year is available for expenditure on account thereof. The certificate must also be signed and verified by the auditor. *Presidential Decree 1445, Sec. 86; Executive Order No. 292, Book V, Title I, Subtitle B, Chap. 7, Sec. 47.* Consequently, any contract entered into by the government without the requisite certificate of availability of funds shall be considered void, and the officer or officers entering into the contract shall be liable to the government or the other contracting party for any consequent damage arising from the contract. *Presidential Decree 1445, section 87.*

It must be noted, however, that the appropriation for the disbursement and the certificate of availability of funds are necessary only if the financial obligation of the local governments are immediately demandable under the contract or must be paid in the current year. In one case, the Supreme Court ruled that a contract for the purchase of electricity for a period of ten years need not have an appropriation nor a certificate of availability covering the whole ten year period. Since under the terms of the contract, the municipality was only bound to pay monthly, an appropriation or certificate of availability of funds covering estimated consumption for six months is sufficient. *Imus Electricity Co. vs. Mun. of Imus,* 58 Phil. 316 (1934).

Since the private sector is not as interested in the equity contribution of the government as it is in other undertakings of the government, the private sector has in some transactions advanced the money for the government's equity contribution. This device is meant to allow the government to finance its equity contribution through earnings from the project, thereby dispensing with the requirement of certificate of availability of funds.

3. **Post-Audit Requirement**

Depending on the percentage share of the local government, the joint venture may become subject to the post-audit jurisdiction of the COA. The Constitution authorizes the COA to review on a post-audit basis government owned or controlled corporations without original charters and their subsidiaries. A government-owned or controlled corporation, as defined under the Administrative Code, refers to any agency organized as a stock or non-stock corporation, vested with functions relating to public needs whether governmental or proprietary in nature, and owned by the Government directly or indirectly through its instrumentalities either wholly, or, where applicable as in the case of stock corporations, to the extent of at least 51% of its capital stock. *Executive Order 292, Sec. 2.*

4. **Government Intervention**

Apart from the potential COA audit, the government entity investing in the joint venture may intervene in the management of the project. The extent of the intervention will depend on the management provisions of the joint venture contract and the articles of incorporation, in case of an equity joint venture. While it is usual for the government entity to take a minority interest in the joint venture, that minority interest still provides the government an avenue to take part in decision-making, allowing it to balance commercial concerns with public interests.

b. ***Provision of Land and Other Properties***

Perhaps one valuable asset which local governments can readily contribute to the joint venture is land. In most government contracts, investors usually require from the government party the obligation to provide land. Aside from being the owner of valuable real properties, local governments may use its power of expropriation to acquire lands for use of the joint venture.

The local government may contribute ownership of land to the joint venture either in the joint venture contract itself or in a separate contract of sale to the joint venture entity. A joint venture contract where local government units undertake to contribute land or other properties constitutes, for all purpose, a disposal of government properties.

A joint venture is a form of partnership that, by law, has a juridical personality, and is considered an entity distinct and separate from the partners who compose it. *Civil Code, Art. 1768.* Once property that a partner has agreed to contribute is delivered to the partnership by any of the modes of delivery recognized under the law, ownership of that property passes from the partner to the partnership. Or at the very least, part ownership will pass to the joint venture partners of the local governments. Under Article 1811 of the Civil Code, a partner is co-owner with his partner of specific partnership property. Thus, whether the contribution of land or other properties is made in the joint venture contract itself or in a separate agreement, the pertinent rules on disposal must be complied with.

1. **Sale of Real Properties**

Under Section 197 of COA Circular 92-386, real estate and their improvement owned by local government units may be sold to other government or private entity under sealed bids or by negotiation if sealed bid has failed at a price determined by the Committee on Awards. The contract or conveyance shall be executed by the local chief executive in behalf of the local government unit concerned and shall be approved by the local *sanggunian*. *COA Circular 92-386, Sec. 197.* Disposal shall also be subject to the approval of the COA regardless of the value of the property to be disposed. *Id; LGC, Sec. 380.* Expenses relative to the registration and transfer of ownership from the local government to the vendee must likewise be borne by the vendee. *Id.*

2. Lease of Real Properties

Local governments may also provide land through a lease to the joint venture. In this respect, Section 198 of COA Circular 92-386 states that idle lands, buildings or other physical structures of local governments may be leased to other government or private entity thru sealed bids or by negotiation if sealed bids have failed. Rental rates must be determined by the Committee on Awards and approved by the *sanggunian*. *COA Circular 92-386, section 198.* Furthermore, the contract of lease must contain the following provisions:

a. Lessee shall be required to deposit an amount equivalent to two months rental or P30,000.00 pesos whichever is higher to answer for damages resulting from improper use of the leased property and an advance of one month rental;

b. Lessee shall promptly pay the monthly billings for facilities like electric, water and telephone during the period of the lease, and shall be held answerable in case of disconnection of said facilities due to his failure to pay the bills;

c. Lessee shall surrender the building/space upon expiration of the lease contract and respond for damages which the local government unit may suffer for his failure to surrender the same;

d. Lessee shall comply faithfully with the terms and conditions of the agreement;

e. In the event the building/space is deserted by the lessee before the expiration of the lease without justifiable cause, the local government unit shall reserve the right to enter and relet the same and receive the rentals corresponding to the unexpired period of the lease; and

f. The local government unit shall reserve the right to terminate the lease contract for failure or refusal of the lessee to pay the rentals agreed upon during the period stipulated in the lease contract or for violation of the conditions of the contract by the lessee. *Id.*

3. Sale of Personal Properties

Local governments may also contribute the ownership of personal or movable properties used in existing infrastructure facilities that will be the subject of the joint venture agreement. Both the LGC and the COA require that movable assets of local governments that have become unserviceable or no longer needed be disposed of in public auction. *LGC, Secs. 356 and 379; COA Circular No. 92-386, Sec. 165.* The COA, however, may sanction the sale of unserviceable properties by negotiation due to "justifiable reasons." *COA Circular No. 92-386, Sec. 166.*

4. Lease of Equipment

Lease of equipment owned by local governments is also subject to the requirement of bidding. Under Section 199 of COA Circular 92-386, idle equipment of the local governments may be leased to a government or private entity thru sealed bids or by negotiation if sealed bids have failed. The contract of lease must also contain the following provisions:

a. lease shall be on fully maintained basis without fuel and operator;

b. lease contracts with terms longer than one month shall be supported by a surety bond to guarantee the replacement cost of the property in case of loss, cost of repair that are not due to normal wear and tear, replacement cost of missing parts, tools, attachments and accessories originally issued with the property;

c. rental must be paid in advance or the lessee shall put up a domestic letter of credit to guarantee the payment of the rental for the period of lease;

d. mobilization cost from the lessor's yard to project site and the demobilization cost from project site to the lessor's yard shall be borne by the lessee;

e. lessee shall be liable for compensation and lawsuits, if any, arising from injury or damage caused to any person or property by reason of the use of the equipment during the period of the lease;

f. a daily basis lease shall correspond to eight hours use and any usage in excess of eight hours shall be considered overtime and corresponding additional rental shall be charged;

g. a monthly basis lease shall be understood to correspond to 160 hours use per month; and

h. a proportionate rental shall be collected on the actual operating hours in excess of the 160 days referred to above regardless of whether the property is in use or not. COA Circular 92-386, Sec. 199.

Rental rate must be determined by the Committee on Awards and approved by the sanggunian. Id. It may also be reduced as the efficiency of the equipment or machinery subject of the lease contract becomes lesser on account of age or obsolescence as long as such reduction (i) shall not be allowed during the first three years from acquisition date of the property and (ii) maximum discount shall not be less than 25% of the property's normal rental rate in accordance with the schedule prescribed under COA Circular 92-386. COA Circular 92-386, Sec. 200. However, rental rates of properties which have not undergone any rehabilitation and are more than seven years old shall be determined by the Committee on Awards and approved by the sanggunian. Id.

Furthermore, no agreement for lease of equipment shall be entered into without a certification from the general services officer, municipal or barangay treasurer, as the case may be, attesting that the property to be leased is not needed for any purpose by any department or office of the local government during the duration of the lease. COA Circular 92-386, Sec. 199.

Aside from being able to use, for the benefit of the joint venture, idle equipment already owned by the local government, such lease is likewise an indirect way of availing the tax exempt privileges granted to local governments. Under Section 382 of the LGC, local governments shall be exempt from the payment of duties and taxes for the importation of heavy equipment or machineries used for the construction, improvement, repair, and maintenance of roads, bridges and other infrastructure projects, as well as garbage trucks, fire trucks and other similar equipment as long as such equipment or machineries shall not be disposed of, either by public auction or negotiated sale, within five years from the importation thereof. Thus, local governments may import equipment to be used for infrastructure projects, avail of their tax privilege, and lease such equipment to the joint venture corporation.

Instead of contributing ownership of real or personal properties or leasing the same to the joint venture under a separate contract, local governments may contribute the use of such properties in exchange for a share in the equity of the joint venture. Since ownership of the property is not contributed to the joint venture, the rules governing disposition will not apply. Neither should the rules governing leases of government properties apply since the use is contributed not in the concept of lease, but in the concept of investment. Nevertheless, the bidding requirement imposed on disposition and lease of government property shows that bidding is the method of choice of the government of getting the best value for its property. Given this obvious policy consideration, whether bidding may be dispensed with when the use of property is disposed of for a share in the joint venture is at the very least an open issue.

c. ***Grant or Sharing of Franchise***

A number of infrastructure joint ventures that have been concluded by far involve a government party who is either a franchise holder or the grantor of a franchise. PNCC through its charter was granted by Congress the franchise to construct, operate and maintain the toll facilities covering the south and north luzon expressways, *Presidential Decree No. 1113, Sec. 1,* and, by virtue of its implied authority to enter into joint ventures, allow others to participate in such franchise. *DOJ Opinion No. 79, s. 1994.* On the other hand, the Subic Bay Metropolitan Authority as well as the Clark Development Corporation are granted the power to grant franchises for water and telecommunication services. *Republic Act No. 7227, Sec. 15; Executive Order No. 80; Presidential Decree No. 66, Sec. 4; Republic Act No. 7916, Secs. 12 and 13.* Both have entered into joint ventures for the provision of such services. Local water districts are also a favorite target for joint ventures because of their exclusive franchise to deliver water services within their respective districts.

Through these joint ventures, private investors are able to participate in the existing franchise of the government party or to acquire a public franchise from the government party who has franchise granting authority. The real attraction is the possibility of operating the service authorized under the franchise to the exclusion of other competitors. The franchise also partakes of the nature of a contract that fixes, so to speak, the rules of the business as between the government and the grantee.

In truth, however, there is no such thing as an exclusive franchise. The Constitution expressly prohibits the grant of a franchise that is exclusive in character. It also provides that a franchise may be granted only upon the condition that it shall be subject to amendment, alteration or repeal by Congress when the common good so requires. *1987 Constitution, Art. XII, Sec. 11.*

Notwithstanding the prohibition against exclusivity, franchise holders can take comfort that no unnecessary competition will be foisted upon them because of the due process clause of the Constitution. The Supreme Court has held that a franchise is guaranteed the due process protection of the Constitution, and consequently, a franchise can not be granted to another entity without the appropriate government body giving the franchise holder an opportunity to be heard and without sufficient proof that the franchise holder is incapable or unwilling to meet the demands of public service. *National Power Corporation, G.R. No. L-67143 (January 31, 1985).*

A joint venture with the government agency with the authority to grant the franchise gives greater assurance of exclusivity. Since the government agency as an investor in the joint venture would itself be concerned with the commercial viability of the business, it is less likely that such government agency will issue competing franchises. The equity interest of the government agency in the venture also gives reasonable assurance that it will not, by law or ordinance, change the terms of the franchise.

Considering the foregoing, it is expected that most joint ventures with local governments will be in areas where the local governments have an existing franchise or an exclusive franchising authority.

Local governments are granted by Congress both the franchise to operate public utilities and the power to grant franchises. By virtue of Section 16 of the LGC, Congress authorizes local governments to exercise such powers necessary and proper to provide for the health and safety, promote the prosperity, improve the morals, peace, good order, comfort, and convenience of the municipality and the inhabitants thereof. This general welfare clause has been held by the Supreme Court as sufficient basis to authorize the City of Davao to own and operate its own telephone system. *Philippine Long Distance Telephone Company vs. City of Davao,* G.R. No. L-23080 (October 30, 1965). Furthermore, Section 17 of the LGC, empowers local governments to exercise such powers and discharge such functions and responsibilities as are necessary, appropriate, or incidental to the efficient and effective delivery of certain basic services and facilities. These basic services include, among others, solid waste collection and disposal, maintenance of roads, bridges, water supply systems, and other infrastructure facilities. In addition, pursuant to their responsibility to deliver basic services, the *sanggunian pambayan* and *panglungsod* are likewise granted the legislative power (i) to regulate, construct, improve, repair and maintain streets, avenues, alleys, sidewalks, bridges, parks and other public places; establish bus and vehicle stops and terminals; (ii) to establish, operate, maintain and repair waterworks and sewerage systems; (iii) to regulate the placing, installation, repair and construction of all gas mains, electric, telegraph and telephone wires, conduits, meters and other apparatus; and (iv) provide for an efficient and effective solid waste and garbage collection and disposal system. *LGC, Secs. 447 (a) (5), 458 (a) (5), 468 (a) (4).* Local governments, therefore, may provide and operate these public utilities pursuant to the above provisions of the LGC.

Complementary to these powers is the legislative power expressly delegated to the *sangguniang bayan, sangguniang panglungsod* and *sangguniang panglalawigan* to grant franchises and enact ordinances authorizing the issuance of permits or licenses intended to promote the general welfare of the inhabitants of their respective local government units. *LGC, Secs. 447 (a) (3), 458 (a) (3), 468 (a) (3).*

While the authority of local governments to grant franchises is cast in such broad terms, the express and specific grant of franchising authority for certain specified services to certain national government agencies seem to negate local governments' franchising authority in these types of services. In fact, the authority to grant franchises for major utilities does not belong to local governments. Under Section 42 of Presidential Decree No. 269, the franchising power of municipal, city and provincial governments to grant franchises for the distribution of electric power plants is repealed and transferred to the National Electrification Administration (NEA). However, the *sanggunians* may still enact ordinances regulating the installation and maintenance of electric power lines or wires within its territorial jurisdiction. *Negros Oriental II Electric Cooperative, Inc. vs. Sangguniang Panlungsod of Dumaguete,* G.R. No. L-72492 (November 5, 1987). Under Republic Act No. 7925, otherwise known as the Public Telecommunications Policy Act of the Philippines, the power to grant franchises to operate a public telecommunications entity has now been reserved by Congress. Section 16 of said Act expressly states that no person shall commence or conduct the business of being a public telecommunications entity without first obtaining a franchise. A franchise is defined as a privilege conferred by Congress upon a telecommunications entity. *Republic Act 7925, Sec. 3.* On the other hand, a public telecommunications entity refers to any person, firm, partnership or corporation, government or private, engaged in the provision of telecommunications services to the public for compensation. *Id.*

Finally, Commonwealth Act No. 146, as amended, otherwise known as the Public Service Law, prohibits any person from operating a public utility within the Philippines without a certificate of public convenience. The function of granting certificates of public convenience for waterworks utilities devolves upon the National Water Resources Board.

While local governments have no authority to grant franchises for power, telecommunications or water utilities, they are expressly allowed to operate such utilities on their own or in joint venture with another entity. The joint venture who will own and operate the utilities, having as it does a personality separate and distinct from the local government party, must secure the necessary franchise from the appropriate government agency. It is worth noting that if a project is awarded to a private party under the BOT scheme, the grant of the franchise becomes a matter of course, unlike in a joint venture scheme.

d.. ***Securing Permits***

Another obligation commonly undertaken by local governments is to assist in securing the necessary national and local permits in behalf of the joint venture. Such obligation becomes significant if one considers the numerous permits a corporation must secure from both national and local governments to validly operate a business or undertake a major infrastructure project.

Under the LGC, chief executives of the municipality, city and province are empowered to issue licenses and permits pursuant to law or ordinance. *LGC, Secs. 444 (b)(3)(iv); 455 (b)(3)(iv), 465 (b)(3)(iv).* Pursuant to this power, local governments have required various permits ranging from the more common business permits or sanitary and plumbing permits to other consequential permits like the land use plan or the locational clearance. The right to issue other permits arises from laws or regulations which seek to devolve functions of national agencies to local governments. The National Building Code, for example, has granted the right to issue the permits required under such law to local governments. Hence, the issuance of building permits, certificates of occupancy, fire inspection certificates, demolition permits, sidewalk permits and electrical permits now rest with the local governments. On the other hand, the Rules on Occupational Safety has also devolved the regulation and inspection of work places to local governments. As of the present, the relevant permits required under these rules may be secured from local governments.

Permits from the national government may be more easily secured by or with the assistance of local governments. The Department of Environment and Natural Resources, for example, requires project proponents to secure an Environmental Compliance Certificate (ECC) prior to the operation of a project and to comply with every condition stated therein during the course of the project's implementation. The cooperation of local governments in conducting the necessary environmental studies or in monitoring compliance with conditions stated in the ECC would be of invaluable assistance to the project proponent.

Thus, whether the permit is required locally or nationally, local governments undoubtedly play a significant role in the process of securing permits. It must be stressed, however, that any assistance that may be offered by local governments in securing local permits should not allow it to deviate from standards set by law or regulation for the issuance of such permits. Local governments, as granting authority and as partner of the applicant, are obviously placed in opposite sides of the same table. Its actions must therefore be always above suspicion in order to prevent future questions on the legality and validity of certain permits issued to the joint venture.

V. Summary and Conclusions

The authority of local governments to enter into joint ventures finds support in various provisions of the LGC. Through joint ventures, local governments may provide an alternative to the BOT scheme and its variants as a vehicle for private participation in their infrastructure projects. The appropriateness of a joint venture for any particular project will depend on the objectives of the local government and the private participant, as well as the risk each of them is willing to take. Certainly, various factors, ranging from the characteristic elements of the joint venture to the applicable approvals, must be considered.

1. Certain features of a joint venture may operate as an advantage or a disadvantage depending on

the objectives of the parties. But unlike other modes of business organization, a joint venture arrangement, in view of the lack of any legal structure which directly governs it, grants parties the flexibility to adapt it, as a business organization, to their particular needs. It allows the parties, for example, to merge the features of a partnership with that of a corporation in order that they may limit their liability or be represented by a centralized body in all their dealings with third parties.

2. For local governments, the decision to use a joint venture as the structure for a particular project may depend both on its capacity and willingness to take certain equity risk that it may avoid totally in a BOT scheme. The equity risk may be preferred where the local government desires to retain a certain measure of control over the project.

3. The private sector participant, on the other hand, may not like joint venture as a transaction scheme because of the potential for greater government intervention in the project. However, in projects where the private sector participant may have to share an existing franchise of, or acquire a new franchise from, the local government unit concerned, a joint venture may be perceived as the more appropriate structure.

4. The attractiveness of a joint venture actually lies in the perception that it may be used to sidestep the requirement of public bidding. Our study shows, however, that where the local governments are required to contribute ownership of properties including lands and existing infrastructure facilities, public bidding may still be required. Even the contribution of the use of properties through lease or other kind of arrangements may still attract the requirement of bidding.

5. There is basis for differentiating a joint venture from a BOT contract and its variants. This difference justifies the conclusion that a joint venture is not governed by the BOT Law and is not subject to the evaluation and approval process set out in that law. For certain types of projects, however, the applicability of the BOT Law may offer an advantage. For instance, where a project would require a franchise, it may be more beneficial to undertake the project using the BOT arrangement since under the BOT, the award of the contract to the contractor automatically entitles the contractor to a franchise.

6. Finally, while a joint venture may not be subject to the structured approval process of the BOT Law, various approvals are still required for the joint venture contract itself and each of the specific undertakings of local governments under the contract. In choosing between BOT and joint venture as a transaction structure, the parties must assess whether the structured process for BOT will take longer than the piecemeal approach for joint ventures.