

DEPARTMENT ORDER NO. 18-01
Series of 2002

**RULES IMPLEMENTING ARTICLES 106 TO 109
OF THE LABOR CODE, AS AMENDED.**

By virtue of the power vested in the Secretary of Labor and Employment under Articles 5 (Rule-making) and 106 (Contractor or Subcontractor) of the Labor Code of the Philippines, as amended, the following regulations governing contracting and subcontracting arrangements are hereby issued:

Section 1. Guiding principles. -- Contracting and subcontracting arrangements are expressly allowed by law and are subject to regulation for the promotion of employment and the observance of the rights of workers to just and humane conditions of work, security of tenure, self-organization, and collective bargaining. Labor-only contracting as defined herein shall be prohibited.

Section 2. Coverage. -- These Rules shall apply to all parties of contracting and subcontracting arrangements where employer-employee relationship exists. Placement activities through private recruitment and placement agencies (as governed by Articles 25 to 39 of the Labor Code) are not covered by these Rules.

Section 3. Trilateral Relationship in Contracting Arrangements. In legitimate contracting, there exists a trilateral relationship under which there is a contract for a specific job, work or service between the principal and the contractor or subcontractor, and a contract of employment between the contractor or subcontractor and its workers. Hence, there are three parties involved in these arrangements, the principal which decides to farm out a job or service to a contractor or subcontractor, the contractor or subcontractor which has the capacity to independently undertake the performance of the job, work or service, and the contractual workers engaged by the contractor or subcontractor to accomplish the job work or service.

Section 4. Definition of Basic Terms. -- The following terms as used in these Rules, shall mean:

(a) "Contracting" or "subcontracting" refers to an arrangement whereby a principal agrees to put out or farm out with a contractor or subcontractor the performance or completion of a specific job, work or service within a definite or predetermined period, regardless of whether such job, work or service is to be performed or completed within or outside the premises of the principal.

(b) "Contractor or subcontractor" refers to any person or entity engaged in a legitimate contracting or subcontracting arrangement.

(c) "Contractual employee" includes one employed by a contractor or subcontractor to perform or complete a job, work or service pursuant to an arrangement between the latter and a principal.

(d) "Principal" refers to any employer who puts out or farms out a job, service or work to a contractor or subcontractor.

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Section 5. Prohibition against labor-only contracting. Labor-only contracting is hereby declared prohibited. For this purpose, labor-only contracting shall refer to an arrangement where the contractor or subcontractor merely recruits, supplies or places workers to perform a job, work or service for a principal, and any of the following elements are present:

- i) The contractor or subcontractor does not have substantial capital or investment which relates to the job, work or service to be performed and the employees recruited, supplied or placed by such contractor or subcontractor are performing activities which are directly related to the main business of the principal; or
- ii) the contractor does not exercise the right to control over the performance of the work of the contractual employee.

The foregoing provisions shall be without prejudice to the application of Article 248 (C) of the Labor Code, as amended.

"Substantial capital or investment" refers to capital stocks and subscribed capitalization in the case of corporations, tools, equipment, implements, machineries and work premises, actually and directly used by the contractor or subcontractor in the performance or completion of the job, work or service contracted out.

The "right to control" shall refer to the right reserved to the person for whom the services of the contractual workers are performed, to determine not only the end to be achieved, but also the manner and means to be used in reaching that end.

Section 6. Prohibitions. Notwithstanding Section 5 of these Rules, the following are hereby declared prohibited for being contrary to law or public policy:

(a) Contracting out of a job, work or service when not done in good faith and not justified by the exigencies of the business and the same results in the termination of regular employees and reduction of work hours or reduction or splitting of the bargaining unit;

(b) Contracting out of work with a "cabo" as defined in Section 1 (ii), Rule I, Book V of these Rules. "Cabo" refers to a person or group of persons or to a labor group which, in the guise of a labor organization, supplies workers to an employer, with or without any monetary or other consideration whether in the capacity of an agent of the employer or as an ostensible independent contractor;

(c) Taking undue advantage of the economic situation or lack of bargaining strength of the contractual employee, or undermining his security of tenure or basic rights, or circumventing the provisions of regular employment, in any of the following instances:

i) In addition to his assigned functions, requiring the contractual employee to perform functions which are currently being performed by the regular employees of the principal or of the contractor or subcontractor;

ii) Requiring him to sign, as a precondition to employment or continued employment, an undated resignation letter; a blank payroll; a waiver of labor standards including minimum wages and social or welfare benefits; or a quitclaim releasing the principal, contractor or subcontractor from any liability as to payment of future claims; and

iii) Requiring him to sign a contract fixing the period of employment to a term shorter than the term of the contract between the principal and the contractor or subcontractor, unless the latter contract is divisible into phases for which substantially different skills are required and this is made known to the employee at the time of engagement;

(d) Contracting out of a job, work or service through an in-house agency which refers to a contractor or subcontractor engaged in the supply of labor which is owned, managed or controlled by the principal and which operates solely for the principal;

(e) Contracting out of a job, work or service directly related to the business or operation of the principal by reason of a strike or lockout whether actual or imminent;

(f) Contracting out of a job, work or service being performed by union members when such will interfere with, restrain or coerce employees in the exercise of their rights to self-organization as provided in Art. 248 (c) of the Labor Code, as amended.

Section 7. Existence of an employer-employee relationship. The contractor or subcontractor shall be considered the employer of the contractual employee for purposes of enforcing the provisions of the Labor Code and other social legislation. The principal, however, shall be solidarily liable with the contractor in the event of any violation of any provision of the Labor Code, including the failure to pay wages.

The principal shall be deemed the employer of the contractual employee in any of the following cases, as declared by a competent authority:

(a) where there is labor-only contracting; or

(b) where the contracting arrangement falls within the prohibitions provided in Section 6 (Prohibitions) hereof.

Section 8. Rights of Contractual Employees. Consistent with Section 7 of these Rules, the contractual employee shall be entitled to all the rights and privileges due a regular employee as provided for in the Labor Code, as amended, to include the following:

(a) Safe and healthful working conditions;

(b) Labor standards such as service incentive leave, rest days, overtime pay, holiday pay, 13th month pay and separation pay;

(c) Social security and welfare benefits;

(d) Self-organization, collective bargaining and peaceful concerted action; and

(e) Security of tenure.

Section 9. Contract between contractor or subcontractor and contractual employee. Notwithstanding oral or written stipulations to the contrary, the contract between the contractor or subcontractor and the contractual employee, which shall be in writing, shall include the following terms and conditions:

(a) The specific description of the job, work or service to be performed by the contractual employee;

(b) The place of work and terms and conditions of employment, including a statement of the wage rate applicable to the individual contractual employee; and

(c) The term or duration of employment, which shall be coextensive with the contract of the principal and subcontractor, or with the specific phase for which the contractual employee is engaged, as the case may be.

The contractor or subcontractor shall inform the contractual employee of the foregoing terms and conditions on or before the first day of his employment.

Section 10. Effect of Termination of Contractual Employment. In cases of termination of employment prior to the expiration of the contract between the principal and the contractor or subcontractor, the right of the contractual employee to separation pay or other related benefits shall be governed by the applicable laws and jurisprudence on termination of employment.

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Where the termination results from the expiration of the contract between the principal and the contractor or subcontractor, or from the completion of the phase of the job, work or service for which the contractual employee is engaged, the latter shall not be entitled to separation pay. However, this shall be without prejudice to completion bonuses or other emoluments, including retirement pay as may be provided by law or in the contract between the principal and the contractor or subcontractor.

Section 11. Registration of Contractors or Subcontractors. Consistent with the authority of the Secretary of Labor and Employment to restrict or prohibit the contracting out of labor through appropriate regulations, a registration system to govern contracting arrangements and to be implemented by the Regional Offices is hereby established.

The registration of contractors and subcontractors shall be necessary for purposes of establishing an effective labor market information and monitoring.

Failure to register shall give rise to the presumption that the contractor is engaged in labor-only contracting.

Section 12. Requirements for registration. A contractor or subcontractor shall be listed in the registry of contractors and subcontractors upon completion of an application form to be provided by the DOLE. The applicant contractor or subcontractor shall provide in the application form the following information:

- (a) The name and business address of the applicant and the area or areas where it seeks to operate;
- (b) The names and addresses of officers, if the applicant is a corporation, partnership, cooperative or union;
- (c) The nature of the applicant's business and the industry or industries where the applicant seeks to operate;
- (d) The number of regular workers; the list of clients, if any; the number of personnel assigned to each client, if any and the services provided to the client;
- (e) The description of the phases of the contract and the number of employees covered in each phase, where appropriate; and
- (f) A copy of audited financial statements if the applicant is a corporation, partnership, cooperative or a union, or copy of the latest ITR if the applicant is a sole proprietorship.

The application shall be supported by:

- (a) A certified copy of a certificate of registration of firm or business name from the Securities and Exchange Commission (SEC), Department of Trade and Industry (DTI), Cooperative Development Authority (CDA), or from the DOLE if the applicant is a union; and
- (b) A certified copy of the license or business permit issued by the local government unit or units where the contractor or subcontractor operates.

The application shall be verified and shall include an undertaking that the contractor or subcontractor shall abide by all applicable labor laws and regulations.

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Section 13. Filing and processing of applications. The application and its supporting documents shall be filed in triplicate in the Regional Offices where the applicant principally operates. No application for registration shall be accepted unless all the foregoing requirements are complied with. The contractor or subcontractor shall be deemed registered upon payment of a registration fee of P100.00 to the Regional Office.

Where all the supporting documents have been submitted, the Regional Office shall deny or approve the application within seven (7) working days after its filing.

Upon registration, the Regional Office shall return one set of the duly-stamped application documents to the applicant, retain one set for its file, and transmit the remaining set to the Bureau of Local Employment. The Bureau shall devise the necessary forms for the expeditious processing of all applications for registration.

Section 14. Duty to produce copy of contract between the principal and the contractor or subcontractor. The principal or the contractor or subcontractor shall be under an obligation to produce a copy of the contract between the principal and the contractor in the ordinary course of inspection. The contractor shall likewise be under an obligation to produce a copy of the contract of employment of the contractual worker when directed to do so by the Regional Director or his authorized representative.

A copy of the contract between the contractual employee and the contractor or subcontractor shall be furnished the certified bargaining agent, if there is any.

Section 15. Annual Reporting of Registered Contractors. The contractor or subcontractor shall submit in triplicate its annual report using a prescribed form to the appropriate Regional Office not later than the 15th of January of the following year. The report shall include:

- (a) A list of contracts entered with the principal during the subject reporting period;
- (b) The number of workers covered by each contract with the principal;
- (c) A sworn undertaking that the benefits from the Social Security System (SSS), the Home Development Mutual Fund (HDMF), PhilHealth, Employees Compensation Commission (ECC), and remittances to the Bureau of Internal Revenue (BIR) due its contractual employees have been made during the subject reporting period.

The Regional Office shall return one set of the duly-stamped report to the contractor or subcontractor, retain one set for its file, and transmit the remaining set to the Bureau of Local Employment within five (5) days from receipt thereof.

Section 16. Delisting of contractors or subcontractors. Subject to due process, the Regional Director shall cancel the registration of contractors or subcontractors based on any of the following grounds:

- (a) Non-submission of contracts between the principal and the contractor or subcontractor when required to do so;
- (b) Non-submission of annual report;
- (c) Findings through arbitration that the contractor or subcontractor has engaged in labor-only contracting and the prohibited activities as provided in Section 6 (Prohibitions) hereof; and
- (d) Non-compliance with labor standards and working conditions. *mt*

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Section 17. Renewal of registration of contractors or subcontractors. All registered contractors or subcontractors may apply for renewal of registration every three years. For this purpose, the Tripartite Industrial Peace Council (TIPC) as created under Executive Order No. 49, shall serve as the oversight committee to verify and monitor the following:

- (a) Engaging in allowable contracting activities; and
- (b) Compliance with administrative reporting requirements.

Section 18. Enforcement of Labor Standards and Working Conditions. Consistent with Article 128 (Visitorial and Enforcement Power) of the Labor Code, as amended, the Regional Director through his duly authorized representatives, including labor regulation officers shall have the authority to conduct routine inspection of establishments engaged in contracting or subcontracting and shall have access to employer's records and premises at any time of the day or night whenever work is being undertaken therein, and the right to copy therefrom, to question any employee and investigate any fact, condition or matter which may be necessary to determine violations or which may aid in the enforcement of the Labor Code and of any labor law, wage order, or rules and regulations issued pursuant thereto.

The findings of the duly authorized representative shall be referred to the Regional Director for appropriate action as provided for in Article 128, and shall be furnished the collective bargaining agent, if any.

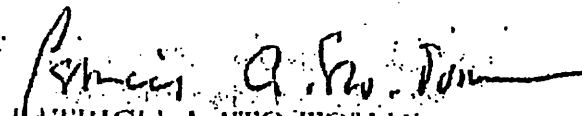
Based on the visitorial and enforcement power of the Secretary of Labor and Employment in Article 128 (a), (b), (c) and (d), the Regional Director shall issue compliance orders to give effect to the labor standards provisions of the Labor Code, other labor legislation and these guidelines.

Section 19. Solidary liability. The principal shall be deemed as the direct employer of the contractual employees and therefore, solidarily liable with the contractor or subcontractor for whatever monetary claims the contractual employees may have against the former in the case of violations as provided for in Sections 5 (Labor-Only contracting), 6 (Prohibitions), 8 (Rights of Contractual Employees) and 16 (Delisting) of these Rules. In addition, the principal shall also be solidarily liable in case the contract between the principal and contractor or subcontractor is preterminated for reasons not attributable to the fault of the contractor or subcontractor.

Section 20. Supersession. All rules and regulations issued by the Secretary of Labor and Employment inconsistent with the provisions of this Rule are hereby superseded. Contracting or subcontracting arrangements in the construction industry, under the licensing coverage of the PCAB and shall not include shipbuilding and ship repairing works, however, shall continue to be governed by Department Order No. 19, series of 1993.

Section 21. Effectivity. This Order shall be effective fifteen (15) days after completion of its publication in two (2) newspapers of general circulation.

Manila, Philippines, 21 February 2002.


PATRICIA A. STO. TOMAS
Secretary