

# It's Official: Employers in Japan Must Convert Some Fixed-Term Employment Contracts to Indefinite Status

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## **Background**

The 2013 amendment to Japan's Labor Contract Act mandates the conversion of certain fixed-term employment contracts into permanent ones whenever (1) an employee has entered into two or more fixed-term employment contracts with an employer and (2) the employee has worked for a total of at least five years under those fixed-term employment contracts.

Japan's labor laws contemplate "lifetime employment," a concept deeply ingrained in Japan's culture and judicial practices. Employers cannot terminate employment except in very limited circumstances—generally, only true misconduct or dire economic circumstances in practice—and when employees challenge their dismissals, labor tribunals regularly grant reinstatements to positions if the stringent standard permitting dismissal has not been met. Fixed-term contracts provide a theoretical loophole, with the apparent ability to allow a contract to expire without renewal. Foreign employers rely on these contracts frequently and—particularly, given the prolonged economic downturn—Japanese employers are doing so as well.

At the time of the 2013 amendment, over a third of employees in Japan were reportedly on fixed-term contracts. The amendment's goal was to “relieve the nonrenewal anxiety of workers on fixed-term contracts, rectify unfair working conditions justified by the fixed-term relationship, and to realize a society where workers can keep working without anxiety.” (*The Japan Times*, March 19, 2013.)

Practically speaking, the law codified what judges had already been doing in many circumstances. When employers have failed to renew a fixed-term contract, Japanese courts have long utilized the “abusive dismissal” doctrine, finding a right to continue working for an employer when the employee has reasons to expect renewal or when a fixed-term contract has been repeatedly renewed. The unwritten requirement for a fixed-term contract to be upheld as such was and is that the employer had a reason for hiring the employee on a fixed-term basis—so employers using fixed-term contracts as, in effect, extended probationary periods were vulnerable to an unfavorable result in a dispute regardless. The difference now is in employee leverage: once employees hit the second renewal and five-year mark, any uncertainty about their legal protection is removed.

### **Exceptions to the 2013 Amendment's Requirements**

Certain exceptions to the 2013 amendment's conversion-to-permanent-contract requirement exist. For example, certain highly compensated (e.g., nearly \$100,000 USD or above) professional employees are exempt from this conversion requirement. For this exemption to apply, the employee must be engaged in a fixed-term project for five to ten years, and the employer must take certain statutory measures (e.g., providing professional training opportunities or additional days off for the employee to do so). Also, employees working beyond retirement age (which used to be 60, but is being gradually raised to 65 by 2025) may be exempt. To take advantage of this exemption, though, the employer must put in place policies to promote the employment of older employees (e.g., raising the retirement age, adopting a re-hiring system for employees having reached retirement age) and take steps to improve the employment of older employees. Importantly, all exemptions must be approved by the local labor office before they can become valid.

### **International Trends**

Limiting fixed-term contracts reflects legal trends in the region, and even worldwide. In the People's Republic of China, for example, the Labor Contract Law requires an employer to enter into an indefinite-term contract with an employee who has either had two employment contracts with the same employer or has serviced the same employer for ten years, as long as the employee exercises the option. (Although some Shanghai courts have enforced this requirement less stringently, the majority view is to strictly enforce the letter of the law against employers.)

In Korea, the supreme court ruled in 2016 that a fixed-term employee has a reasonable expectation of conversion to an indefinite term based on certain factors such as the employer's history of offering

permanent jobs to other fixed-term employees performing similar duties to those of permanent employees, and other circumstances indicating an expectation of a permanent status.

In France, indefinite-term employment contracts are the norm, and fixed-term contracts the exception. If, for example, a fixed-term contract continues after its term or is renewed more than twice for an overall duration of more than 18 months, French labor courts may deem such a contract as one with an indefinite term. Similarly, in Italy, when the total duration of a fixed-term contract (including extensions and renewals and also including employment through staffing agencies regarding the same duties) exceeds 36 months, it will be automatically deemed an indefinite-term contract after the 36th month.

And in Russia, a fixed-term contract is allowed merely for up to five years and permitted only for statutorily enumerated reasons, which are extremely restrictive. Fixed-term contracts failing to meet the stringent statutory requirements are deemed indefinite-term contracts by Russian courts.

### **Key Takeaways**

The five-year milestone in Japan provides a good opportunity to reevaluate practices regarding fixed-term contracts.

- Review contracts for all employees in Japan with more than five years of service, counting from the *earliest possible* service date of any fixed-term contract starting on or after April 1, 2013 (including employees with service from an acquired company and employees who worked or work for the company as staffing-agency employees or independent contractors). Employees meeting the above-discussed legal qualification will be treated as indefinite-term employees upon their request.
- For employees with fewer than five years of service, calendar 30 days before term expiration dates to maximize leverage in any termination or resignation negotiations. As mentioned above, nonrenewal of a contract is no guarantee of a valid termination of employment—even when the employee does not yet qualify for the mandatory conversion to an indefinite-term status.
- Initiate applications for any applicable exemptions you wish to pursue well before any applicable conversion dates. Absent an approval before an eligible conversion date, qualified fixed-term contracts would automatically become indefinite term on that date as long as the employee desires so.
- Consider your standard practices on fixed-term contracts. For example, consider instituting longer initial terms or longer probationary periods (which should not exceed a year) or conducting early evaluation of whether indefinite contracts are realistic for certain positions.
- Train leaders administering Japanese employment contracts. Anyone with responsibility over employment contracts governed by Japan's laws must be aware that fixed terms are always vulnerable to a determination that they are actually “indefinite” arrangements—and that fixed terms are not forever in any case.
- Review work rules (akin to an employment handbook in the United States), applicable policies, and labor-management agreements (known as “Article 36 agreements,” which are agreements employers entered

into with labor unions or with worker representatives under Article 36 of Japan's Labor Standards Act). Both work rules and labor-management agreements must be filed with the Labor Standards Inspection Office. In Japan, if work rules or other internal policies provide better terms and benefits than particular employment contracts, the ones more favorable to the employees will apply. Thus, if there is no distinction between regular employees (i.e., those with permanent status by agreement but not by the operation of law) and employees who convert to permanent status under the 2013 amendment, the more beneficial terms meant only for regular employees may become mandatory for converted employees as well. If there is the potential of such a discrepancy, the employer should consider revising the work rules or other policies following the applicable procedural requirements, which include submitting them in Japanese for approval by the Japanese labor authorities.

## TOPICS

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