

Fixed-Term Contracts (Japan)

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Law stated as of 01 Jan 2023 • Japan

A Practice Note setting out the key issues concerning fixed or definite-term employment contracts (FTC) in Japan. This Note discusses the different types of FTCs, advantages and disadvantages of using FTCs, limitations on FTCs, employee rights and tips for drafting FTCs.

An employer may want to employ an individual under a fixed or definite-term employment contract (FTC) due to the advantages of an FTC, such as the relative certainty offered by the finite duration of the employment relationship. However, there may be limitations and restrictions on when an FTC is permitted, what is an FTC, and the duration of an FTC. Consequently, other arrangements may be more appropriate for the parties.

This Note examines the key considerations when employing an individual on an FTC in Japan. The topics covered include:

- The different types of FTC.
- The advantages and disadvantages of using an FTC.
- When FTCs are permitted.
- The limitations on the duration of an FTC.
- The rights of fixed-term employees.
- Tips when drafting an FTC.

Definition of an FTC

An FTC in Japan means an employment contract with a fixed term as stipulated in Article 17 of the [Labor Contracts Act \(Act No. 128 of 2007\)](#) (LCA).

No conditions, pre-requisites, or justified reasons (for example, working temporarily) are required to enter an FTC in Japan, and the parties have discretion to decide whether to enter into an FTC.

In principle, any FTC terminates with the expiration of its term, and the employer can only terminate an FTC before its term expires when there are unavoidable circumstances (Article 17(1), LCA) (see [What to Consider When Terminating Employment Under an FTC](#)).

Advantages and Disadvantages of an FTC

The advantage of an FTC for an employer is that it is easier to terminate an FTC employee compared to an indefinite term employee. That is, the employment terminates on the expiry of the FTC without the need to provide prior notice or follow any additional process (however, see [Restriction on Non-Renewal of FTC](#)). This allows an employer to easily adjust the labor force according to unpredictable economic changes and the employer's business performance.

An FTC is also an ideal option for an employee who wants to work on a specific task, only for a particular period, or with limited responsibilities.

FTCs are quite common in Japan and about one in four employees in Japan is an FTC employee. According to the [statistics of Labor Force Survey](#) conducted by Statistics Bureau of Japan, the share of FTC Employees in the labor force ranged between 25% and 29% over the past decade.

FTC Employees and Indefinite Term Employees: Key Differences

Japanese law does not differentiate between the roles of FTC employees and indefinite term employees. Therefore, both can have the same functions and responsibilities. However, in practice FTC employees tend to have:

- Limited job descriptions.
- Limited work locations (such as no transfers or relocations).
- Fewer overtime hours.

Due to these differences and lesser demands placed on the FTC employee, an FTC employee may sometimes need to compromise on salary amount, bonuses, various allowances, and retirement benefits enjoyed by an indefinite term employee (see [Fair Treatment of FTC employees](#)).

There are no additional remuneration requirements for an FTC employee in Japan.

An FTC employee can undertake the same role as that of an indefinite term employee. An employer is not required to justify the reason for the different types of employment but must justify the reason for any difference in rights and benefits between an FTC employee and an indefinite term employee.

Fair Treatment of FTC Employees

In 2020, the [Act on Improvement of Personnel Management and Conversion of Employment Status for Part-Time Workers and Fixed-Term Workers \(Act No. 76 of 1993\)](#) (Part-Time Workers and Fixed-Term Workers Act) was amended to address the fair treatment of FTC employees.

This law introduced the unique Japanese version of the *equal pay for equal work* system. In general, *equal pay for equal work* means that the same wage or compensation should be paid to employees whose job descriptions are the same or equivalent. However, most companies in Japan use a wage system based on career development for the future and years of service, rather

than mere job descriptions. This is because, for a long time in Japan, new graduates often worked at the company they first joined until their retirement age (so-called life-time employment).

Since employees employed under an FTC, by their very nature, do not usually stay with the company until the end of their career, the wage system for FTC employees does not consider career development for the future and years of service.

As a result, Japan uses a different wage system for regular employees (mainly consisting of indefinite term employees) and non-regular employees (consisting of FTC employees and part-time employees). It is therefore difficult to make simple comparisons between employees with different wage systems and achieve equal pay for equal work.

Under the Japanese version of equal pay for equal work, the Part-Time Workers and Fixed-Term Workers Act provides that the following factors be analyzed when determining whether an FTC employee and an indefinite term employee are comparable and whether their compensation and benefits should be the same or similar (that is, there has or has not been unreasonable treatment, see [Prohibition of Unreasonable Treatment](#) and see [Prohibition of Differential Treatment](#)):

- The similarity of the job descriptions, namely the kind of the duties and types of primary duties. Primary duties are established using the following criteria:
 - work that is essential to the worker's assigned duties;
 - work whose results have a significant impact on the performance and evaluation of the establishment;
 - work that occupies a large proportion of the worker's total duties in terms of time and frequency; and
 - levels of responsibility associated with those duties.
- The similarity of the scope of changes in the job descriptions:
 - transfer of workplace exists (that is the employer can change the employee's place of work;
 - the extent and scope of the transfer of the workplace is the same;
 - the employer has the option to change the job description and job assignment; and
 - the scope of change to the job description and job assignment is the same.

Prohibition of Unreasonable Treatment

An employer must not create *unreasonable* differences between the base pay, bonuses, and other treatment of an FTC employee and its corresponding treatment of an indefinite term employee (Article 8, Part-Time Workers and Fixed-Term Workers Act). Whether treatment is considered unreasonable in the circumstances depends on different factors, including job descriptions and their scope of changes, job performance, competence, experience, and the history of negotiations between the employer and the applicable trade union.

Article 8 of the Part-Time Workers and Fixed-Term Workers Act aims for *balanced treatment* by ensuring the differences in treatment between indefinite term employees and FTC employees, are in accordance with the difference in circumstances between the employees and are not *unreasonable* considering their job descriptions. Therefore, an employer must justify the differences in treatment between an FTC and an indefinite term employee by explaining why the job descriptions, their scopes of change, or any other relevant considerations (such as, performance), are different.

The Ministry of Health, Labor, and Welfare (MHLW) has issued guidelines providing specific examples of the standards used to determine what a *reasonable* treatment of an FTC employee is compared to an indefinite term employee:

- The same amount of base salary must be paid to an FTC employee as an indefinite term employee if the assessments of the following factors (as applicable) are the same for each employee:
 - ability or experience;
 - performance or results; or
 - years of service.
- Regarding bonuses paid in proportion to the FTC employee's contribution to the company's business performance, the same amount must be paid to the FTC employee as the indefinite term employee who made the same degree of contribution as the FTC employee (for example, both employees have worked the full bonus year, in the same or similar roles, and performed to the same or similar level).
- Overtime and late-night work allowances, commuting allowances, and allowances for employees who live by themselves away from their family must be paid at the same rate as indefinite term employee.

Prohibition of Differential Treatment

An employer must not subject an FTC employee to unequal treatment (that is, less favorable treatment) compared to an indefinite term employee if:

- Their job description is the same as that of the indefinite term employee.
- The scope of changes to their job description throughout their employment term is likely to change within the same scope of the indefinite term employee.

(Article 9, Part-Time Workers and Fixed-Term Workers Act.)

The law aims to ensure equal treatment between FTC employees and indefinite term employees by prohibiting discriminatory treatment of employees, with the same or similar job descriptions and the same or similar scopes of changes to their job descriptions, based on whether they have an FTC.

Possible Actions by Authorities on Unreasonable and Differential Treatment

If an employer does not fairly treat an FTC employee compared to an indefinite term employee (that is, in accordance with Articles 8 and 9 of the Part-Time Workers and Fixed-Term Workers Act), it may be subject to the following actions:

- The Minister of Health, Labor, and Welfare (Minister) may request the employer to file a report and may further advise the employer, issue guidance, or issue a recommendation.
- If the Minister issues a recommendation to an employer who violated the provisions of Article 9 of the Part-Time Workers and Fixed-Term Workers Act and such employer fails to follow it, the Minister may make this fact public. If the employer violates Article 8, the Minister cannot make this fact public, but can only advise the employer, issue guidance, or issue a recommendation.
- If an employer does not fairly treat an FTC employee compared to an indefinite term employee, the employee can claim damages for the amount equivalent to the difference in wages.

(Article 18, Part-Time Workers and Fixed-Term Workers Act.)

FTC Employees and Independent Contractors: Key Differences

The key distinction between an FTC employee and an independent contractor is that the employee is under the employer's instruction and control, rather than there being a client and service provider relationship. An FTC employee is more suitable for an employer who wants to freely decide the job descriptions and assignments of the employee under the direction of the employer.

FTC Employees and Agency Workers: Key Differences

The key distinction between an FTC employee and an agency worker is who the employer of the individual is. An agency worker is employed by an agency and dispatched to a client company based on a *worker dispatch* contract between the agency and the client company. Although an agency worker is under the client company's supervision and control, the agency is the employer of the agency worker. An FTC employee is more suitable for an employer who wants full control over an employee.

Requirements of an FTC

Regardless of whether the contract is an FTC or an indefinite term, the parties should set out the working conditions in writing, whenever possible (Article 4, LCA).

When entering an employment contract, an employer must disclose the terms of the employment contract to the employee (Article 15 (1), *Labor Standards Act (Act No. 49 of 1947)* (LSA), and Article 5 (1), Item (i) to (iv) and Article 5 (3), *Ordinance for Enforcement of the LSA (Ordinance of the Ministry of Health and Welfare No. 23 of 1947)*).

An employer who enters into an FTC with an employee, must clearly state:

- The start and end date of the FTC.

- Whether the FTC may be renewed (for example, automatically renewed, may be renewed, or not renewed).
- If applicable, the matters concerning standards for the FTC renewal. This may include:
 - the amount of work conducted and completed by the employee by the end of the contract period;
 - the employee's work performance and attitude;
 - the employee's ability to perform work;
 - the employer's business condition; or
 - the on-going progress of work being engaged by the employee.

(Article 5 (1), Item (i)-2, Ordinance for Enforcement of the LSA and Article 1, *Standards for the Execution, Renewal, and Termination of FTC*).

The working conditions that an employer must clearly indicate to an employee when entering an employment contract are not limited to the above conditions concerning renewal. Such conditions are not provided in this note since they are not unique to the FTC. The *model FTC* can be found on MHLW's website.

Duration and Renewal of FTCs

Duration

In Japan, generally, the maximum duration of an FTC is three years (Article 14, LSA). However, the parties can agree to a term of five years in the following circumstances:

- An FTC that defines the period necessary to complete a certain project, and the duration of such project is beyond three years.
- An FTC entered with a worker who has expert knowledge, skills, or experience falling under the standards prescribed by the *Minister of Health, Labor, and Welfare of Japan* as being an advanced level. This exception is limited to a worker who is appointed to work on activities requiring the prescribed advanced level of expertise.
- An FTC entered with a worker who is 60 years or older.

(Article 14 (1) and (2), LSA.)

A worker who has expert knowledge, skills, or experience is limited to persons:

- With a doctoral degree.

- Who are highly qualified such as certified public accountants, doctors, lawyers, and first-class architects.
- With a certain level of education and work experiences such as system engineers and designers, and annual income of at least 10.75 million yen.

(MHLW of Health, Labor and Welfare Announcement No. 356, [Enforcement of the Law Partially Amending the LSA as of October 22, 2003](#)).

There is no minimum limit for a period of FTC.

There are also no limits on the number of renewed FTCs and their total cumulative period. For example, an employee can be employed on two consecutive FTCs of three years, a total of six years. However, although such FTCs do not convert into an indefinite term contract automatically, when the cumulative period of two or more FTCs exceeds five years the employee can request the contract be converted to an indefinite term contract and the employer is deemed to have accepted such request (Article 18(1), LCA) (see [Renewal](#)).

If there is a six-month gap between FTCs, the previous FTC is not counted when calculating the cumulative period.

Renewal

The employer and the employee can agree to renew the FTC at any point. The employer is also not required to justify the reason for the renewal. However, the potential to renew must be stated in the FTC (see [Requirements of an FTC](#)).

The employer can renew an FTC at its discretion. Generally, an FTC terminates on the expiry of its term without the need for prior notice; however, the employer must provide at least 30 calendar days' advance notice of non-renewal if either:

- The FTC was already renewed more than three times.
- The total cumulative period of the FTC is longer than one year.

(Article 2, Standards for the Execution, Renewal, and Termination of FTC.)

In 2012, Japan established a scheme to convert an FTC to an indefinite term contract to ensure the stability of employment for FTC Employees.

Accordingly, and as detailed in [Duration](#), if an FTC employee whose total cumulative employment period through two or more FTCs with the same employer, and with a gap of less than six-months between each FTC, exceeds five years files an application to the employer for an indefinite term contract before the current FTC expires, the employer is deemed to have accepted such application (that is the FTC converts into an indefinite term contract without a clear or express agreement of the employer) (Article 18, LCA). In such cases, the terms and conditions of the employment contract remain the same even after the FTC converts into an indefinite term contract (Article 1(1), LCA).

Short-Term FTCs

An employer should not continually renew an FTC with a short duration unless it is required for the purpose or aim of the FTC (Article 17 (2), LCA). This means, an employer can enter an FTC for one month if the project is genuinely expected to only last one month. Short-term FTCs should not be entered with the intention of simply making it easier to terminate an employee's employment. The courts have not ruled that an FTC becomes immediately illegal because it violates Article 17(2) of the LCA since this provision merely requires the employer to give consideration to the employee's position (Tokyo High Court, (hanrei jihou) 2388, 7 February 2018).

Exceeding Limits on Duration and Failing to Confirm Non-Renewal

When the intended duration of a single FTC is longer than the maximum duration stipulated under the LSA (that is, three or five years respectively, see [Duration](#)), the duration of the single FTC is limited to and reduced to three or five years depending on the type of FTC (Article 14, LSA).

Unless there is a requirement to provide notice of non-renewal, an FTC automatically ends on the expiration of the term.

If an employee continues to work after the expiration of the term and an employer does not object, such FTC is considered renewed under the same terms and conditions as the previous FTC (Article 629, [Civil Code, \(Act No. 89 of 1896\)](#)). The law is not clear whether the new contract is an FTC or an indefinite term contract, but the prevailing view is that the renewed contract is an FTC instead of an indefinite term contract.

If the employer objects to the continued work and the renewal, the FTC will not be renewed. However, the employer is deemed to accept the renewal of the FTC if such employer's refusal:

- Lacks objectively reasonable grounds.
- Is not found to be appropriate in general societal terms.

(Article 19, LCA.)

For more detail, see [Restriction on Non-Renewal of FTC](#).

What to Consider When Terminating Employment Under an FTC

Notice

There are very limited grounds on which an FTC can be terminated early on notice (see [Early Termination of FTC](#)). If such ground or justification applies, when an employer terminates an FTC early, the employer must either:

- Give at least 30 calendar days' advance notice of termination.
- Pay the employee the average salary they would have earned had they worked for a period of at least 30 calendar days (advance notice allowance).

(Article 20, LSA.)

The average salary is calculated by dividing total amount of wages over the three-month period preceding the termination notice day by the total number of calendar days during that period (Article 12, LSA).

If an employer does not provide advance notice, the FTC terminates only when either:

- 30 calendar days have passed from the notice of termination.
- The employer pays the advance notice allowance.

An employee is not required to give advance notice to an employer under the LSA and Civil Code. However, if the cumulative period of an FTC is more than five years, the employee must provide at least two weeks' advance notice of termination (Article 626, Civil Code).

For more detail on notice of termination requirements in Japan, see [Practice Note, Notice of Termination \(Japan\)](#).

Employee Rights on Termination of the FTC

Early Termination of FTC

The overarching principle is that when entering an FTC the expectation between the parties is that the employment continues until the expiry of the term. As a result, under Japanese law there are strict limitations on when an FTC can be terminated early.

Article 17, Paragraph 1 of the LCA provides that an employer may not dismiss an FTC employee until the expiration of the term of the employment contract, unless there are *unavoidable circumstances*. Unavoidable circumstances include the employee's inability to work, malicious misconduct, significant incompetence, and poor performance.

Meeting the requirement of unavoidable circumstances is more difficult than meeting objectively reasonable grounds and general societal terms which are required to dismiss indefinite term employees.

In the event an FTC employee's employment is terminated early without unavoidable circumstances, the dismissal is invalid and the employee retains the status of an employee under the FTC.

Restriction on Non-Renewal of FTC

The courts have created judicial precedents to protect FTC employees by applying the doctrine of abuse of the right to dismiss an employee articulated under Article 16 of the LCA, to a non-renewal of an FTC (The Supreme Court, (minshu) 2217, 22 July 1974 (Toshiba Yanagimachi Factory Case)).

Article 19 of the LCA provides that the employer must renew the FTC if the employee duly applies for a renewal, and the employer's refusal to accept the renewal lacks objectively reasonable grounds (for example, poor work attitude, poor health condition, misconduct, unfitness for duty, and need for personnel reduction) when either of the following circumstances apply:

- The FTC is substantially the same as an indefinite term contract. That is, the FTC has been repeatedly renewed to the extent that the expiry of the FTC without renewal would be considered similar to terminating an indefinite term of

employment. For example, an instructor at a driving school who was employed for one year as an FTC employee, the court adjudicated that such FTC is substantially the same as an indefinite term contract given the fact that:

- many of the FTC employees have been working for more than 10 years, and had their FTCs renewed on multiple occasions;
- the job description (training tasks) was the same as an indefinite term employee; and
- the same work rules have been applied to both FTC employees and indefinite term employees.

(Kyoto District Court, (rodo-hanrei) No.1062, 16 July 1999 ((Iwakura Driving School Case).))

- The employee's expectation of continued employment is based on reasonable grounds and is considered a right worthy of legal protection. For example, in a case of an employee employed on an FTC of two months duration, the court concluded the parties' expectation of continued employment should be considered a right worthy of legal protection since the FTC had already been renewed five times (each of two months duration) even though the employee's tasks were simple, and a strict procedure has been taken to confirm the employee's will to renew the FTC. (Supreme Court, (rodo-hanrei) No.486, 4 December 1986 (Hitachi Medico Case.))

The judicial precedents held that the following facts are relevant to determine whether Article 19 of the LCA applies or not:

- The identity and similarity of the job descriptions and work conditions to those of indefinite term employees.
- The status of the employment management classification, meaning whether there is a clear distinction in working conditions (for example, transfers and promotions) between indefinite term contract employees and FTC employees.
- The number of times the FTC has been renewed and years of service of the FTC employee.
- The manner and strictness of the renewal procedures in place. That is, for example whether:
 - there is an interview at each renewal;
 - a decision of renewal is made by the committee;
 - a detailed written statement of the conditions after renewal is issued.
- Whether the employer indicated by words or actions that the employment contract is expected to continue.
- Whether the FTCs with other employees have been renewed.

In practice, some employers include a non-renewal clause in the FTC as a countermeasure to these protections for an FTC employee. Although there is some dispute over the legal effect of such non-renewal clauses, both in academic circles and judicial precedents, the prevailing view is that when an employee gives free and voluntary consent to a non-renewal provision, the employee is considered to have waived their expectation of continued employment.

Redundancy (Lay-off) or Re-organisation

In the context of collective redundancy, it is common for an employer to choose not to renew any FTCs before deciding to terminate any at risk indefinite term employees. The Japanese courts have supported this approach on the grounds that the expectations of continuance of employment differ between FTC Employees and Indefinite Term Employees.

Severance Pay

An employer is not required to pay any amount of severance when an FTC is not renewed (that is, the employment terminates on the expiry of the term).

However in practice, to amicably terminate an FTC early (even where unavoidable circumstances apply) the employer may be required to make a severance payment. In such cases, the parties enter into an agreement whereby the employee resigns and waives any claims against the employer, in return for a severance payment. These agreements are often called separation agreements.

Practical Tips When Entering into FTCs

Short Term FTCs and Probation Periods

Since the termination of an FTC before the end of the term is strictly restricted (see [Notice](#) and [Early Termination of FTC](#)), to allow an employer to evaluate an FTC, an employer is recommended to either enter:

- An FTC with a short initial term (such as a month to three months).
- An FTC with a longer total term but including an initial probation period of a month to three months.

The challenge with shorter-term FTCs, and FTCs with a probation period, is that they may not be as attractive to prospective employees.

Length of Probation Period

Although no specific maximum term for a probation period is stipulated in law, a probation period that is too long compared to the overall contract period is considered invalid under Article 90 of the Civil Code.

For example, in a case where a securities analyst's FTC with a term of one year had a six-month probation period, the probation period of more than three months was deemed invalid (Tokyo District Court, (rokeisoku) No.2180, 31 January 2017 (Leading Securities Case)).

Notice of Termination During Probation Period

See [Practice Note, Notice of Termination \(Japan\)](#), [Notice During Probationary Period](#).

No advance notice of termination is required until the 14th calendar day of the probation period, but after the 15th calendar day, one month's notice of termination is necessary (Article 21, LSA).

Although there is some dispute as to whether unavoidable grounds are required for dismissal during the probationary period, the prevailing view in academic circles and judicial precedents is that the requirement of unavoidable grounds should not be interpreted the same way during the probation period as for dismissal after formal hiring (that is, the employment after the probation period).

If an FTC has been renewed, the second or subsequent FTCs cannot have probation periods.

No Certain End Date

An employer must disclose the terms of the FTC when entering into the FTC. If an employer needs an employee for a period necessary to complete a certain project and it is difficult to determine the specific time, providing an open-ended period such as "until the completion of the construction" may be acceptable. Please note, however, that such method of providing the time period is not explicitly allowed under the relevant laws and regulations and may be regarded as a breach of Article 15 Paragraph 1 of LSA. The employer can be punished with a fine of not more than JPY 300,000 (Article 120 (1), LSA).

Human Resources Expert

When an employer enters an FTC in Japan, the employer's Japanese Human Resources expert should review the [Guideline for Employment Management of Fixed-Term Contract Workers](#) issued by the MHLW, to know what an employer needs to be careful of.