Commentary

If a Fixed-term Labor Contract Has been Set Renewable for Up To Five Years, Is It Permissible for the Employer to Refuse to Renew the Contract in the Fifth Year When Workers' Right to Apply for Conversion to an Indefinite-term Contract Arises?

The *Nippon Express (Kawasaki Branch)* Case
Tokyo High Court (Sept. 14, 2022) 1281 *Rodo Hanrei* 14

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I. Facts

In September 2012, X (plaintiff, appellant) started working as a temporary agency worker dispatched by Company S, a temp agency, at the oil distribution center affiliated to Branch C of Company Y (defendant, appellee), a company engaging in logistics business in general and related businesses, including motor truck transportation, railway freight transportation, construction, and specialized transportation. In June 2013, X concluded a fixed-term employment contract with Y as a clerical worker at the oil distribution center for a contract term of one year. With regard to the renewal of the contract, the written contract executed between X and Company Y provided that the contract "may be renewed. The renewal is determined depending on the workload, work performance, attitude, and ability, the financial conditions of the branch office where the worker is employed, and the progress of the work performed by the worker, at the end of the expiration of the contract term." In addition, it also stated, "The contract will not be renewed for a period exceeding five years in total from the date of commencement of the first employment contract with the Company (hereinafter referred to as the 'renewal limit clause')." The duties assigned to X could be performed by other contract workers. At the time when Company Y refused the renewal of X's contract, the oil distribution center where X worked had been in business for more than 17 years, and although it was run in the red, there was no plan to close any of its business establishments. Before and after X worked at Company Y, there were fixed-term contract workers who had been working at Company Y for more than five years, but the contract conditions applicable to those workers were different from those of X because no renewal limit was set under their initial fixed-term employment contracts.

X and Company Y subsequently renewed the employment contract four times, and at each renewal, a written contract was prepared with X's signature and seal. When the contract was renewed for the fourth time on June 29, 2017, the written contract stated that the contract would not be renewed the next time. On this occasion, a procedure was carried out wherein a manager read out to X the explanation concerning the renewal limit, or the non-renewal of the contract, and a written confirmation was prepared as proof that X received the explanation, and was submitted to Company Y.

Around June 1, 2018, Company Y notified X in writing that the Employment Contract with X (hereinafter, the "Employment Contract") would expire on June 30, 2018. The renewal limit clause was cited as one of the reasons for the expiration of the contract.

On July 31, 2018, X filed a suit against Y to seek a confirmation that X had the status of a worker who has rights under the employment contract, alleging that the renewal limit clause is invalid as it was an attempt to avoid the worker's right to apply for

conversion to an indefinite-term contract under Article 18 of the Labor Contracts Act, and X had a reasonable expectation for continued employment, and that Company Y's refusal to renew X's contract is unacceptable under Article 19 of the Labor Contracts Act as it is not found to be objectively reasonable or appropriate in general societal terms. The court of first instance dismissed X's claim (The Yokohama District Court, Kawasaki Branch (Mar. 30, 2021) 1255 *Rohan* 76). X appealed to the high court.

II. Judgment

The court of second instance dismissed X's appeal and upheld the judgment in first instance that dismissed X's claim to seek a confirmation of the status of a worker. The summary of the judgment in second instance is as follows.

Article 18 of the Labor Contracts Act provides for a system for converting a fixed-term labor contract into an indefinite-term contract (a labor contract without a fixed term) if the fixed-term labor contract is renewed repeatedly over a period exceeding five years in total. It is interpreted that this system is intended to prevent the abusive use of fixed-term labor contracts and ensure stable employment of workers. The background to the establishment of this provision is that when fixed-term labor contracts are repeatedly renewed and employment continues for a long period of time, there is a risk that the legitimate exercise of rights by workers may be restrained due to the fear that their employers would refuse to renew their contracts.

On the other hand, it is interpreted that even afte the introduction of Article 18 of the Labor Contracts Act, it is still permissible to use workforce in short-term employment by concluding fixed-term labor contracts for up to five years in total. Therefore, even if the employer concludes fixed-term labor contracts with a total contract term not exceeding five years and subsequently refuses to renew the contract, such conduct would not be immediately deemed an abusive use of fixed-term labor contracts contrary to the purpose of Article 18 of the Labor Contracts Act, nor would it necessarily be considered an act designed to circumvent that provision. Article 19, item (ii) of the Labor Contracts Act codifies the theory established in the Supreme Court 1986 decision in the *Hitachi Medico* Case (Supreme Court (Dec. 4, 1986)). Whether a fixed-term labor contract meets the condition of "having reasonable grounds upon which the worker expects the fixed-term contract to be renewed when the fixed-term contract expires," which is a requirement for applying the theory under this provision to restrict an employer's refusal to renew a fixed-term contract, should be determined comprehensively. This determination involves considering various objective circumstances, such as whether the worker has been employed on a temporary or regular basis, the number of times the contract has been renewed, the total period of employment, the situation of contract term management, and whether the employer's behavior has caused the worker to expect that their employment would continue (hereinafter referred to as "circumstances for consideration"). The fact that the employer and the worker concluded a labor contract that explicitly specifies the maximum period of renewal would be one of the factors for consideration, in combination with the circumstances for consideration mentioned above, in the course of determining whether there are reasonable grounds for the worker to expect that the fixed-term labor contract would be renewed. In other words, such fact would be one of the circumstances due to which the existence of reasonable grounds for the worker's expectation for the renewal of the contract should be denied.

Based on the above, X's argument that "the employer's refusal to renew a fixed-term labor contract to avoid the worker's right to apply for conversion to an indefinite-term contract is impermissible, and the non-renewal clause and renewal limit clause are against public policy and invalid because they were established in an attempt to avoid or circumvent the application of Articles 18 and 19 of the Labor Contracts Act" cannot be accepted.

Under a labor contract, workers are in a position

to be subject to the employer's directions and orders and have limited ability to collect information that they could use as the basis for making their own decisions, and thus they may be forced to accept agreements that are disadvantageous to them. Therefore, for example, when a worker under a fixed-term labor contract has come to have a reasonable expectation for the renewal of the contract, and subsequently enters into a new contract with a specified renewal limit, there may be cases where it should be carefully determined, from the perspective mentioned above, whether the worker can be deemed to have accepted, on their own free will, that such reasonable expectation would be extinguished due to the introduction of the renewal limit.

However, the non-renewal clause and renewal limit clause disputed in this case had been explicitly prescribed in the relevant written contracts since the Employment Contract was concluded for the first time. In addition, it is unambiguously clear that the employment term under the Employment Contract is set as not exceeding five years in total. The section chief of Company Y had an interview with X and explicitly presented and explained this contract condition to X. X entered into the Employment Contract while being fully aware of the existence of the non-renewal clause and renewal limit clause. Given these facts, it is difficult to say that there were circumstances in which an agreement was reached without X's free will, such as that X was forced to accept conditions that were contrary to their legitimate confidence and expectations with respect to the renewal of the contract in the process of concluding the Employment Contract.

According to the above, in light of the facts of this case, it is not found that there are reasonable grounds for X to expect that their employment under the Employment Contract would continue at the time of expiration of the Employment Contract. In other words, the Employment Contract does not satisfy the requirement set forth in Article 19, item (ii) of the Labor Contracts Act, and therefore the theory restricting an employer's refusal to renew a fixed-term contract prescribed in Article 19 of the Labor Contracts Act does not apply. Consequently, the court of first instance was justified in dismissing X's claim by determining that the Employment Contract was terminated upon the expiration of the term of the contract.

III. Commentary

In this case, given the fact that the employer set the total contract term (following several times of renewal) in advance upon concluding a fixed-term labor contract and refused to renew the contract when the total contract term reached the upper limit, the worker disputed the effect of such refusal to renew the contract (*yatoidome*), alleging that it was an attempt to circumvent Article 18 of the Labor Contracts Act, which provides for a worker's rights to apply for conversion to an indefinite-term contract when the total contract term following several times of renewal exceeds five years, or Article 19 of the same Act, which restricts an employer's refusal to renew a fixed-term contract under certain conditions in the same manner as the "abuse of the right to dismiss" theory .

In Japan, fixed-term labor contracts were only regulated by setting the limit to the maximum contract term, and there were no restrictions on the reasons for using fixed-term labor contracts, and also no restrictions on the number of contract renewals or the total contract term. As a result, not a few workers repeatedly renewed their fixed-term labor contracts and worked for the same employer for many years. Then, a case law theory was established to the effect that the abuse of the right to dismiss theory applies by analogy to the employer's refusal to renew a fixed-term contract if the worker's expectation for continued employment is recognized with reasonable grounds, such as when a fixed-term labor contract is repeatedly renewed.[1]

As the number of contract renewals and the total contract term were considered as factors for determining whether the worker reasonably expected that their employment would continue, employers often tried to eliminate such expectation for continued employment by setting the upper limit of the number

of renewals in advance or including in the contract for renewal a provision that the contract would not be renewed next time. Due to such practice, the validity of a clause that sets such upper limit of the number of renewals or the total contract term and a clause that stipulates the subsequent non-renewal of the contract (hereinafter these clauses are collectively referred to as "renewal restriction clauses") has often been challenged.[2]

In the 2000s, the precarious state of employment and unfair treatment (low income) of non-regular workers became social problems. In 2012, the Labor Contracts Act was amended for the purpose of protecting workers with fixed-term contracts (almost equal to non-regular workers). This amendment introduced the right of a fixed-term contract worker to apply for conversion of the fixed-term labor contract to an indefinite-term contract if the fixed-term labor contract has been repeatedly renewed over a period exceeding five years (right of conversion to indefinite-term contract; Article 18 of the Labor Contracts Act).[3]

As a result, it became a common practice to include renewal restriction clauses in a contract so that the total contract term would not exceed five years and the worker's right of conversion to indefinite-term contract would not arise. On the other hand, such manner of using renewal restriction clauses was criticized as substantially preventing the occurrence of a fixed-term contract worker's right of conversion to an indefinite-term contract and thereby attempting to circumvent law. As a result, the legal effect of the renewal restriction clauses was also challenged in relation to Article 18 of the Labor Contracts Act. The case discussed in this article can be positioned as one of such cases.

The issues surrounding renewal restriction clauses can be roughly divided into two cases: (1) cases in which a clause setting the limit to the number of contract renewals, etc. (hereinafter "renewal limit clause") has been explicitly indicated in the initially concluded fixed-term labor contract; and (2) cases in which a fixed-term labor contract is concluded without any clause on contract renewal, and then a new clause restricting renewal is added or other measures are taken when the contract is subsequently renewed. This case is categorized as type (1).[4]

In type (1) case, there are two theoretical questions. First, the renewal limit clause would result in preventing the occurrence of a fixed-term contract worker's right of conversion to an indefinite-term contract when the total contract term reaches five years. The question is whether the practice of including such clause in a fixed-term contract would be regarded as unlawfully depriving the worker of the right of conversion to an indefinite-term contract, which is legally guaranteed under Article 18 of the Labor Contracts Act, and judged to be circumvention of law or violation of the purpose of the system under that Article. Second, if the renewal limit clause is not immediately rendered invalid, a question arises as to how such clause would be judged when the applicability of the theory restricting an employer's refusal to renew a fixed-term contract prescribed in Article 19 of the Labor Contracts Act is at issue, especially in the course of determining whether there are "reasonable grounds upon which the worker expects the fixed-term labor contract to be renewed when the fixed-term labor contract expires" as referred to in item (ii) of that Article.

In the judgment on the case discussed in this article, the court held as follows regarding the first question. It is understood that even after the introduction of Article 18 of the Labor Contracts Act, it is still permissible to use workforce in short-term employment by concluding fixed-term labor contracts for up to five years in total. Therefore, even if the employer concludes fixed-term labor contracts for a contract term not exceeding five years in total and then refuses to renew the contract, such practice would not be immediately judged to be an abusive use of fixed-term labor contracts contrary to the purpose of Article 18 of the Labor Contracts Act. In conclusion, the court ruled that the renewal limit clause would not immediately be judged to be invalid. Although there are some court decisions prior to this judgment that expressed the same purport,[5] the first significance of this judgment is that it clarified this point. As discussed below, this judgment states that even if the renewal limit clause

is not immediately rendered invalid, this does not necessarily preclude the possibility of contract renewal beyond the limit specified in that clause, but it serves as nothing more than one of the important factors in considering the worker's expectation for continued employment. It then follows that the existence of the renewal limit clause itself does not uniformly deprive a fixed-term contract worker of the possibility of conversion to an indefinite-term contract[6] and therefore it does not immediately contradict the purpose of Article 18 of the Labor Contracts Act. Thus, the argument presented in this judgment can be evaluated to be consistent.[7]

Regarding the second question, previous court decisions can be divided into two groups: those that hold that the existence of a reasonable expectation for continued employment is itself denied by the renewal limit clause[8] and those that regard the renewal limit clause as one factor for consideration in determining whether there is a reasonable expectation for continued employment along with other factors.[9] In this judgment, the court held that the fact that the employer and the worker concluded a labor contract that explicitly specifies the maximum period of renewal would be one of the factors for consideration, in combination with the circumstances for consideration, in the course of determining whether there are reasonable grounds for the worker to expect that the fixed-term labor contract would be renewed. Thus, the court clearly adopted the view of the latter of the abovementioned two groups. This is the second significance of this judgment. In the administrative interpretation of Article 19, item (ii) of the Labor Contracts Act,[10] the competent administrative authority took the position that all circumstances that occurred between the time of conclusion of the contract and the time of its expiration should be comprehensively taken into consideration when determining whether there is a reasonable expectation for continued employment, which is an appropriate view.

However, if this approach is taken, the next question is how much weight should be given to the fact that the renewal limit clause is agreed upon under the initially concluded contract in determining whether there is a reasonable expectation for continued employment. In this regard, many court decisions ruled that a reasonable expectation would not arise if the renewal limit clause is agreed upon, unless there are special circumstances.[11] This judgment does not clearly take such position. However, this judgment cites the portion of the determination by the court of prior instance that emphasizes the fact that the renewal limit had been explicitly indicated in the initially concluded contract, and draws the conclusion that a reasonable expectation did not arise on the grounds that "it is difficult to say that there were circumstances in which an agreement was reached without X's free will" in the process of concluding the contract with the renewal limit clause. Accordingly, it is possible to understand that this judgment takes the abovementioned position.

On the other hand, this judgment also presents a view that denies the constancy of work due to the financial conditions at the oil distribution center where X was assigned.[12] After all, it is not definite how much weight the court considers the renewal limit clause to have in determining whether there is a reasonable expectation. In addition, if the renewal limit clause eliminates an expectation for continued employment (unless there are special circumstances), it could in effect eliminate the possibility of conversion to an indefinite-term contract through setting a finite total of the labor contract term. Considering this point, there may be leeway for questioning the consistency with the purpose of Article 18 of the Labor Contracts Act, which is to prevent the abusive use of fixed-term contracts, and the conventional theory restricting an employer's refusal to renew a fixed-term contract, which requires various circumstances to be comprehensively taken into consideration in determining a reasonable expectation for continued employment.[13] Questions such as how the renewal limit clause should be positioned in determining whether there is a reasonable expectation for continued employment and in what cases the renewal limit clause is regarded as an abusive use of fixed-term contract and its effect is denied are open to further discussion.

1. The *Hitachi Medico* case, Supreme Court (Dec. 4, 1986) 486 *Rohan* 6, cited above.
2. The *Qantas Airways Limited* case, The Tokyo High Court (Jun. 27, 2001) 810 *Rohan* 21; The *Hokuyo Denki* case, The Osaka District Court, (Sept. 11, 1987) 504 *Rohan* 25;The *Kinki Kensetsu Kyokai* case, The Kyoto District Court, (Apr. 13, 2006) 917 *Rohan* 59; The *Hotoku Gakuen* case, The Kobe District Court, Amagasaki Branch (Oct. 14, 2008) 974 *Rohan* 25; The *Rikkyo Jyogakuin* case, The Tokyo District Court, (Dec. 25, 2008) 981 *Rohan* 63.
3. For the commentary on the regulations for fixed-term labor contracts and the amendment to the Labor Contracts Act in 2012, see Ryo Hosokawa, "Is a Part-time Instructor Whose Role is Exclusively to Teach University Language Classes a 'Researcher'?" The *Senshu University (Conversion of a Fixed- Term Labor Contract to an Indefinite-term Labor Contract)* Case, *Japan Labor Issues* 7, no.43 (May 2023): 56–61. https:// www.jil.go.jp/english/jli/documents/2023/043-04.pdf.
4. For the issues and court decisions regarding type (2) cases, see Takashi Araki, *Rodoho* [Labor and Employment Law], 5th ed. (Yuhikaku, 2020), 566–569. As a type (2) case involving Nippon Express, see The *Nippon Express (Tokyo)* case, The Tokyo High Court (Nov. 1, 2022) 1281 *Rohan* 5.
5. The *Baiko Gakuin* case, The Hiroshima High Court (Apr. 18, 2019) 1204 *Rohan* 5, The *Sendai City Council of Social Welfare* case, The Sendai High Court (Dec. 10, 2020), *Journal of Labor Cases*, no.110 (May 2021): 38.
6. Kentaro Hayashi, "Keiyaku teiketsu tosho kara 5 nen no koshin gendo ga settei sare ta yuki koyo rodosha ni taisuru yatoidome no tekiho-sei: The *Nihontsuun (kawasaki)* case, Tokyo High Court (Sept. 14, 2022)" [Legality of the employer's refusal to renew a fixed-term labor contract which is renewable for up to five years since the conclusion of the initial contract], *Horitsu Jiho* 95, no. 13 (December 2023): 268–271.
7. Among academic theories, the view that the renewal limit clause is not illegal or invalid unless there are special circumstances as in this judgment (Takashi Araki, Kazuo Sugeno, Ryuichi Yamakawa, *Shosetsu Rodo keiyaku ho* [Labor Contracts Act], 2nd ed., (Kobundo 2014), 177) is dominant (there is a view that basically does not deny the effect of the renewal limit clause but requires sufficient explanation and strict implementation of the clause—Nobutaka Shinohara, "Hi seiki rodosha no koyo shuryo hori to 2018 nen mondai" [Theory of termination of employment of non-regular workers and the 2018 problem], *Quarterly Labor Law*, no.264:77). On the other hand, there is a persistent view that the renewal limit clause is against public policy and invalid unless the employer can prove that this clause is not intended to avoid the worker's right to apply for conversion to an indefinite-term labor contract (reasonable grounds for setting the upper limit of renewal) (Miki Kawaguchi, *Rodoho* [Labor Law], 8th ed. (Shinzansha, 2024), 590–594, Keiko Ogata, "Yuki rodo keiyaku no koshin gendo joko ni kansuru ichi kosatsu" [Consideration on the renewal limit clause in fixed-term labor contracts], *Quarterly Labor Law* 266: 116–127; Tomoko Kawada, "Muki tenkan ruru ni taiko suru goi no koryoku"[Effect of agreement against the rule for conversion to an indefinite- term labor contract], in *Yamada Shozo sensei koki kinen, Gendai koyo shakai ni okeru jiyu to byodo* (Shinzansha, 2019): 350–351, [A festschrift in honor of the 70th birthday of Professor Shozo Yamada, "Freedom and equality in modern employment society"]). The latter view, however, would require special freedom for the conclusion of fixed-term labor contracts (less than five years in total), and would be interpreted in the same way as establishing "entrance regulations" for restricting the use of fixed-term labor contracts (Nobuyuki Inatani, "Koshin jogen kisei ni yoru muki tenkan chokuzen no yatoidome no tekiho-sei" [Legality of the employer's refusal to renew a fixed-term labor contract under regulations limiting the duration of the contract immediately before the conversion to an indefinite-term labor contract] *Min-Shoho Zasshi* 158, no.5 (December 2022): 1237–1248). This may involve an issue as to whether such an effect can be understood as the purpose of Article 18 of the Labor Contracts Act.
8. The *Kyoto Shimbun COM* case (The Kyoto District Court (May 18, 2010) 1004 *Rohan* 160).
9. The *Daikin Kogyo* case (Osaka District Court (Nov. 1, 2012) 1070 *Rohan* 142); The *Docomo Support* case (Tokyo District Court (June 16, 2021) *Journal of Labor Cases*, no.115 (Oct. 2021): 2).
10. Notice on Enforcement of the Labor Contracts Act (Notice *Ki-Hatsu* No. 0810-2, August 10, 2012), 5-5(2)C, which is issued by the Director of the Labour Standards Bureau of the Ministry of Health, Labour and Welfare.
11. The *Baiko Gakuin* case and the *Sendai City Council of Social Welfare* case, *supra* note 5. For the academic theory that takes the same position, see Araki, *supra* note 4, 566.
12. For a view that raises a question about the determination in this judgment, see Hisashi, Takeuchi (Okuno), "Koyo tosho kara fusa re te i ta 5 nen o koe nai to no koshin jogen joko no koryoku" [Effect of the five-year renewal limit included in the initially concluded contract], *Monthly Jurist* no. 1568 :128, and Yoko Hashimoto, "Koshin jogen-sei to fukoshin joko to Rokeiho 19 jo" [Renewal limit clause and non-renewal clause and Article 19 of the Labor Contracts Act], *Monthly Jurist*, no.1580: 5.
13. For a view that points out this issue, see Hayashi, *supra* note 6, 271.

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