



Introduction to employment law in Japan



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For further information
please contact

Kazuki Okada
E kazuki.okada@freshfields.com

Akiko Yamakawa
E akiko.yamakawa@freshfields.com

Akasaka Biz Tower 36F
5-3-1 Akasaka Minato-ku Tokyo 107-6336

T +81 3 3584 8500
F +81 3 3584 8501

W freshfields.com

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Introduction

Economic predictions for 2009 are bleak and suggest that there is another year of turmoil ahead. Businesses have to adjust to a tougher financial environment and restructuring and cost-cutting are often on the agenda. As a result, some employers may need to review headcount and consider redundancies. In light of that, all companies operating in Japan should be aware of and take steps to ensure compliance with Japanese employment law and assess the implications of related decisions in Japanese courts.

The main employment legislation in Japan is the Labour Standards Law (*roudou kijun hou*) and the Labour Contract Law (*roudou keiyaku hou*). The Labour Standards Law was first enacted in 1947 and has since been amended several times. The most recent amendment will become effective on 1 April 2010. The Labour Contract Law was enacted in 2007 and came into effect on 1 March 2008. It codifies important principles of employment contracts, most of which were historically based on court precedents.

This guide outlines some of the key areas of Japanese employment law that companies operating in Japan should be aware of.

General

Statutory law

The Labour Standards Law and the Labour Contract Law are the primary statutes governing employment relationships in Japan and contain mandatory provisions that apply to all employees working in Japan. The Labour Standards Law establishes, among other things, a minimum standard for terms and conditions of employment and the Labour Contract Law governs the contractual relationship between an employer and an employee. There are also several other statutes that regulate certain specific aspects of labour relations, such as wages, equal opportunity, social insurance programmes, health and safety and labour unions.

Competent authority

The Ministry of Health, Labour and Welfare has authority over labour-related matters and can conduct workplace inspections through its Labour Standards Inspection Offices (*roudou kijun kantoku-sho*), which are located in each administrative area.

Starting employment

Hiring

As a general rule, employers can freely determine the person they would like to hire as an employee. This has been recognised as a special freedom under the Japanese employment law system, under which it is relatively difficult to terminate an employee's contract once the employee has been hired. There are certain limited exceptions to this right, such as the requirement that men and women are given equal opportunities, the requirement that a certain percentage of hires are persons with disabilities and certain limitations on using age in hiring criteria.

Offer of employment

The Labour Standards Law requires an employer to specify clearly the terms and conditions of employment upon or before entering into an employment contract. The law requires certain important terms and conditions to be specified in writing. As most of the terms and conditions of employment will usually be stipulated in the employer's 'work rules' (*shuugyou kisoku*; see 'Work rules' below), it is common practice for an employer to provide a prospective employee with an offer letter that stipulates mainly those terms that are specific to the prospective employee (eg salary, job function, place of work etc) and provide a copy of the work rules when employment starts.

Non-competition/non-solicitation clauses

In some industries, it is common for an employment contract to include a non-competition clause (a clause prohibiting employees from working with a competitor for a certain period of time after termination of employment) and/or a non-solicitation clause (a clause prohibiting employees from soliciting other employees to move to other firms). Post-termination non-competition restrictions will be enforceable only if they are regarded by the court as 'reasonable'. The following factors will generally be considered when determining whether a particular restriction is reasonable:

- whether the employer has a legitimate business interest to protect (eg the relevant employee had access to client information or other confidential information);
- whether the employee is adequately compensated for the restrictions (eg the employee was provided with a generous retirement package); and
- whether the scope of the restriction is reasonable (eg the length of the restriction, the type of activities that the employee is restricted from engaging in and the geographic scope of the restriction must be reasonable).

For example, a six-month non-competition restriction imposed on a high-level managerial employee who had access to client and confidential information, and had received a generous retirement package (see page 14), is likely to be held valid. It would generally be difficult to justify a non-competition restriction that is longer than one year. Non-solicitation clauses

also need to be reasonable to be found enforceable, although it is generally easier for such clauses to satisfy this test.

Cancellation of an offer (*naitei-torikeshi*)

It is considered that once an employer has made a formal offer of employment to a prospective employee and the prospective employee has accepted it, a certain employment relationship has been established, even if the employee has not yet started work. Although employers have a right to cancel an accepted offer before the actual start of employment, a court may treat such a cancellation as invalid or illegal if it determines that there were no reasonable grounds for cancelling the offer. A cancellation can be considered 'reasonable', for example, if the prospective employee has provided material false information to the employer or if the firm is in financial difficulties that would justify a redundancy (see 'Redundancy' below).

Probationary period

It is permissible and customary in Japan to designate a fixed period of time from the starting date as a probationary period for a new employee. It will normally range from three to six months. During a probationary period, an employee can be dismissed on 'reasonable and socially acceptable' grounds. What is considered 'reasonable and socially acceptable' grounds for dismissal in a probationary period is construed relatively broadly compared with the dismissal of employees who are not in a probationary period (see 'Dismissal' below). Typical grounds that would be considered reasonable and socially acceptable are poor performance, behaviour issues, insubordination and lack of expertise. The duration and terms of a probationary period must be stipulated in the work rules. An employer can extend the probationary period for a reasonable period of time (eg three months) as long as the possibility of extension is stipulated in the work rules.

Work rules (*shuugyou kisoku*)

The importance of work rules

In Japan, most of the terms and conditions of employment are stipulated in work rules established by the employer. Work rules cover matters such as:

- working hours and breaks;
- holidays;
- wages (eg monthly salary, bonuses, retirement allowance etc);
- termination of employment;
- disciplinary actions; and
- other matters that apply generally to all employees at the workplace.

Provided that the terms and conditions stipulated in the work rules are 'reasonable' and the employees have been informed of the contents of the work rules, the terms and conditions stipulated in the work rules will form the terms and conditions of employment for all employees who are subject to the work rules. Although it is possible to stipulate the terms and conditions of employment in individual employment contracts or offer letters, it is important to note that the terms and conditions in the work rules will take precedence over any terms and conditions in an individual employment contract or offer letter if the terms and conditions in the work rules are more favourable to the employee.

Establishing and filing the work rules

All employers who continuously employ 10 or more employees at a workplace must:

- establish work rules;
- obtain a written opinion on the work rules from a labour union or employee representative representing the majority of the employees in the work place;
- file the work rules with the relevant Labour Standards Inspection Office with the written opinion from the labour union or employee representative; and
- inform the employees of the contents of the work rules.

It should be noted that the written opinion is an 'opinion', not a 'consent'. The same procedure must be followed in making any amendments to the work rules.

Amending the work rules

An employer can unilaterally amend the terms and conditions of employment of all the employees in a workplace by amending the applicable work rules. An amendment to the work rules will be binding on all employees if it is favourable to them or, if it is unfavourable, it is regarded

by the court as reasonable. If the amendment is unfavourable to the employees and it cannot be considered 'reasonable', it is not effective with respect to employees who have not consented to it. The following factors will be considered in determining whether an amendment is 'reasonable' and are therefore a helpful guide to the steps an employer can consider when making an amendment:

- how detrimental the amendment would be to the employees;
- the extent to which it was necessary for the employer to make the amendment;
- the reasonableness of the amended terms and conditions (eg whether the contents of the amendment are reasonable, whether any improvements have been made to other terms and conditions, whether any measures have been taken to mitigate the adverse effects on the employees etc);
- the negotiation process with the employees (eg whether the employer has engaged in good faith negotiations with the employees or the labour unions representing the employees, what proportion of the employees have consented to the amendment etc); and
- other relevant matters (eg market standard in relation to the amended terms and conditions etc).

The amended work rules must be filed with the relevant Labour Standards Inspection Office with the written opinion from the labour union or employee representative.

Wages

General principles regarding the payment of wages

The wages of Japan-resident employees must be:

- paid in Japanese yen in cash;
- paid directly to each employee;
- paid in full (eg an employer cannot 'set off' its obligation to pay wages to an employee against any monetary obligations that the employee may owe to the employer, unless the employee specifically consents to such set-off); and
- paid at least once a month on a specified date.

Working hours

Statutory requirements

Under the Labour Standards Law, the general principle is that employers cannot require employees to work for more than eight hours per day and 40 hours per week. Employers must provide employees a 45-minute break if the daily working hours exceed six hours and a one-hour break if the working hours exceed eight hours (see below). Employers must also provide employees at least one rest day per week.

Overtime work

Employers can require employees to work in excess of the statutory maximum working hours (ie eight hours per day and 40 hours per week) and require employees to work on rest days if they enter into a so-called 'Article 36 Agreement' (*saburoku kyoutei*) with a labour union or employee representative representing the majority of the employees in the workplace and file the Article 36 Agreement with the Labour Standards Inspection Office. The Article 36 Agreement must set out the maximum hours of overtime work. Under current administrative guidelines, the maximum hours cannot exceed 45 hours per month (although the Article 36 Agreement can stipulate that this maximum can be exceeded under exceptional circumstances that are specified in the agreement). It is extremely important for employers to enter into an Article 36 Agreement because making employees work in excess of the statutory maximum working hours without one is a criminal offence.

Overtime work allowance

Under the Labour Standards Law, employers are required to pay 125 per cent of the employee's base hourly wage for overtime work and 135 per cent for rest-day work. Employers are further required to pay an additional 25 per cent for night-time work (ie work undertaken between 10pm and 5am). For example, if an employee works overtime at night, he or she is entitled to 150 per cent of his or her base hourly wage.

Under the amendment to the Labour Standards Law that will become effective on 1 April 2010, overtime work exceeding 60 hours per month must be compensated at a rate of at least 150 per cent of the employee's base hourly wage or by additional paid leave in lieu of payment of overtime allowance (permissible only for the additional 25 per cent portion). Additional paid leave in lieu of overtime payment can be used only if the employer agrees so with a labour union or an employee representative representing the majority of the employees in the workplace. Small and mid-sized firms will be exempt from this new regulation for a period of time (the length of which is not yet known). Also, under the amended law, overtime work of between 45 and 60 hours per month will be required to be compensated at a rate to be agreed separately between the employer and a labour union or employee representative representing the majority of the employees in the workplace. Companies must endeavour to set this rate at over 125 per cent.

Exemption for managerial employees (*kanri-kantokusha*)

Managerial employees are exempt from the regulations on working hours. In other words, employers can require managerial employees to work in excess of the statutory maximum working hours and on rest days without entering into an Article 36 Agreement and these employees are not entitled to overtime work allowance or rest day work allowance. Managerial employees are, however, entitled to night-work allowance. In determining whether an employee is a managerial employee, the court will generally consider the following three factors:

- whether the employee has authority to participate in management decisions;
- whether the employee has discretion in deciding his or her own working hours; and
- whether the employee is adequately compensated as a managerial-level employee.

Generally speaking, the courts tend to examine these three factors strictly. For example, under court precedents, store managers who have the authority to manage their own stores but not to participate in the firm's overall management decisions have been denied managerial employee status. In most situations, this is obviously a very difficult standard to meet. The Labour Standards Inspection Offices generally put more weight on the second and third factors and take a different approach to the first factor (participation in management decisions). In relation to this factor, the Labour Standards Inspection Offices tend to focus on whether the employee has authority to manage people, rather than the authority to participate in overall management decisions.

Holidays and leave

Annual paid leave

Under the Labour Standards Law, an employee who has been continuously employed for six months and whose attendance has been at least 80 per cent of the total number of working days during that period is entitled to a minimum of 10 days' annual paid leave. The number of minimum days' entitlement for annual paid leave increases with the length of employment to a maximum of 20 days a year. Although employees who have accrued annual paid leave are free to use their leave whenever they wish, employers may exercise their right to have employees change their leave schedules if the proposed schedule would interfere with the normal conduct of business. Any unused annual leave can be carried forward for a maximum of one year. It is illegal for employers to unilaterally 'buy out' annual leave instead of granting the leave.

Under the amendment to the Labour Standards Law that will become effective on 1 April 2010, an employer may agree with a labour union or an employee representative representing the majority of the employees in the workplace that employees may take paid leave on an hourly basis up to the number of hours equivalent to five days.

Maternity leave, child care leave and family care leave

A pregnant employee is entitled to maternity leave for a period of six weeks before the expected date of birth and eight weeks after the birth. Employers are prohibited from dismissing employees on maternity leave regardless of the reason claimed for dismissing them. An employee who lives with and is raising a baby under one year of age is eligible for child care leave. In addition, employees are eligible for family care leave of up to 93 days to care for a family member. These absences can be without pay and, if so, a certain percentage of the employee's base salary will be paid under the national health insurance scheme or unemployment insurance scheme.

Personnel assignments

Promotions and demotions

Generally speaking, employers have broad discretion in promoting and demoting employees. Demotions that are used as a means of 'disciplinary action' are subject to separate restrictions. An employer's decision will be deemed illegal if the decision is regarded as discriminatory (eg discrimination based on nationality, creed, social status, sex or union membership) or is regarded as abusive.

Transfers to a different role/department or workplace (*haiten*)

Generally speaking, employers have authority to transfer employees to a different role, department or workplace, as long as the right is stipulated in the work rules. Employers are generally granted broad discretion in ordering such transfers. However, a transfer order will be illegal if it is regarded by the court as abusive. Whether a transfer order is abusive will be determined by evaluating the business necessity for it and the disadvantages inflicted on the employee (eg transferring an employee if there is no particular business reason or transferring an employee who needs to care for a family member to a far-away workplace will be regarded as being abusive). If it is clear from the employment contract that the employee was hired for a specific role, department or work place, then the employee's consent is required to transfer the employee to a different role, department or workplace.

Secondment to group companies (*shukkou*)

In Japan, it is quite common for employees to be seconded to a group company of the employer. A secondment involves a temporary assignment of an employee from his or her regular employing entity to a recipient entity, while maintaining employment with the regular employing entity. The terms and conditions of the secondment will be governed by the secondment agreement entered into between the regular employing entity and the recipient entity. As long as the work rules provide that an employee may be seconded to a group company as the business requires, employee consent will not be required to second the employee to a group company. Again, an employer's secondment order will be illegal if it is regarded by the court as abusive.

Transfers to group companies (*tenseki*)

It is also not uncommon for employees to be transferred to a group company. In the case of a transfer, the employment relationship between the employee and the original employing entity will end and the employee will enter into a new employment contract with the recipient entity. Even if the work rules provide that an employee may be transferred to a group company if the business requires it, the employee's consent will be required to transfer the employee because a transfer (unlike a secondment) involves a change in the employing entity.

Termination of employment

Resignation

It is customary for employers to stipulate in the work rules that employees must give 30 days' notice of resignation. Any notice period that is longer than this is likely to be held invalid unless the employer can demonstrate that it has a genuine business need to require such a longer notice period (eg requiring certain limited high-level employees who have access to highly sensitive or confidential information to give 60 days' notice).

Retirement

It is common for employers to stipulate a retirement age in the work rules. Under the Law concerning the Stabilisation of Employment of Older Persons, it is prohibited to set the retirement age at less than 60 years of age. Also, if the retirement age is set at less than 65 years of age, the law requires employers to establish a system to re-employ employees who wish to work past the retirement age until they reach 65 years of age.

Dismissal

Reasonable and socially acceptable grounds for dismissal

Under Japanese law, although the general rule is that employers have a right to dismiss employees, a dismissal will be regarded as an 'abuse of rights' and thus invalid if the court determines that the dismissal lacks 'reasonable' grounds and is not 'socially acceptable'. Typical grounds that would be considered as 'reasonable and socially acceptable' include:

- a loss of or significant lack in ability/capability to perform work duties (eg non-work-related sickness or injuries);
- employee misconduct;
- insubordination;
- provision of material false information about one's background;
- poor performance; and
- behaviour issues.

Note that it is generally difficult to convince a court that an employee's performance was so poor as to merit dismissal unless the performance was considerably below all standards and well documented. Grounds for dismissal must be stipulated in the work rules.

Seeking voluntary resignation

Given that it is relatively difficult to convince the courts of the existence of 'reasonable and socially acceptable' grounds for dismissal – and to avoid legal disputes – it is customary in Japan for employers to seek voluntary resignations from the employees they wish to leave. While it is not a legal requirement, employers may offer payment of a certain amount of money to encourage certain employees to resign voluntarily. The size of the package would generally be determined by considering the level of risk the employer

would be exposed to if the employer were to dismiss the employee and the employee were to file a lawsuit disputing the dismissal.

Redundancy (*seiri kaiko*)

The same general rules will be applied in a redundancy situation – ie an employer must demonstrate ‘reasonable and socially acceptable’ grounds to carry out redundancies. The courts generally consider the following four conditions in determining whether there are ‘reasonable and socially acceptable’ grounds to dismiss employees in a redundancy scenario:

- whether there is a genuine business necessity for the redundancy (eg the business has been making a loss for a number of years);
- whether the employer has made efforts to avoid dismissals (eg exhausting other cost-cutting measures, considering placing the redundant employees in different positions/divisions, seeking voluntary resignations etc);
- whether reasonable selection criteria were used in determining who should be dismissed (eg criteria based on performance, length of service, difficulty of finding alternative employment etc); and
- whether the employer has consulted in good faith with the employees (eg informing the relevant employees of reasons for the redundancy and engaging in good faith negotiations with each relevant employee on matters such as whether alternative roles are available within the firm and, if not, the reason for that).

The court would generally consider these four conditions in a comprehensive manner to determine whether the dismissal, as a whole, can be regarded as being based on ‘reasonable and socially acceptable’ grounds. In this sense, the four conditions may be interrelated to an extent (eg if the business need for the dismissal is very strong, the obligation to make efforts to avoid dismissal may be less burdensome, whereas if the business need is weak, the standard required for satisfying the other conditions would be higher).

Again, to avoid the uncertainty inherent in a court decision in respect of redundancies and negative publicity, it is usual for Japanese companies to first seek voluntary resignation from the employees targeted for redundancy with an offer of a reasonable redundancy package.

Disciplinary dismissal (*choukai kaiko*)

A dismissal may also be used as a means of disciplinary action. To enable a firm to take disciplinary action against an employee, the grounds and means for disciplinary action must be stipulated in the work rules. Typical grounds include:

- provision of material false information about one’s background;
- tardiness or absence without notice;
- insubordination;

- disrupting the firm's business; and
- breach of work rules and other internal rules.

Typical means for disciplinary action are:

- written reprimand;
- reduction of base salary;
- suspension;
- demotion;
- resignation instruction; and
- disciplinary dismissal.

A disciplinary action will be illegal if the court determines that the means of disciplinary action was not appropriate in light of the type and degree of, and circumstances surrounding, misconduct.

In the case of a disciplinary dismissal, it is common for the work rules to provide that retirement allowance (ie the allowance stipulated in the work rules to be paid upon termination of employment, the size of which is typically calculated based on the relevant employee's years of service and base pay) will not be paid to the employee. Given such economic disadvantages and the 'stigma' that the employee will suffer from being disciplinarily dismissed, disciplinary dismissals are subject to strict court scrutiny if the employee disputes the validity of the dismissal. As such, if there are doubts over the validity of a disciplinary dismissal, it is advisable to dismiss the relevant employee through a normal dismissal procedure, rather than using a disciplinary dismissal.

Notice requirement

Employers must give at least 30 days' notice of dismissal or provide payment of base salary in lieu of notice. This also applies to disciplinary dismissals, although an employer can dismiss an employee without notice (or payment in lieu of notice) if it obtains approval from the Labour Standards Inspection Office. It normally takes at least a week to obtain such an approval.

<p>ABU DHABI The Avenue Business Centre PO Box 33763 Abu Dhabi T + 971 2 412 4105 F + 971 2 412 4111</p>	<p>BRUSSELS Bastion Tower Place du Champ de Mars/ Marsveldplein 5 B-1050 Brussels T + 32 2 504 7000 F + 32 2 504 7200</p>	<p>HANOI #05-01 International Centre 17 Ngo Quyen Street Hanoi T + 84 4 38247 422 F + 84 4 38268 300</p>	<p>NEW YORK 520 Madison Avenue 34th floor New York, NY 10022 T + 1 212 277 4000 F + 1 212 277 4001</p>
<p>AMSTERDAM Strawinskylaan 10 1077 XZ Amsterdam T + 31 20 485 7000 F + 31 20 485 7001</p> <p>Mailing address PO Box 75299 1070 AG Amsterdam</p>	<p>COLOGNE Heumarkt 14 50667 Cologne T + 49 221 20 50 70 F + 49 221 20 50 79 0</p>	<p>HO CHI MINH CITY #1108 Saigon Tower 29 Le Duan Boulevard District 1 Ho Chi Minh City T + 84 8 38226 680 F + 84 8 38226 690</p>	<p>PARIS 2 rue Paul Cézanne 75008 Paris T + 33 1 44 56 44 56 F + 33 1 44 56 44 00</p>
<p>Mailing address PO Box 75299 1070 AG Amsterdam</p>	<p>DUBAI The Exchange Building 5th floor Dubai International Financial Centre Sheikh Zayed Road PO Box 506 569 Dubai T + 971 4 5099 100 F + 971 4 5099 111</p>	<p>HONG KONG 11th floor Two Exchange Square Hong Kong T + 852 2846 3400 F + 852 2810 6192</p>	<p>ROME Piazza di Monte Citorio 115 00186 Rome T + 39 06 695 331 F + 39 06 695 33800</p>
<p>BAHRAIN Almoayyed Tower 21st floor Seef District PO Box 18259 Bahrain T + 973 1 756 7900 F + 973 1 756 7901</p>	<p>DÜSSELDORF Feldmühleplatz 1 40545 Düsseldorf T + 49 211 49 79 0 F + 49 211 49 79 10 3</p> <p>Mailing address Postfach 10 17 43 40008 Düsseldorf</p>	<p>LONDON 65 Fleet Street London EC4Y 1HS T + 44 20 7936 4000 F + 44 20 7832 7001</p>	<p>SHANGHAI 34th floor Jinmao Tower 88 Century Boulevard Shanghai 200121 T + 86 21 5049 1118 F + 86 21 3878 0099</p>
<p>BARCELONA Mestre Nicolau 19 08021 Barcelona T + 34 93 363 7400 F + 34 93 419 7799</p>	<p>FRANKFURT AM MAIN Bockenheimer Anlage 44 60322 Frankfurt am Main T + 49 69 27 30 80 F + 49 69 23 26 64</p>	<p>MADRID Fortuny 6 28010 Madrid T + 34 91 700 3700 F + 34 91 308 4636</p>	<p>TOKYO Akasaka Biz Tower 36F 5-3-1 Akasaka Minato-ku Tokyo 107-6336 T + 81 3 3584 8500 F + 81 3 3584 8501</p>
<p>BEIJING 3705 China World Tower Two 1 Jianguomenwai Avenue Beijing 100004 T + 86 10 6505 3448 F + 86 10 6505 7783</p>	<p>HAMBURG Alsterarkaden 27 20354 Hamburg T + 49 40 36 90 60 F + 49 40 36 90 61 55</p> <p>Mailing address Postfach 30 52 70 20316 Hamburg</p>	<p>MILAN Via dei Giardini 7 20121 Milan T + 39 02 625 301 F + 39 02 625 30800</p>	<p>VIENNA Seilergasse 16 1010 Vienna T + 43 1 515 15 0 F + 43 1 512 63 94</p>
<p>BERLIN Potsdamer Platz 1 10785 Berlin T + 49 30 20 28 36 00 F + 49 30 20 28 37 66</p>	<p>MOSCOW Kadashevskaya nab 14/2 119017 Moscow T + 7 495 785 3000 F + 7 495 785 3001</p>	<p>MUNICH Prannerstrasse 10 80333 Munich T + 49 89 20 70 20 F + 49 89 20 70 21 00</p>	<p>WASHINGTON 701 Pennsylvania Avenue, NW Suite 600 Washington, DC 20004-2692 T + 1 202 777 4500 F + 1 202 777 4555</p>
<p>BRATISLAVA Laurinská 12 81101 Bratislava T + 421 2 5926 3111 F + 421 2 5926 3602</p>			<p>25116</p>