

Using fixed term contracts of employment

An overview of the legal issues involved in using fixed term contracts of employment

Introduction

Fixed term contracts used to be very popular with employers because:

- employers could treat fixed term employees differently to permanent employees with regards to pay and benefits - often employing individuals on a fixed term basis was a cheaper option
- employers could ensure that fixed term contracts of employment contained clauses whereby the fixed term employees waived their rights to bring claims for unfair dismissal and statutory redundancy payments

Recently, both these advantages have been removed because of new legislation. In fact in many cases, there is no advantage now in using a fixed term contract rather than a permanent one (also known as a contract of indefinite duration).

Types of fixed term contract

There are three basic types of fixed term contracts of employment:

- **specific period contract** - a contract of employment which lasts for a specific finite duration which is fixed in advance (even if the contract also contains notice provisions) for example where an employee is employed for a set period of say 6 months or 2 years
- **specific task contract** - a contract of employment which is intended to terminate on the completion of a particular task, for example where an employee is employed to complete a particular project and his/her employment will end when the project is finished
- **specific event contract** - a contract which is intended to terminate on the occurrence or non-occurrence of a specific event, for example where an employee's employment will terminate if the funding grant making the employment possible is not renewed

Fixed Term Employees (Prevention Of Less Favourable Treatment) Regulations 2002

These regulations were introduced with effect from 1 October 2002 and include a number of particularly significant changes.

Equal treatment principle

The regulations introduce the principle that employees employed under one of the three types of fixed term contract (known as fixed term employees) should not be treated less favourably than comparable permanent employees with regard to certain aspects of their employment.

Scope of the equal treatment principle

The equal treatment principle extends to ensuring equal treatment for fixed term employees in the relation to the following:-

- their terms and conditions of employment
- being subjected to any detriment by their employer
- any service qualification relating to any particular condition of service for example the employer must not have different rules for fixed term employees and permanent employees as to how long they need to have been employed before qualifying for enhanced holiday entitlement
- the opportunity to receive training
- the opportunity to secure permanent employment with the employer¹

unless the employer can justify the difference in treatment on valid objective grounds.

This principle means in general terms that fixed term employees can not be paid less than equivalent permanent employees and must be given the same benefits. In addition, your policies must apply equally to permanent and fixed term employees, including your disciplinary and grievance procedures.

The extent of the equal treatment principle has been considered by the Court of Appeal in the case of the *Department of Work and Pensions v Webley* [2005] IRLR 288. In this case, the Claimant was employed under a series of fixed term contracts which came to a natural end after she had accumulated fifty one weeks' continuous service. The Claimant sought to argue that her employer had chosen to dismiss her, rather than a permanent employee, and that this constituted less favourable treatment on the grounds of her fixed term employee status.

¹ In relation to the last bullet point, the regulations specifically provide that fixed term employees must be informed of all available permanent vacancies which the employer may have. It is important for employers to ensure that they have mechanisms whereby fixed term employees are advised of permanent vacancies.

Although in the initial stages of the case (at the Employment Tribunal and the EAT stages), the Claimant was successful, the Court of Appeal upheld the appeal by the DWP. The Court of Appeal held that the essence of a fixed term contract is that it is intended to come to an end at the expiry of the fixed term. Lord Justice Wall said in the case that "the termination of a [fixed term] contract by the simple effluxion of time cannot, of itself, constitute less favourable treatment by comparison with a permanent employee."

The need for a comparator

Like individuals bringing a claim under the Equal Pay Act, in order to bring a claim under the regulations, a fixed term employee is required to establish that they are being treated less favourably than a comparator. Under the Equal Pay Act the comparator is a person of the opposite gender doing the same or similar work. Under the regulations, the comparator needs to be an employee employed by the same employer and who is engaged in the same or broadly similar work as the fixed term employee, taking account where relevant, as to whether both employees have the same level of qualification, skills and experience.

Where possible the fixed term employee must compare him or herself with a permanent employee who works in the same part of the company. Where no suitable comparator exists at the fixed term employee's place of work however, a comparison can be made with a permanent employee working in another part of the company.

Defences

A further hurdle for the fixed term employee to overcome relates to the potential defences which can be argued by his or her employer.

(a) Whole package

When considering whether a fixed term employee is actually being treated less favourably than a comparable permanent employee, the entire package of each employee will have to be considered. This means that if an employer can establish that the terms of the fixed term employee's contract of employment, taken as a whole, are at least as favourable as the terms of the comparable permanent employee, there will be no difference in treatment. For example, if a fixed term employee is excluded from an employer's pension scheme, but earns extra salary over and above the rates paid to permanent employees, thus enabling him or her to contribute to a private pension plan, this will be acceptable.

(b) Pro-rata

In addition, the regulations allow for the operation of a pro-rata principle. This means that it will be acceptable for employers to give a fixed term employee a proportion of the pay or benefits paid to a permanent employee providing the proportion is reasonable in all the circumstances bearing in mind the length of service of the fixed term employee and the basis on which the pay or benefit is conferred. In cases, where the pro-rata principle operates fairly less favourable treatment will not be established.

(c) Justification

Even if less favourable treatment is established however, employers will be able to argue that the difference in treatment is justified. Under the regulations, provided any differences in treatment between fixed term and permanent employees are for sound business reasons employees' claims will fail.

Written complaint procedure

Before bringing a formal claim, fixed term employees will be well advised to write to their employers complaining of unequal treatment. The regulations specifically require an employer who receives such a complaint to reply in writing within 21 days setting out the reasons for any difference in treatment between fixed and permanent employees. The reply is admissible in any subsequent tribunal proceedings. The tribunal may draw appropriate inferences from any failure to provide a reply so employers should always answer, no matter how spurious a potential claim may appear to be. The reply should not be evasive or equivocal either as this will also be likely to lead the tribunal to suspect the worst.

Protection from victimisation

The regulations also protect fixed term employees who complain of less favourable treatment from victimisation. If a fixed term employee who makes a complaint about unequal treatment subsequently suffers a detriment or is dismissed for doing so, the employee will also be entitled to bring a claim. A dismissal in this circumstance will be automatically unfair if the reason for the dismissal is the employee's previous complaint.

Limit on successive fixed term contracts

Under the regulations, if a fixed term employee is continuously employed for a period of four years or more (beginning any time after 10 July 2002) through a series of fixed term contracts (where there are no gaps), the employee will automatically be converted into a permanent employee, unless the employer can justify keeping the employee on a fixed

term basis. It will still be possible to enter into single fixed term contracts which are intended to last for four years or more however.

Waivers

As stated above, it used to be possible for employees on fixed term contracts to agree to waive away their rights to bring an unfair dismissal claim and this was one, if not the main reason for using a fixed term contract. This was changed with effect from 25 October 1999 by the Employment Relations Act 1999.

Many fixed term contracts still contain waivers against unfair dismissal, but these will now be invalid unless the contract began or was renewed before 25 October 1999.

The waiver in relation to redundancy payments lasted a little longer than the unfair dismissal waiver, but has now been removed by the regulations. Waivers of the right to receive a redundancy payment will now be invalid unless the contract began or was renewed before 1 October 2002.

NB If you are having to pay a redundancy payment to an employee at the end of a fixed term contract, you must take account of any period of continuous employment from a previous fixed term contract, even if earlier contracts included waivers.

Bringing a fixed term contract to an end

Contractual position

A fixed term contract can lawfully be brought to an end in four ways:

(a) naturally - depending on the type of fixed term contract in place, the contract will come to a natural end because either:

- for specific period contracts - the specific period of time for which the contract was specified to last has expired;
- for specific task contracts - the specific task which the employee was employed to complete has been completed; or
- for specific event contracts - the specific event has occurred (or not occurred as the case may be) which was intended to bring the contract to an end.

- (b) through either party giving the other notice - this is only possible if the fixed term contract contains a notice provision allowing the parties to terminate it early by giving notice - if there is no notice provision, the contract will continue even if one party purports to give notice to the other.
- (c) breach - if either party commits a fundamental breach of the contract the other party can treat the contract as having been terminated.
- (d) by agreement - the parties can voluntarily agree to end the contract at any time. The agreement must be genuine and not imposed by one party on the other to be valid.

The statutory position: unfair dismissal

In order to bring an unfair dismissal claim, an employee must first establish that he or she has been dismissed by his/her employer.

Although the ending of the contract in situation (a) above (where the fixed term contract comes to its natural end) is lawful in terms of the basic principles of contract law, the statutory position has to be considered. Provisions in the Employment Rights Act 1996 provide that if a fixed term contract is not renewed, the failure to renew is deemed to be a dismissal for the purposes of unfair dismissal legislation.

In the case of situation (b) where notice is given by the employer, this obviously constitutes a dismissal.

In the case of situation (c) where the employee resigns in response to a fundamental breach by the employer this will also constitute a dismissal through the legislative provisions which create the concept of constructive dismissal; where the employer dismisses the employee for gross misconduct, this is obviously a dismissal.

If at the time that the fixed term contract comes to an end, the employee has 1 or more year's service with the employer, he/she will be entitled to bring a claim of unfair dismissal to an employment tribunal. If the employee can establish that the reason for the termination of his/her employment under the fixed term contract is one of the automatically unfair reasons, there will be no length of service required in order to bring a claim.

In addition, regardless of the reason for the dismissal or the employee's length of service, the statutory dismissal and disciplinary procedure ("DDP") will apply in situations (a) and (b) above. This requires the employer to comply with three basic steps:

- to write to the employee explaining the employer's plans to dismiss him or her, whether this is a direct dismissal (a) or because the employer is not renewing the employee's fixed term contract (b);

- to meet with the employee to discuss the dismissal and the reason for it; and
- to offer the employee a right of appeal against the decision to dismiss him or her.

If the employee has more than 1 year's service and the employer fails to comply with the requirements of the DDP, the employee will be deemed to be unfairly dismissed. If the employee has less than 1 year's service, he or she will not normally be eligible to bring an unfair dismissal claim. However the employer's failure to follow the DDP could lead to the employee getting increased compensation if the dismissal is discriminatory on one of the grounds prohibited by law.

The statutory position: redundancy

If at the time that the fixed term contract comes to an end, the employee has 2 or more years' service with the employer and if the circumstances fall into the legal definition of a redundancy situation, he or she will be entitled to a statutory redundancy payment (see further below).

Avoiding claims for unfair dismissal

Employers who wish to avoid claims for unfair dismissal from fixed term employees have three possible choices:

- employ people on short contracts of less than 1 year;
- ensure that when you dismiss, you do it fairly; or
- avoid a dismissal situation altogether by bringing the employment relationship to an end through agreement.

Short contracts

If an employee does not accrue 1 or more years' continuous service with his/her employer, he or she will not be entitled to bring a claim for unfair dismissal, when the employer terminates the employment relationship. The only exception to this is if the employee can demonstrate that he or she has been dismissed for one of the "automatically unfair" reasons.

Employing an individual on a short contract is fine if you only require their services for a short period. However this is no use where you need them for longer than 1 year. However, the option of using short contracts has led to a number of employers trying to get around the unfair dismissal legislation by using a series of short fixed term contracts with gaps in between them.

The Employment Rights Act 1996 includes provisions which state how an employee's period of continuous service must be calculated. The general rule is that only weeks when the employee has a contract of employment (whether verbal or in writing) with the employer count towards continuous employment². Any weeks where there is no contract will cause there to be a gap. Continuity is preserved during leave for sickness, holiday and other forms of statutory leave such as maternity and paternity leave because the employment relationship continues during the period of leave.³

Under the general rule, if you employ someone on a fixed term contract which comes to an end and then leave a break of at least two clear weeks before you re-employ them, the employee's continuous service will be broken. There are two exceptions to the general rule however, which mean that this is not always the case. These exceptions are:

- (a) where the reason for the employee's absence at work is due to a temporary cessation of work; or
- (b) where there is an arrangement or custom under which the individual is regarded as continuing as an employee, despite not having a contract of employment.

Temporary cessation of work

The Employment Rights Act 1996 provides that if the reason for the employee's break in employment is due to a temporary cessation of work, continuity of service should not be broken, but should continue⁴. The obvious application of this provision is where there is an involuntary suspension of normal operations for some emergency reason. The typical example is where an employer has to lay off a number of employees because work suddenly falls off, but is able to re-employ them a short time later.

This exception to the general rule has been applied in a situation which is less obvious however. This occurred in the case of *Ford v Warwickshire County Council* [1983] IRLR 126.

In this case a teacher was employed under a fixed term contract which lasted for the length of the academic term only (i.e. September to June). The teacher did not have a contract of employment during the summer holiday. For a number of years however the teacher was re-employed at the start of the new autumn term, again on the same basis. When after several years of this arrangement, Warwickshire County Council decided not to renew the teacher's contract, the teacher brought a claim of unfair dismissal. Warwickshire County Council argued that the teacher did not have more than 1 year's continuous services because each summer holiday constituted a break in continuity. The teacher won however because the House of Lords, who heard the case, felt that the summer holidays constituted a temporary cessation in the employer's activities and applied exception (a).

² s.212(1) Employment Rights Act 1996

³ s.212(3)(a) Employment Rights Act 1996

⁴ s.212(3)(b) Employment Rights Act 1996

Arrangement or custom

The second exception is where there is in place an arrangement or custom under which the employee is treated as having continuous services, despite having no contract of employment.⁵ An obvious example is where an employer allows an employee to take a period of long term unpaid leave, but agrees with him or her that when the leave is over the employee can return to work.

In the case of *Booth v United States of America* [1999] IRLR 16, the Employment Appeal Tribunal considered the application of this exception. In this case, the applicants were maintenance workers employed by the US army on UK bases. The US army employed the individuals on a series of fixed term contracts with gaps in between. The employer's express and deliberate intention was to avoid the employees ever accruing enough continuous service to be eligible to bring claims for unfair dismissal.

The employees argued that the gaps between their contracts should be ignored for the purposes of calculating their period of continuous employment. They claimed that when they returned after the gaps they were given the same employment number, tools, clothing and lockers and that surely this was an arrangement or custom whereby their continuity of employment should be preserved.

The EAT disagreed and found that the employer was perfectly entitled to arrange its affairs in this way and avoid the application of the unfair dismissal legislation. The EAT said that for an arrangement or custom to be in place, some discussion or agreement in advance of the break must occur to the effect that the parties regard the employment relationship as continuing. Without this continuity will not be preserved. In this case it was significant that the workers had to reapply for their positions. There was no agreement in advance that they would be automatically re-employed.

The EAT also considered whether exception (a) (temporary cessation of work) could be applied in this case, but found that it did not because there was no cessation of work. There was no period when work ceased. Whilst one of the workers was on a break, the others continued. The situation of a break for the summer holidays as in the *Ford* case simply did not arise.

summary

Whilst it is tempting to think that employing individuals on short term contracts is the answer to avoiding unfair dismissal claims, if you need someone to carry out a job for a year or more, problems arise.

In rare circumstances, you may be able to rely on an arrangement similar to that operated in the *Booth* case. Care must be taken however to avoid the circumstances mirroring the *Ford* case. It is unlikely that the *Booth* reasoning would work

where there is a unique role, as any gap will constitute a cessation of work. The *Booth* reasoning is only likely to be successful where there are several employees carrying out the same role and where the gaps between their contracts occur at different times.

In addition, the DDP applies regardless of an employee's length of service so you need to be alert to the fact that you need to follow this procedure.

Ensuring the dismissal is fair

To ensure that the dismissal is fair, you will need to be able to establish that:

- you had a fair reason for dismissing the employee or failing to renew his/her fixed term contract;
- you followed the DDP;

and

- taking into account all the circumstances (including the size and administrative resources of your company and the procedure you followed) you acted reasonably in treating the reason as a sufficient reason for dismissal.

There are a limited number of "fair" reasons for dismissing an employee (i.e. failing to renew his/her fixed term contract). The main fair reasons that can be relied upon are:-

- misconduct
- capability
- redundancy
- some other substantial reason of a kind such as to justify the dismissal of an employee holding the position which the employee held ("SOSR")

Misconduct

An employee's misconduct constitutes a fair reason for his/her dismissal. However, in order to ensure that the dismissal is fair, the employer will need to demonstrate that it has followed a fair disciplinary procedure under which (unless the misconduct is gross misconduct) the employee has been given a series of prior warnings.

⁵ s.212(3)(c) Employment Rights Act 1996

Although misconduct may be used as a reason to justify a dismissal during the continuation of a fixed term contract, it will be very rare, if ever, that the circumstances of a case will support this being a reason for failing to renew a fixed term contract. This is because it is highly unlikely that the timing of the misconduct and progress of the disciplinary procedure will match the timing of the natural end of the fixed term contract.

Although it is unlikely that you will be able to justify a failure to renew a fixed term contract because of misconduct, you should not ignore this reason. If an employee's conduct is not meeting the required standard, you should initiate appropriate procedures to deal with it.

Incapability

An employee's incapability to perform his or her role to the employer's required standard constitutes a fair reason for the employee's dismissal. As with misconduct dismissals, in order to ensure a dismissal for incapability is fair, the employer must comply with certain procedural requirements. These include informing the employee of his/her performance shortcomings and considering, in conjunction with the employee, whether these can be overcome with support, assistance and training. The employee should be given a reasonable period of time to improve. This is known as a process of performance management.

In the case of shorter fixed term contracts, there may be scope for using the length of the fixed term to guide the process of performance management. It is not inconceivable for the end of a fixed term contract to coincide with a final performance review of an employee. If the employee's performance weaknesses have been well documented and the employee has been given appropriate support as required but has not improved, this may justify your failure to renew the employee's fixed term contract.

The difficulty in relying on incapability comes however when the employee has been performing the same role satisfactorily for a significant length of time. It becomes very difficult to accuse the employee of being incapable at a later stage, unless there is an obvious deterioration in their performance.

It is unlikely, for example, that you would be able to rely on incapability to justify failing to renew a two year contract, as the employee will have been doing the job for too long. It is more likely that the process of performance management would last a maximum of a year.

Redundancy

One fair reason for failing to renew a fixed term contract is if the employer no longer has work for the employee to carry out either because:-

- the employee's job has disappeared through a restructuring process;
- the work carried out by the employee in his/her job is no longer required – this may be because the project the employee was employed to carry out is now complete or simply because you no longer need someone to do the employee's job; or
- the employer can no longer afford to employ the employee. Most likely because funding for the post has not been renewed.

In order to ensure that a dismissal for redundancy is fair (even in the case of a fixed term contract redundancy), the employer is expected to consult with the employee in advance of the end of the contract and where possible offer the employee alternative employment. This does not mean that the employer is obliged to create a vacancy for the employee, but if the employer has any existing vacancies for posts which the employee could perform, these should be offered to him or her. The employee should not have to compete for these existing vacancies, except with other employees who are being made redundant at the same time. These procedural requirements are very important and further advice should be sought.

The position of the employer, in relation to a tribunal believing the genuineness of the redundancy situation, will be helped if, at the outset of the employment, the employer made it clear to the employee that the post was not expected to continue indefinitely whether because of the uncertainty of future funding or because the role was to complete a particular project only. The fact that the employee was aware from the beginning of this possibility should also be raised during the consultation process.

If the employee has 2 or more years' service with the employer at the time that the fixed term contract comes to an end because of a redundancy situation the employee will be entitled to a statutory redundancy payment. A statutory redundancy payment is calculated on the basis of the employee's age, length of service and weekly pay. The only exception to this will be where the fixed term contract contains a term, agreed before 1 October 2002, waiving the employee's rights to a redundancy payment.

It is very important that if you envisage being unable to renew a fixed term contract in future because of uncertainty about future funding and that therefore the employee faces a possible redundancy situation, the cost of the statutory redundancy payment is taken into account. Similarly, if you are taking someone on for a particular project which will last for two years or more, you should factor in the cost of paying them a redundancy payment at the end of the project.

SOSR

One reason commonly relied on when terminating the employment of a fixed term employee is the “catch all” reason contained in the Employment Rights Act 1996, known as “SOSR”. This catch-all reason should be relied upon with caution as it is rare for tribunals to accept it without question. However, it is particularly useful in the context of using fixed term contracts where, for example a temporary employee has been engaged to provide cover for sickness absence or maternity leave. In this example, the employer continues to need an employee to undertake work and so does not have a genuine redundancy situation nor does the employer have grounds to dismiss for conduct/capability. However, the employer can fairly dismiss the temporary employee using this “catch-all” reason.

To ensure dismissal in this context is fair the DDP needs to be followed and the employer needs to consider the question of whether the temporary employee can be successfully redeployed before moving to dismissal.

agreement

The third way of avoiding an unfair dismissal claim when you bring a fixed term contract to an end, is to agree the termination with the employee concerned. This will avoid there having ever been a dismissal as the contract will have come to an end by agreement and not through one of the parties bringing it to an end.

The problem with this solution is that, unless the employee enters into a formal agreement called a Compromise Agreement with your organisation, his/her agreement may not prevent the employee submitting a subsequent claim of unfair dismissal to a tribunal and potentially arguing that he or she was given no choice regarding the end of his/her employment, but was forced into the agreement.

A Compromise Agreement is a formal agreement which can be entered into on termination of employment whereby an employee agrees to waive his or her rights to bring any statutory employment claims. For the agreement to be valid, certain conditions have to be met. The agreement has to be in writing. In addition the employee must have received independent legal advice by a qualified adviser. This is usually a solicitor, but may be a barrister or an appropriately qualified trade union official or CAB worker.

As entering into a Compromise Agreement means giving something up, i.e. the right to sue your former employer for unfair dismissal compensation, the employee will expect to be paid appropriate compensation through the agreement. Although when you first suggest a Compromise Agreement to an employee, he or she may be unaware of his/her rights and appear to be happy to settle for a small sum, this position may not last. As soon as the employee visits the independent adviser, you may find that the employee’s expectations of how much he/she should receive increase. This

can make entering into a Compromise Agreement an expensive business for an employer, depending on the degree of exposure it faces regarding the employee's potential unfair dismissal claim.

Employees with 4 or more years continuous service from 10 July 2002

Employers should be aware that under Regulation 8, fixed-term employees with four or more years of continuous employment who have their contracts renewed or are re-engaged on a new fixed-term contract, unless a further fixed-term contract can be objectively justified, are deemed to be employed on a permanent (or indefinite) contract. Only service since 10 July 2002 counts towards the calculation of four years' continuous service for these purposes. Therefore, fixed-term workers will start to gain permanent status under this rule from 10 July 2006.

summary

It should be clear from this guidance note that, where you anticipate the employment relationship will last more than 1 year, there is now very little advantage in employing someone on a fixed term basis rather than a permanent basis. A contract of indefinite duration can be brought to an end by giving an employee the correct notice at any time. In most cases, this may well be as administratively convenient as employing the individual on a fixed term basis with a contract that is due to come to a natural end.

The only significant advantages of employing an individual on a fixed term basis would appear to be:

- being able to avoid giving notice or paying in lieu of notice; and
- as a useful way of ensuring that both you and your employee's expectations of the future position are the same.

It is very important that when you wish to employ someone to work for you, you consider carefully the length of time for which you will need the individual, the type of arrangement which will be appropriate and whether you are likely to be exposed to a future unfair dismissal claim or obligation to pay a statutory redundancy payment.

This briefing note is intended solely as an overview of the law. It was last updated on 20 October 2005. No responsibility can be accepted for the completeness or accuracy of this briefing note and professional advice should be taken in relation to any specific problems.

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