

# Fixed-Term Contracts (India)

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A Practice Note setting out the key issues concerning fixed or definite-term employment contracts in India.

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An employer may want to employ an individual under a fixed or definite-term employment contract (FTC). However, there may be limitations and restrictions on when an FTC is permitted, what constitutes 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 India. 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.

## What is an FTC?

In India, an FTC is an employment arrangement where an employer employs an employee for a specific period and this employment automatically comes to an end when the fixed period expires. This applies unless the employment is terminated early or the parties agree to extend the arrangement, in which case the employment comes to an end on expiry of the extended term.

The leading principle and requirement for an FTC is that the individual is hired only for projects that are of a temporary nature. Examples of instances when an employer may employ a fixed-term employee include:

- To work on a time bound project.
- To replace a woman employee who is on maternity leave of 26 weeks.
- To cover a seasonal peak at work.

While phrases such as short-term employment or temporary employment are interchangeably used in the context of an FTC, the most commonly used phrase in India is fixed-term employment.

Fixed term employment is regulated by Indian labour laws in the Model Standing Orders framed under the *Industrial Employment (Standing Orders) Act, 1946* (SO Act) and the *Industrial Disputes Act, 1947* (IDA) which are the two main federal laws that govern working conditions for "workmen" (that is, excluding employees in managerial, supervisory, and administrative positions).

The Model Standing Orders under the SO Act is a standard document setting out the terms and conditions of employment (including classification of working relationship), and can be adopted by employers either:

- In their standard form.
- By amending without changing the substance.
- By amending to the benefit of the employees.

The Model Standing Orders define "fixed-term employment" as a class of employment "in which a workman has been engaged on the basis of a written contract of employment for a fixed period." This definition has also been adopted in the Model Standing Orders framed by certain states including Karnataka and Haryana. For example, the Model Standing Orders in Karnataka define "temporary workmen" as "workmen who have been engaged for work which is essentially of a temporary nature, likely to be finished within a limited period."

Similarly, the definition of an employee in some of the state specific Shops and Establishments Acts (SEAs) include persons engaged on "a contract basis."

*The Industrial Relations Code, 2020* (IR Code) and *the Code on Social Security, 2020* (SS Code) are expected to replace certain federal-level labour laws which lay down terms and conditions of employment in industrial establishments and undertakings and provide for social security benefits respectively. These codes define fixed-term employment as the "engagement of a worker on the basis of a written contract of employment for a fixed period." Although both the Codes have been notified, they are not yet in force and effective.

Regarding non-workmen (that is, employees in managerial, supervisory, and administrative positions) there is no specific law governing FTC arrangements. While the legal developments with respect to workmen under the SO Act are fairly new, the general principles of law governing FTCs are based on case law as upheld by Indian courts and apply to all employees, including workmen and non-workmen.

## Types of FTC

An FTC engagement may be structured as follows:

- An FTC that terminates on the expiry of the pre-determined term, without the need for any further notice.
- An FTC that permits the employer to terminate the FTC early on notice, failing which, the FTC shall terminate only on expiry of the term.
- An FTC that terminates on the expiry of the term unless the employer provides notice of its intention for extension of the arrangement for a fixed term.

## When an FTC is Permitted

There is no labour law provision restricting or strictly regulating fixed term employment. However, courts have held that fixed-term employees or temporary employees must be hired only for projects that are of a temporary nature or to serve as a temporary replacement. For example, seasonal work, a short finite project, or to cover the role of an employee that is absent for fixed temporary period (such as maternity leave).

Employers should also note the following:

- The employment contract should provide that the employment will come to an end on expiry of the set period or completion of the project, without any need for further notice (if applicable).
- The employment must end at, and not continue beyond, the set period, unless there is a cogent reason for extension. For example, if the employee has been engaged for a specific project and if such project gets extended for certain reasons.

Employers should have sufficient justification to employ an individual on an FTC as opposed to an ongoing employment relationship.

Several Supreme Court cases (for example: *S.M. Nilajkar vs. Telecom District Manager, 2003 II CLR; Ors. v. Telecom, District Manager, Karnataka ,AIR 2003 SC 3553*) and High Court cases (for example: *Chief Administrator, Haryana Urban Development Authority, Manimajra v. Industrial Tribunal, Rohtak, 1994 LLR 554*) have differentiated between genuine and non-genuine cases of fixed-term employment based on the factual situation in each case. Engaging workmen on an FTC basis for permanent positions (that is, not for a temporary project) is construed as an unfair labour practice under Indian labour laws. If a court finds an individual to be a de facto permanent employee (that is, not a fixed-term employee), the individual is entitled to:

- All salary and benefits as provided to permanent employees.
- Benefits that are linked to continuous service (such as severance and gratuity).
- Protection under the retrenchment related provisions under the IDA applicable only to workmen.

Previously, Indian courts deemed fixed term contracts illegal if:

- The contract was for a continuous business activity.
- The work did not have any fixed purpose.
- The contract was repeatedly renewed with or without notional breaks.
- The objective of the arrangement was to circumvent the retrenchment related protections and obligations under applicable law.
- The work done by the fixed-term employees was the same or similar to that of regular indefinite term workers and was not really connected to a particular project or a temporary requirement.

In cases where appointment of an employee was made for repeated periods in the same position with notional breaks, the court observed that the FTC arrangement was devised to circumvent the benefit of permanency of employment and therefore such practice was illegal (*Chief Administrator, Haryana Urban Development Authority, Manimajra v. Industrial; Tribunal, Rohtak, 1994 (69) FLR 35 (P&H HC)*).

In the event a court finds the purpose of engaging a workman on a fixed-term contract is not justified, the repercussions of such a finding may include:

- A determination that the expiry of the fixed term is in fact a case of retrenchment, warranting associated payment of retrenchment compensation.
- A determination that the expiry of the fixed term is a case of illegal termination of employment, which may lead to a direction of reinstatement of the concerned employee with or without backpay, compensation, or both.

(See *Advantages and Disadvantages of FTC*.)

A conviction of an employer for engaging in unfair labour practice under the IDA may lead to a penalty of up to six months' imprisonment, a fine of up to INR1000, or both.

## Advantages and Disadvantages of FTC

An employer usually prefers an FTC model if the nature of a job is temporary. FTCs are particularly appealing in sectors where workforce requirements or needs are not certain, are expected to be short-term, and employers can meet any immediate needs using the FTC model without the long-term commitment and costs associated with permanent arrangements.

A major attraction for employers to use FTCs is that under an FTC employers do not need to comply with the retrenchment related obligations under the IDA when the FTC terminates on the expiry of the term.

Retrenchment obligations apply generally when an employee (that is, a workman) is to be terminated on the grounds of redundancy or for any other reasonable cause other than misconduct (for example, poor performance).

However, an FTC is exempt from these obligations when the employment terminates on the expiry of the FTC, and the parties have the flexibility to specify how and when employment will end. For example, the FTC shall expire on a specific date or on completion of a specific event or project.

Although fixed-term employees are largely entitled to the same employee benefits as indefinite term employees, candidates may not prefer a fixed-term employment since a short-term contract may not be as attractive as a permanent and on-going position.

While there are benefits for an employer in using FTCs, there are also legal risks associated with an FTC if its use cannot be objectively justified by the employer. The IDA provides that hiring a workman temporarily and having them work for years with the object of depriving them the status and privilege of a permanent employee is considered as an unfair labor practice (*section 25T read with Fifth Schedule, IDA*).

In the Indian context, it is not uncommon for employers to use fixed-term employment arrangements to circumvent some of the provisions of law applicable to regular indefinite term employment arrangements. Therefore, historically such arrangements have been subject to scrutiny.

The courts have held that there should be a reasonable justification for hiring employees on a fixed-term basis, for example, the work required to be undertaken by the fixed-term employee must be for a temporary period only (*Ram Prasad v. State of Rajasthan, 1993 LLR 59 (Raj HC)*). Likewise, in *Haryana State Electronics v Mamni, AIR 2006 SC 2427*, the Supreme Court of India examined fixed-term engagements for its bona fide nature. In this case, the

court found the arrangement to be in bad faith since it found the gaps between successive fixed-term appointments to be artificial breaks intended to prevent a permanent employment relationship.

## FTC Employee Versus Indefinite Term Employee

The main difference between an FTC employee and an indefinite term employee is the termination procedure that may apply. A workman employed under an FTC whose employment terminates on the expiry of the term is not subject to or protected by the retrenchment obligations and rights provided in the IDA. (*Section 2(oo)(bb) read with Section 25F, IDA.*)

This means that when a workman's employment terminates on the expiry of the FTC, the employer does not have to comply with the following compliance requirements that apply when terminating the employment of an indefinite term workman who has completed at least 240 days of continuous employment:

- Providing notice or payment in lieu of notice.
- Retrenchment compensation.
- Notifying the labor authorities.

In terms of benefits applicable to both categories of employees, the central Model Standing Orders under the SO Act central rules and some of the state Model Standing Orders provide:

- Fixed-term employees are eligible for all statutory benefits available to a permanent worker.
- These benefits will be available proportionately according to the period of service rendered by the worker even if the period of employment does not extend to the qualifying period of employment required in the statute (see *Fair Treatment of FTC Employees*).
- The hours of work, wages, allowances, and other benefits shall not be less than that of a permanent employee.

(*Paragraph 2(h), Industrial Employment (Standing Order) Central Rules, 1946; Paragraph 3(ca), Schedule I, Industrial Employment (Standing Orders) Punjab Rules, 1949.*)

There is also no additional remuneration requirement for fixed-term employees.

## Fair Treatment of FTC Employees

According to Model Standing Orders under the SO Act central rules and SO Act state specific rules, fixed-term employees are entitled to the same benefits as regular indefinite term employees proportionate to their period of service. The SO Act central rules, and some of the state rules under the SO Act, require employers to set the following terms and conditions at a par with equivalent indefinite term employees:

- Working hours.
- Wages.
- Allowances

- Other benefits.

Employers covered under the SO Act central rules and applicable state rules (in some states such as Haryana, Goa, Orissa, and Karnataka) must also make statutory payments and benefits to fixed-term employees proportionate to their length of service, irrespective of any applicable eligibility criteria under the respective statute. For example, the Payment of Gratuity Act, 1972 requires an employee to have completed five years of service to be eligible to receive gratuity. However, such employers are required to make pro-rata gratuity payments to fixed-term employees irrespective of the fact that the employee did not complete five years of continuous service.

Section 2(o) of the IR Code and the Section 2(34) of the SS Code (which are yet to be enacted) also stipulate:

- A fixed-term employee's working hours, wages, allowances, and other benefits cannot be less than that of a permanent employee doing the same work or work of a similar nature.
- Fixed-term employees are eligible for all benefits available to a permanent employee under any law, irrespective of whether they meet the qualifying period of employment. These benefits must be paid in proportion to the period of service rendered.

In India, there is no legal obligation to notify fixed-term employees of indefinite term vacancies. The employer can also decide not to extend benefits to the FTC employee if the following are met:

- The benefits are truly discretionary or contractual in nature (potentially including benefits provided for in the employment contract, provision of which are discretionary), such as discretionary long-term service payments and ex gratia payouts.
- The employer has just reasons for not extending such benefits to FTC employees. For example, discretionary payouts that are meant to be made to long-service employees.

## **FTC Employee Versus Independent Contractor**

An independent contractor (also referred to as consultant, adviser, retainer, or freelancer) unlike a fixed-term employee, is someone who works based on a contract for service between two parties (rather than a contract of service). Here, the parties do not have an employer-employee relationship.

Indian courts have primarily applied the factor of "control and supervision" to determine the true nature of a service relationship, namely whether the relationship is that of an employer-employee or an independent contractor arrangement. While there is no single test to determine control and supervision, which will vary from business to business, some of the important factors for determining an employer-employee relationship include whether the:

- Engaging party extends any employee benefits to the hired individual.
- Work performed by the hired individual is similar to the work performed by the employees of the engaging party.
- Hired individual is provided a title or designation similar to employees.

The tax considerations are also different for a fixed-term employee and an independent contractor. In the case of fixed-term employees, as opposed to an independent contractor, the employer must withhold and pay certain taxes

like income taxes and social security, while an independent contractor is responsible for making payments of all taxes.

Employers usually prefer the FTC model if they want:

- A resource for a limited period of time.
- A higher degree of control over the individual and the work output.
- The worker to work solely for the hiring entity during the engagement period.
- To avoid any potential misclassification risks.

If the activity is very different from what regular employees perform and there is no need to supervise or control such worker, an employer may prefer an independent contractor arrangement.

## FTC Employee Versus Agency Worker

While fixed-term employment is a direct employment relationship between the employer and employee, agency workers are employees of a third-party agent (contractors), and are referred to as "contract labourers" under Indian labour laws. Engagement of agency workers (contract labourers) is primarily governed by the *Contract Labour (Regulation and Abolition) Act, 1970* (CLRA). The CLRA applies to every principal employer establishment (the client of the agency) that engages at least 20 agency workers (contract labourers) (not including off-site workers) in the preceding 12 months (*section 1(4), CLRA*). The CLRA also applies to every agency who employs or has employed 20 or more workmen in the preceding 12 months. While the number threshold is typically 20 in most of the states, this has been enhanced to 50 in certain Indian states such as Haryana and Maharashtra.

For short term service requirements that are the same or similar to the core services of an employer establishment, it is more suitable for employers to hire fixed-term employees. However, where the required services are non-core in nature, for example, housekeeping or security services in an IT or ITeS (Information Technology enabled Services) establishment, engaging agency workers may be preferred.

## Requirements of an FTC

While there is no national-level labour law that mandates an FTC to be in writing (or employment contracts generally), in certain Indian states such as Karnataka (Bangalore), Telangana (Hyderabad), West Bengal (Kolkata), there are requirements under the state-specific SEAs to issue an appointment order to all employees in a specific format containing certain clauses, which applies to fixed-term employees as well. An appointment order is a form containing information regarding an employee's employment, such as the employee's name, address, designation, and wages.

Apart from the terms that are specifically required to be mentioned in the appointment orders according to the prescribed format under some of the state laws, most of the FTC terms are a matter of contract and can be mutually agreed between the parties. There is no specific legal requirement to execute the FTC in local language.

The employer should ideally communicate the contract terms to the employee at the beginning of the employment by executing a fixed-term employment contract.

Although often not a legal requirement, it is a common practice for employers to execute FTC contracts outlining the terms and conditions of engagement upfront, leaving no room for ambiguity. In addition to a start date and end date, or event, the following are common terms that are typically included in the FTC contract:

- Pre-conditions of employment (for example, satisfactory background check results).
- Location of employment.
- Justification for fixed-term arrangement.
- Probation period (if any).
- Compensation and benefits.
- Intellectual property assignment.
- Confidentiality.
- Termination provisions, including:
  - whether the FTC can be terminated early on notice and, if so, the applicable notice period and payment in lieu of notice; and
  - any automatic renewal (in specific situations) or prior notice requirement for extension of the term.

## Duration and Renewal of FTCs

Under Indian law there is no limit on the duration of a single FTC or the number and length of successive FTCs. However, FTCs are meant to be adopted only for temporary assignments.

There is no legal restriction with respect to renewal of FTCs. The FTC does not need to explicitly state the right or option of renewal. The parties are free to either execute a new FTC or renew the existing contract, if necessary, based on mutual agreement.

An FTC can be renewed:

- Automatically, provided that the contract provides for the same and specifies the circumstances in which the FTC would extend automatically (for example, extension of the project for which the fixed term employee has been employed).
- At the discretion of the employer, depending on the way the contract is worded.
- Through a mutual agreement between the parties.

There are no specific limitations on an employer choosing to extend or renew an FTC. However, Indian courts have come down heavily on employers who, with the intent to circumvent some of the applicable provisions of law to regular indefinite term employees, kept continually renewing FTCs (with or without artificial breaks in between), in particular where the employer could employ a permanent employee in the job role.



In these cases, the courts have held that the arrangement was actually a regular indefinite term employment arrangement disguised as an FTC. (See *When an FTC Is Permitted* and *Advantages and Disadvantages of FTC*.)

Therefore, to help mitigate the risks of an employee asserting that the employee is a permanent employee, employers are advised to:

- Hire FTC employees only for specific temporary purposes for short term and necessary periods.
- Avoid renewing the arrangement unless there is a convincing and objectively justifiable reason for the extensions.
- Document the grounds and justification for employing an FTC employee and for any renewal of the arrangement.

## What to Consider When Terminating Employment Under an FTC

### Notice

Termination of the FTC before expiry of the term must be done in accordance with the terms of the FTC contract. For example, an FTC may contain a provision which enables the employer or employee to terminate the contract early by giving one month's notice before its expiry. The parties can, however, mutually agree to terminate an FTC at any point, even if a clause of early termination is not contained in the FTC contract.

In the absence of any provision regarding renewal at the end of the term and assuming that no notice of early termination has been served in accordance with the applicable notice provision, the FTC automatically terminates on expiry of the fixed term without the need for any notice from either party.

If the employer wishes to terminate the FTC early (with or without an early termination provision stated in the FTC), they must comply with the statutory requirements including:

- Providing a notice or payment in lieu (see below).
- Payment of retrenchment compensation (applicable only for workmen who have completed 240 days of employment).
- Notifying the labor authorities.

In the event the FTC does not specify any notice requirement for early termination (or the contractual notice requirement is less than one month), the employer must give one month's notice of termination or a payment in lieu thereof (for immediate termination) if the fixed term employee has completed either:

- 240 days of continuous service (applicable only to employees who are workmen under the IDA).
- Three to six months of employment, depending on the applicable state specific SEA.

If an employee fails to provide notice or terminates an FTC in breach of their obligations, the employer may file a civil claim for recovery of notice pay and other damages (if any) in the relevant court. In practice, several employers make deductions (for example, the salary that would have been earned in the notice period) from the full and final

settlement amounts payable to the employee at the time the employment terminates. However, this is subject to the risk of an employee claiming that the deduction is not listed as a permissible deduction from wages under applicable laws.

## Employee Rights on Termination of the FTC

The length of service of a fixed term employee and the timing of the termination may have an impact on the employee's rights.

An FTC employee that terminates on expiry of the term does not benefit from retrenchment rights and protections. In contrast, an FTC employee who is dismissed before the expiry of the fixed term, having completed 240 days of continuous service with an employer, is entitled to:

- One month's notice or pay in lieu.
- Retrenchment compensation (see *Severance Pay*).

There are also similar provisions under some state-specific SEAs (for example, the Telangana Shops and Establishments Act, 1988 applicable in Hyderabad).

The length of the employee's service will also allow them to get leave accrual and higher payment in lieu of accrued but unused annual leave when the employment terminates.

There is no provision under Indian law allowing an employer and employee to contract out of statutory rights of employees. In theory, the employer may incentivise the employee to mutually separate early by signing a release of claims in return for an ex gratia consideration. However, it may not be possible to enforce a release and waiver, to the extent they relate to statutory entitlements of employees.

If the employer wants to terminate the contract due to the employee's misconduct, the employer must first conduct an internal investigation (that is, a disciplinary inquiry) to establish the alleged misconducts. The employer is not required to provide notice for employment termination if the misconduct is proved through a domestic inquiry following principles of natural justice.

An FTC employee that is terminated prior to the expiry of the FTC cannot bring additional claims that an indefinite employee cannot claim under the law, except to the extent of pro rata statutory benefits. There are no additional protections or rights offered to an FTC employee.

## Redundancy (Lay-Off) or Reorganisation

There is no specific legal restriction with respect to FTC employees in a redundancy scenario. Therefore, in the event an FTC is to terminate early due to redundancy, the general termination related considerations applicable to indefinite term employees in case of a redundancy, a reorganisation, or lay-off (temporary dismissal from work as per Indian law) will apply to the FTC employee.

Redundancy is a justified reason for an employer to terminate an employee (*The Board of Directors of the South Arcot Electricity Distribution Co., Ltd. v. N.K. Mohammed Khan and Ors.* [1970(21) FLR174]), which also applies to termination of a fixed-term employee prior to expiry of the fixed term. In such a scenario, the employer will need to comply with the retrenchment obligations under the IDA (if the workman has completed 240 days of continuous employment), which include:

- Notice requirements or payment in lieu.
- Payment of retrenchment compensation.
- Notification to the labor authorities in the specified format.
- Payment of leave encashment where applicable.

The non-renewal of an FTC (meaning the employment terminates on the expiry of the term) does not require the employer to conduct a redundancy process, even if the reason for the non-renewal is a reduction (or cessation) in the need for the work undertaken by the employee.

## Severance Pay

A statutory severance payment (retrenchment compensation) may be payable to a workman where the employer has terminated the FTC prior to expiry of the fixed term. In the event that the workman has completed at least 240 days of continuous service with the employer, retrenchment compensation will be payable at the rate of 15 days' salary for every completed year of service exceeding six months (*section 25F, IDA*). However, the employer is not liable for retrenchment compensation if the employee voluntarily resigned or the employer lawfully terminated the employee for misconduct (*section 25F, IDA*).

For employees engaged in commercial establishments in the state of Telangana (Hyderabad) who have completed at least one year of service, there may be an additional requirement to pay a service compensation in certain circumstances (*section 47, Telangana Shops and Establishments Act, 1988*).

## Practical Tips When Entering into FTCs

Employers are advised to consider the following when entering into an FTC:

- The employer should clarify its needs and justification for the FTC and determine the length of the FTC accordingly.
- The contract should be drafted to specifically and clearly include the scope of services and the justification for fixed-term arrangement.
- The contract should have clear and unambiguous start and end dates, or period of validity.
- To avoid confusion and challenges, the benefits and policies applicable to fixed term employees, including if on a pro rata basis, should be clearly identified in the FTC.
- The parties are advised to avoid frequent renewal of FTCs.
- Automatic renewal should be limited to specific circumstances (for example, extension of the project that the employee has been engaged for, to cover for the continued period of absence of an employee).
- If a fixed term employee is converted into a permanent employee, the employer should execute a new contract (rather than an extension agreement) with a break between the two terms, in order to de-link both periods and mitigate the risk of the fixed-term period being perceived as permanent employment.

- A provision for the employer to terminate the FTC prior to expiry by providing notice should be clearly stated in the FTC. This notice requirement should not apply to misconduct terminations.

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