Keep the faith?

The good, the bad and the uncertain in Australian employment contracts

"The law concerning the duty of good faith, if any, in employment contracts is currently in a state of flux, just as it is in the law of contracts generally."[1]
— Mark Irving

In 2012, barrister Mark Irving commenced the section on good faith in employment contracts in his text with that pithy summary of the uncertain legal position. He continued:

> "The following description of the law will be completely outdated once the High Court has resolved these issues."[2]

When Mr Irving appeared before Australia's apex judiciary two years later, for the respondent in *Commonwealth Bank of Australia v Barker*,[3] he must have wondered whether those words would prove prophetic.

Unfortunately for Australian employment lawyers, the occasion has not yet arisen for Mr Irving to wholly revise his consideration of the implied term of good faith. While the High Court in *Barker* definitively rejected the implication of a term of mutual trust and confidence in employment contracts, they refused to consider its 'sibling', good faith.[4]

The plurality of French CJ, Bell and Keane JJ observed:

> "The above conclusion [regarding mutual trust and confidence] should not be taken as reflecting upon the question whether there is a general obligation to act in good faith in the performance of contracts. Nor does it reflect upon the related question whether contractual powers and discretions may be limited by good faith and rationality requirements analogous to those applicable in the sphere of public law. Those questions were not before the Court in this appeal."[5]

Kiefel J provided a slightly lengthier consideration, pondering that 'in some legal systems good faith is regarded as a vitally important ingredient for a modern general law of contract … [T]his raises the question how other legal systems cope without it.'[6] Yet she too refused to delve further. Despite admitting that the question had not been resolved in Australia, as it was not raised in argument she concluded:

> "It is therefore neither necessary nor appropriate to discuss good faith further, particularly having regard to the wider importance of the topic."[7]

Since *Barker*, to applicants good faith has effectively become a like-for-like replacement of mutual trust and confidence in employment disputes, and the term has been litigated inconclusively before several intermediate courts. In March, the New South Wales Court of Appeal delivered judgment in *Bartlett v Australia & New Zealand Banking Group Ltd*,[8] with Macfarlan JA and Simpson JA disagreeing on the good faith issue. As no High Court pronouncement in this uncertain area of law seems forthcoming, the discussion in *Bartlett* is worthy of examination.

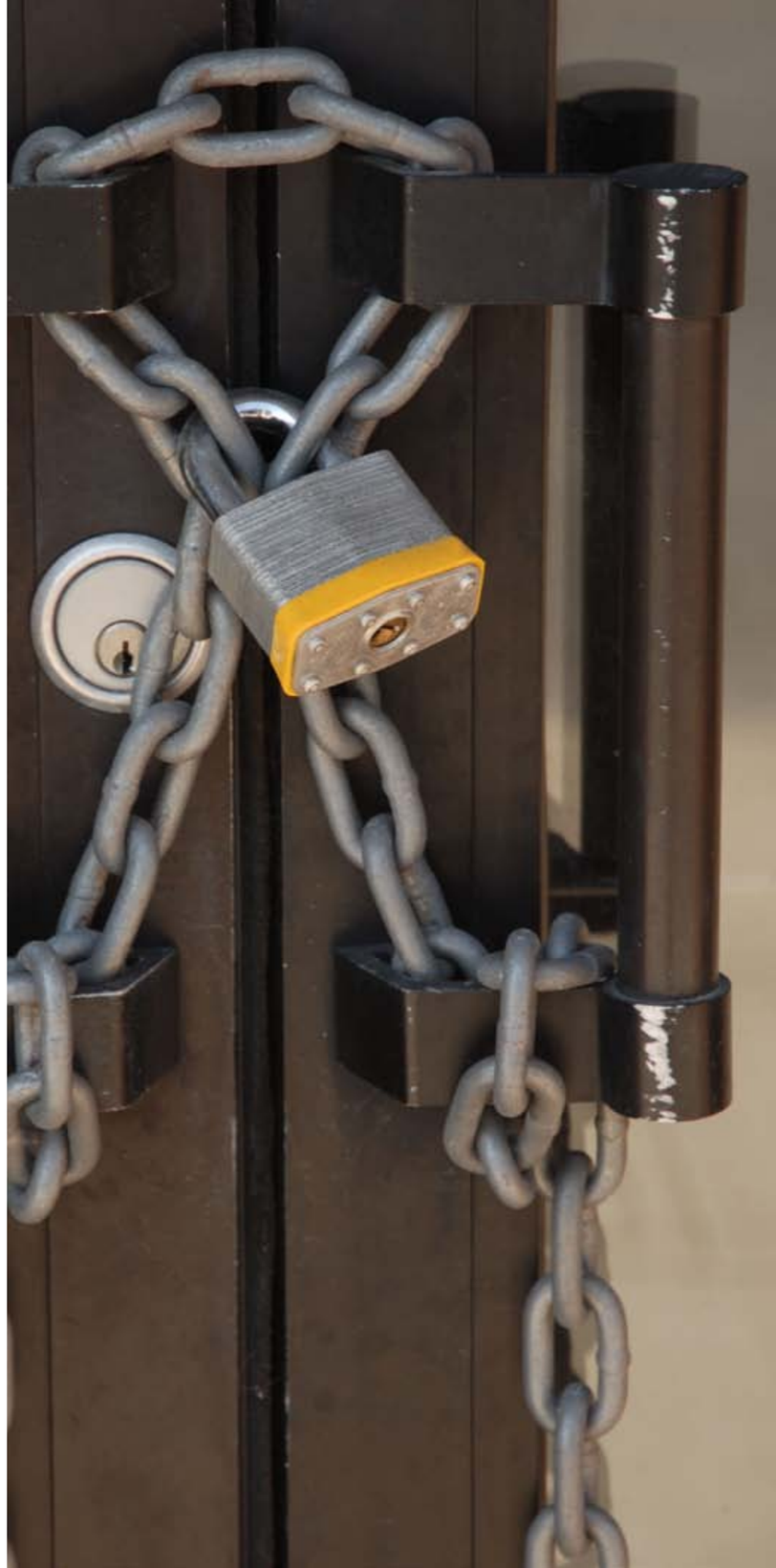
This article will commence by outlining the development of a contractual good faith obligation. It will then discuss the term's possible content, before analysing the divergent perspectives offered in *Bartlett*. The article will conclude by speculating about the future of good faith in employment contracts: whether, to echo Bon Jovi, the High Court will keep the faith.

History

The contractual concept of good faith — or *bona fides* as it then was — has historical origins in Roman law.[9] As early as the 1700s, British courts recognised that '[i]n contracts of all kinds, it is of the highest importance that courts of law should compel the observance of honesty and good faith.'[10]

The development of a good faith principle quickly came into conflict with a core tenet of Anglo contract law: freedom of contract.[11] It is difficult to reconcile good faith with the *caveat emptor* doctrine and other consequences of the economic freedom conception of contract law.[12] English law thus became increasingly hostile to the concept, with Lord Ackner noting in the negotiation context that good faith is 'inherently repugnant to the adversarial position of the parties' and 'as unworkable in practice as it is inherently inconsistent.'[13] Yet the pendulum of opinion has begun to swing back, with the Supreme Court of the United Kingdom recently confirming that in the absence of clear and unambiguous language to the contrary, 'a contractual discretion must be exercised in good faith and not arbitrarily or capriciously.'[14]

In other jurisdictions, the term was embraced with warmth. Good faith has been accepted, and codified, in the United States.[15] The Canadian Supreme Court, meanwhile, acknowledged in 2014 that 'good faith contractual performance is a general organizing principle of the common law of contract which underpins and informs' common law rules.[16] The concept has also been described by one judge as 'a latent premise' of New Zealand



jurisprudence,[17] and been accepted in South Africa's blended civil and common law system.[18]

In Australia, good faith has received a mixed reception. In *Service Station Association Ltd v Berg Bennett & Associates Pty Ltd*, Gummow J compared it with related developments in equity. He wrote: 'To some extent equity has regulated the quality of contractual performance … [N]otions of good conscience play a part. *But it requires a leap of faith* to translate these well established doctrines and remedies into a new term as to the quality of contractual performance, implied by law.'[19]

Yet federal and state courts have been willing to take that leap, with recognition of good faith by judges across the country.[20] Although debate rages as to the nature of the concept: whether it is an implied term (and if so how implied), or a principle of construction, or an assumption made by parties to a contract,[21] good faith's existence — at least in commercial contracts — appears settled at an intermediate court level. One author even writes, '[u]ntil the legislature or the High Court says otherwise, the contractual duty of good faith is here to stay.'[22]

Content

An obvious question follows: what is good faith, and in the contractual context what does it require? This is not an easy query to answer. Finn J described the concept as 'protean',[23] while to Geoffrey Kuehne it is 'chameleonic'.[24] At minimum, it seems to require that the parties act in a way which is not capricious or arbitrary in the performance of the contract. Beyond that, judges and academics remain split on good faith's content: to some it is restricted to a limited notion of honesty, while to others it includes a duty to act reasonably.[25] The quest for a definition often leads to the circular answer that good faith includes an obligation not to act in bad faith, which hardly progresses our understanding.

The broader view of good faith finds support in *Renard Constructions (ME) Pty Ltd v Minister for Public Works*, where Priestley JA held:

> "The contract can in my opinion only be effective as a workable business document under which the promises of each party to the other may be fulfilled, if the subclause is read … as subject to requirements of reasonableness."[26]

Conversely, leading contract law academics have described such an approach as 'misconceived' and contended that it is not 'even arguable that for a party to a contract to act in good faith it must discharge a positive obligation to act reasonably.'[27] On this view, good faith can be equated strictly to honesty and 'fidelity to the bargain'.[28]

In the employment contract setting, the best elucidation of the possible content of the obligation comes from Rothman J's judgment in *Russell v The Trustees of the Roman Catholic Church for the Archdiocese of Sydney*.[29] His Honour posited that 'if there exists a duty to act in good faith it "imports a requirement that the person doing the act exercise prudence, caution and diligence"'.[30] He continued: '[T]he rights and/or duties reposed in either the employer or employee would need to be exercised honestly and reasonably; with prudence, caution and diligence, and with "due care to avoid or minimise adverse consequences" to the other party that are inconsistent with the agreed common purpose and expectations of the parties to the contract.' In light of the employment relationship in dispute, Rotham J held 'it is impossible to imagine that the contract of employment could operate without a duty of good faith.'[31] On appeal, Giles JA, Basten JA and Campbell JA assumed (without deciding) the existence of the good faith term, but found that it had not been breached.[32]

Even if Rothman J's pronouncement is accepted, legitimate questions remain as to whether, and if so how, good faith differs from the mutual trust and confidence term rejected in *Barker*. In oral argument in that case, French CJ pondered: 'How does the implication found here differ from an implication of good faith? Is that a subset or is it just a manifestation?' Bret Walker SC, for the Commonwealth Bank, responded that he could not discern 'any factor which would distinguish the supposed implied term in this case from something as broad as a notion of good faith.'[33]

In sum, the content of an implied term of good faith — whether in employment contracts or generally — remains unclear. The Canadian Supreme Court's concession that the obligation is 'incapable of precise definition' provides little encouragement in the search for a more exacting description.[34] Such uncertainty was on display in *Bartlett*.

Bartlett

Proceedings in *Bartlett* commenced after ANZ terminated an executive for allegedly doctoring and then leaking a confidential internal email to the *Australian Financial Review*. ANZ undertook an investigation, which found 'sufficient circumstantial evidence' that Mr Paul Bartlett was responsible.[35] As a result, Mr Bartlett was in breach of the applicable Code of Conduct and Ethics, and despite his protestations of innocence, he was terminated without notice for serious misconduct. Mr Bartlett lost at first instance, with the primary judge rejecting his wrongful dismissal claim and finding that he was responsible for the leak.[36]

In the New South Wales Court of Appeal, all three judges allowed Mr Bartlett's appeal. Clause 14.3(b) of Mr Bartlett's employment contract permitted ANZ to terminate without notice if, in ANZ's opinion, the employee engaged in serious misconduct. ANZ accepted that in exercising the power it was required to act in good faith, a curious concession, but argued that a duty of reasonableness was not located within that concept.[37]

After reviewing recent authorities and noting that *Barker* had expressly refused to clarify the existence or scope of any duty of good faith, Macfarlan JA turned to a recent British case which found that an employer was obliged to act reasonably in the administrative law sense.[38] This led His Honour to the conclusion that, 'in forming an opinion under Clause 14.3(b) … the Bank was obliged to act reasonably, at least in the *Wednesbury* sense and at least so far as its process, as distinct from result, was concerned.'[39] Macfarlan JA did not, though, explicate whether this reasonableness requirement came from within a good faith obligation or was conceptually distinct. His reference to an earlier New South Wales Court of Appeal case, which offered that there was 'no distinction of substance between the implied term of reasonableness and that of good faith', provides little assistance.[40]

As ANZ's investigation process suffered from a number of defects, Macfarlan JA held that 'its departure from the standard of conduct which could be expected from a reasonable corporate employer was such as to satisfy the *Wednesbury* test.'[41] In this respect, the remainder of the bench concurred.

However, Macfarlan JA and Simpson JA diverged on the construction of clause 14.3(a) of Mr Bartlett's employment contract, that 'ANZ may terminate your employment for any reason' by giving notice. It is on this issue that the central question arose once more: 'whether, in exercising that right, the Bank was under an obligation to act reasonably and/or in good faith.'[42]

Macfarlan JA distinguished clause 14.3(a) from 14.3(b). He observed that 'none of the authorities' previously referred to warrant 'the implication of any restriction of the

Bank's power … Such a restriction would be inconsistent with those quoted words. Unlike Clause 14.3(b), that subclause does not require the Bank to form a specified opinion as a pre-condition to the exercise of the power.'[43] Accordingly, no good faith obligation attached to the without cause termination clause, and thus Mr Bartlett's damages were limited because ANZ could have terminated the contract in any event and paid out his notice.

Simpson JA had 'difficulty' with this approach.[44] Her Honour began by considering several commercial contract cases involving termination for convenience clauses, which had suggested a limitation based on good faith.[45] She then observed: 'If these authorities can be taken to support the proposition that a term of good faith and fair dealing is to be implied in termination clauses in commercial contracts, it is difficult to see why a similar position ought not to apply to contracts of employment.'[46] However, because this issue had only been agitated in post-hearing submissions, Simpson JA declined to consider it further: 'I am far from convinced that they should *not* [be imported into a contract of employment]; such a proposition is simply unsupported by authority and not the subject of adequate argument.'[47]

Bartlett thus provides both clarity and confusion. From it we can tentatively distil the following: an administrative law standard of reasonableness exists when employers need to form a particular view about conduct to exercise a contractual right; and this may, or may not, form part of an implied term of good faith. Whether this good faith term might have broader application is yet to be determined.

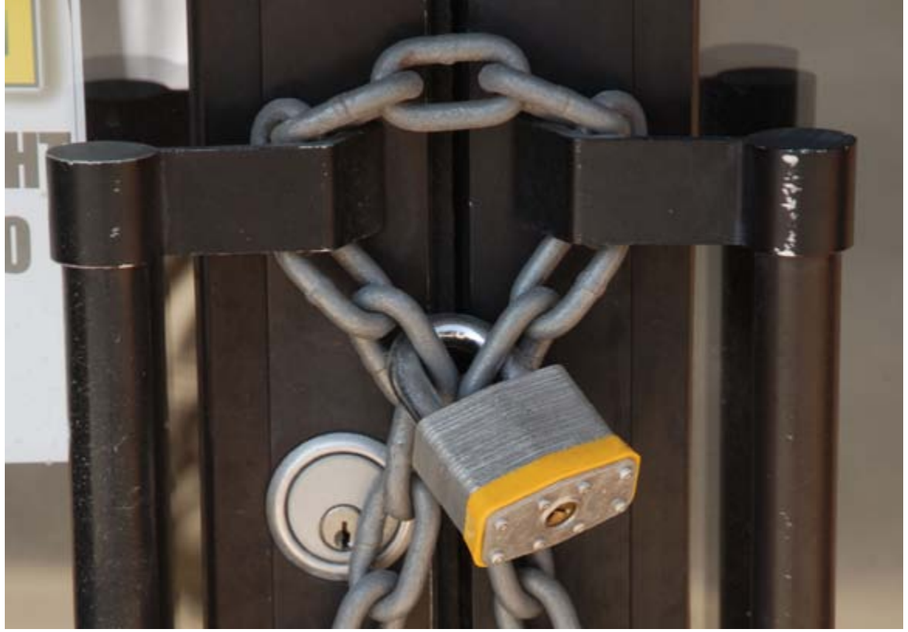
Where to now?

ANZ has not sought special leave to appeal to the High Court. Accordingly, a conclusive determination as to the presence and scope of a good faith term in Australian employment contracts remains elusive.

In a contribution to the *Journal of Contract Law* last year, an all-star cast of academics offered an extensive critique of *Barker*.[48] They suggested that the 'not wholly convincing' decision represented a 'missed opportunity' for the Court to 'chart a new direction' on implied terms.[49] As to good faith, they observed that in light of *Barker* 'it is difficult to see how it could be implemented', unless 'the content of any such duty is minimal'.[50]

There are numerous persuasive policy rationales for the implication of a good faith term. The concept has historical origins, and recognises that cooperation and fairness are necessary elements in contractual performance.[51] Good faith has become commonplace in many jurisdictions, via case law or statute, and is a crucial element in the *UNIDROIT Principles of International Commercial Contracts*. Article 1.7 of those principles, which often govern international trade contracts, demands that '[e]ach party must act in accordance with good faith and fair dealing', and that '[t]he parties may not exclude or limit this duty'.[52]

In the employment context, such a term would be consistent with the modern contractual nature of the relationship, far removed from the master-servant model of previous times. J W Carter et al criticised *Barker* on this basis — which refused



to imply an obligation of *mutual* trust and confidence despite accepting that *employees* owe an implicit duty of fidelity not to conduct themselves in a manner 'destructive of the necessary confidence between employer and employee'.[53] This asymmetry of obligations is an 'unattractive view of employment standards in Australia', argued Carter et al, and was ill-suited to the current nature of the employment relationship.[54] Accepting a good faith term would go some way to restoring the contractual equilibrium between employer and employee.

Yet the Court's reasoning in *Barker* is seemingly at odds with the possibility of an implied term of good faith. The plurality cautioned that '[t]he common law in Australia must evolve within the limits of judicial power and not trespass into the province of legislative action.'[55] The wide-ranging impact of a mutual trust and confidence term, they continued, 'locates the propounded implication close to the boundary between judicial law-making and that which is within the province of the legislature.'[56]

For that reason, and others, they shied away from implying such a term, lest they cross 'the Rubicon that divides the judicial and the legislative powers'.[57] Given a term of good faith is as wide, if not wider, than that of mutual trust and confidence, it would take considerable judicial creativity to sidestep *Barker*. While the High Court was at pains to make clear that they were *not* casting judgment on the good faith term, such a conclusion may follow from the logic of their decision. Indeed Simpson JA added in *Bartlett*: 'The vigour in which the proposition was rejected [in *Barker*] might suggest that the decision foreclosed the present question'.[58] Where this would leave *Bartlett*'s reasonableness obligation is unclear.

Until the High Court directly confronts this topic — and shows some 'much-needed intellectual leadership in this space' — the law surrounding employment contracts will remain plagued by uncertainty.[59] It took 17 years from a seminal British decision on mutual trust and confidence for the High Court to offer their view — a rate that suggests clarity as to good faith may be well over the horizon.

To modify another Bon Jovi lyric, the present state of good faith gives legal certainty a bad name. We can only hope that a third disgruntled banking executive brings the question squarely to the High Court's attention sooner rather than later.

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Endnotes

1. Mark Irving, *The Contract of Employment* (LexisNexis Butterworths, 2012) 503.
2. Ibid.
3. (2014) 253 CLR 169 ('*Barker*').
4. Joellen Riley, 'Siblings But Not Twins: Making Sense of "Mutual Trust" and "Good Faith" in Employment Contracts' (2012) 36 *Melbourne University Law Review* 521.
5. *Barker* (2014) 253 CLR 169, 195.
6. Ibid 213.
7. Ibid 214.
8. [2016] NSWCA 30 (7 March 2016) ('*Bartlett*').
9. Simon Whittaker and Reinhard Zimmermann, 'Good Faith in European Contract Law: Surveying the Legal Landscape' in Reinhard Zimmermann and Simon Whittaker (eds), *Good Faith in European Contract Law* (Cambridge University Press, 2000) 7, 16.
10. *Mellish v Motteux* (1792) 170 ER 113, 113–14. See also *Carter v Boehm* (1766) 97 ER 1162, 1164.
11. Geoffrey Kuehne, 'Implied Obligations of Good Faith and Reasonableness in Performance of Contracts: Old Wine in New Bottles?' (2006) 33 *University of Western Australia Law Review* 63, 66.
12. See Kirby J's comments in *Royal Botanic Gardens and Domain Trust v South Sydney City Council* (2002) 240 CLR 45, 75–6.
13. *Walford v Miles* [1992] 2 AC 128, 138.
14. *British Telecommunications Plc v Telefónica O2 Ltd* [2014] UKSC 42 (9 July 2014) [37].
15. Kuehne, above n 11, 79–83.
16. *Bhasin v Hrynew* [2014] 3 SCR 494 [33] (Cromwell J).
17. *Livingstone v Roskilly* [1992] 3 NZLR 230, 237 (Thomas J).
18. Kuehne, above n 11, 78.
19. (1993) 117 ALR 393, 405–6.
20. See Anthony Gray, 'Good Faith in Australian Contract Law After *Barker*' (2015) 43 *Australian Business Law Review* 358, 362.
21. Ibid 370–6.
22. Justice Robert McDougall, 'The Implied Duty of Good Faith in Australian Contract Law' [2006] *NSW Judicial Scholarship* 2, 9.
23. *Secretary, Department of Education, Employment, Training and Youth Affairs v Prince* (1997) 152 ALR 127, 130.
24. Kuehne, above n 11, 64.
25. Gray, above n 21, 366–9.
26. (1992) 26 NSWLR 234, 258.
27. Elisabeth Peden, 'When Common Law Trumps Equity: The Rise of Good Faith and Reasonableness and the Demise of Unconscionability' (2005) 21 *Journal of Contract Law* 226, 236; J W Carter and Elisabeth Peden, 'Good Faith in Australian Contract Law' (2003) 19 *Journal of Australian Contract Law* 155, 157.
28. *United Group Rail Services Ltd v Rail Corporation (NSW)* (2009) 74 NSWLR 618, 636 (Allsop P).
29. (2007) 69 NSWLR 198.
30. Ibid 227.
31. Ibid.
32. *Russell v The Trustees of the Roman Catholic Church for the Archdiocese of Sydney* (2008) 72 NSWLR 559.
33. Transcript of Proceedings, *Commonwealth Bank of Australia v Barker* [2014] HCATrans 73 (8 April 2014) 364–9.
34. *Wallace v United Grain Growers Ltd* [1997] 3 SCR 701 [98] (Iacobucci J).
35. [2016] NSWCA 30 (7 March 2016) [5]–[19].
36. *Bartlett v Australia and New Zealand Banking Group Ltd* [2014] NSWSC 1662 (24 November 2014) (Adamson J).
37. [2016] NSWCA 30 (7 March 2016) [38].
38. *Braganza v BP Shipping Ltd* [2015] UKSC 17 (18 March 2015), cited in ibid [46].
39. [2016] NSWCA 30 (7 March 2016) [49].
40. *Burger King Corporation v Hungry Jack's Pty Ltd* (2001) 69 NSWLR 558, 570 (Sheller JA, Beazley JA, Stein JA), cited in ibid [41].
41. [2016] NSWCA 30 (7 March 2016) [51].
42. Ibid [109] (Simpson JA).
43. Ibid [87].
44. Ibid [108].
45. Ibid [122]–[125].
46. Ibid [126].
47. Ibid [135] (emphasis added).
48. J W Carter et al, 'Terms Implied in Law: "Trust and Confidence" in the High Court of Australia' (2015) 32 *Journal of Contract Law* 203.
49. Ibid 203, 230.
50. Ibid 230.
51. See Jeannie Paterson, Andrew Robertson and Peter Heffey, *Principles of Contract Law* (Thomson Lawbook Co, 2nd ed, 2005)
52. *UNIDROIT Principles 2010*.
53. *Blyth Chemicals Ltd v Bushnell* (1933) 49 CLR 66, 81 (Dixon and McTiernan JJ), cited with approval in *Barker* (2014) 253 CLR 169, 190 (French CJ, Bell and Keane JJ).
54. Carter et al, above n 49, 225.
55. *Barker* (2014) 253 CLR 169, 185 (French CJ, Bell and Keane JJ).
56. Ibid 194.
57. Ibid 185, quoting *Dietrich v The Queen* (1992) 177 CLR 292, 320 (Brennan J).
58. *Bartlett* [2016] NSWCA 30 (7 March 2016) [131] (Simpson JA).
59. Gray, above n 20, 358.