

RECENT DEVELOPMENTS IN EMPLOYMENT DISPUTES: EMPHASISING THE LAW OF CONTRACT

Tom Brennan¹

Barrister, 13 Wentworth Chambers

Australian law has shifted from regulating the employer/employee relationship on the basis of status to now rely principally on contract.²

In *Commonwealth Bank of Australia v Barker*³ a majority of the High Court endorsed that principal reliance on contract and reasoned that when considering the construction of a contract of employment, and the implication of terms into it, Australian Courts ordinarily apply orthodox principles applicable to contracts generally.

Three decisions of intermediate Courts of Appeal in March 2016 underline the centrality of those orthodox principles of construction applicable to contracts generally in the resolution of employment disputes. Two of those principles are:

First, the meaning of the contract is to be determined objectively:

*The meaning of the terms of a contractual document is to be determined by what a reasonable person would have understood them to mean. That, normally, requires consideration not only of the text, but also of the surrounding circumstances known to the parties, and the purpose and object of the transaction.*⁴

Second, the interpretation of any clause of a contract must occur in the context of the whole document, and not in isolation:

*The whole of the instrument has to be considered, since the meaning of any one part of it may be revealed by other parts, and the words of every clause must if possible be construed so as to render them all harmonious one with another.*⁵

¹ Tom Brennan was junior counsel for the successful appellant in *Bartlett v ANZ* to which reference is made

² *Byrne v Australian Airlines* (1995) 185 CLR 410 at 436 per McHugh and Gummow JJ.

³ *Commonwealth Bank of Australia v Barker* (2014) 253 CLR 169 at [16] and [20] – [25] per French CJ, Bell and Keane JJ.

⁴ *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* (2004) 219 CLR 165 at [40].

⁵ *Australian Broadcasting Commission v Australian Performing Rights Association Limited* (1973) 129 CLR 99 at 109 (per Gibbs J).

Employers' Policies

It is commonplace for contracts of employment to include a term that the employee will comply, or be expected to comply, with company policies as published or in force from time to time. It is common practice that employers publish, and from time to time amend, policies on issues such as occupational health and safety, financial controls and standards of conduct expected in the workplace and with customers.

The Federal Court's "incorporation" approach

In recent years the Full Court of the Federal Court has dealt with numerous claims by employees to the effect that contractual provisions of that kind result in an incorporation of the company policy into the contract, or at least mutual promises by the employee and employer to comply with the policy as it is in force and published from time to time.

In *Riverwood International Australia Pty Limited v McCormick*⁶ the contract contained a term:

You agree to abide by all company policies and practices currently in place, any alterations made to them, and any new ones introduced.

North J found that that clause was effective to incorporate each company policy into the contract and, because of the objective theory of contract referred to above:

*Any alteration or addition to the company policies and practices could only achieve binding contractual effect if there were separate agreement to such alterations or additions, either by way of variation of the existing agreement or by way of entering into a new agreement.*⁷

That was a surprising conclusion given that the express term of the contract referred to any alterations made to policies and any new policies introduced.

Mansfield J reasoned that the term by which the employee undertook to "abide by" those policies incorporated each of them by reference into the contract as they were in force from time to time.⁸

In *Goldman Sachs JB Were Services Pty Ltd v Nikolich*⁹ the contract provided:

From time to time the company has issued and will in the future issue office, memoranda and instruments with which it will expect you to comply as applicable.

⁶ [2000] FCA 889; (2000) 177 ALR 193.

⁷ At [111].

⁸ At [150].

⁹ (2007) 163 FCR 62.

Black CJ and Marshall J applied *Riverwood* in finding that the contract incorporated those parts of policy documents which were “promissory” in nature.

In *Romero v Farstad Shipping (Indian Pacific) Pty Limited*¹⁰ the contract relevantly provided:

All Farstad Shipping policies are to be observed at all times.

One of those policies was an anti-discrimination policy which was detailed and directory as to the standards of behaviour expected and as to the processes for complaint and investigation of possible contravention of those standards.

Allsop CJ, Rares and McKerracher JJ reasoned that the objective theory of contract meant that:

- (a) the starting point was the language of the contract;¹¹
- (b) in this case the text of the relevant term – policies “are to be observed” appeared “to bind both the employee and employer”;¹²
- (c) in deciding what the contents of the contract were it was necessary to have regard not only to the internal linguistic considerations of the document but also “to consider the circumstances with reference to which the words in question were used and, from those circumstances, to discern the objective which the parties had in view”.¹³

An important part of those circumstances were the terms of the anti-discrimination policy as it was in force at the time the contract was made.

The Court reasoned:

In situations where clear language is used and sufficient emphasis is placed upon the need for compliance (implicitly by both parties) with the terms of a company policy, then especially where that goes to fundamental conditions of employment, such as payment and method of compliance with external statutory obligations, objectively viewed, the parties would be expected to regard such terms as contractually binding.

As a result the Court found that the employer was bound by the provision of its anti-discrimination policy.

¹⁰ (2014) 231 FCR 403.

¹¹ At [35].

¹² At [33].

¹³ At [37] citing *Royal Botanic Gardens and Domain Trust v South Sydney City Council* (2002) 240 CLR 45 at [10].

A retreat from “incorporation”

In March 2016 the New South Wales Court of Appeal and the Full Court of the Federal Court have retreated from the ready incorporation of policy terms into contracts of employment as occurred in *Riverwood* and *Goldman Sachs*.

In *McKeith v Royal Bank of Scotland*¹⁴ the contract of employment provided:

You agree to be bound by the policies of ABN AMRO as may exist from time to time. You acknowledge and accept that it is the prerogative of ABN AMRO to vary, change or terminate existing policies as well as to devise and introduce new policies.

One of ABN AMRO’s policies was its redundancy policy which provided for redundancy benefits. The former Australian Chief Executive and another senior officer of the Australian arm of ABN AMRO sued for redundancy benefits calculated in accordance with that policy.

The Court refused to follow the approach of the Federal Court in *Riverwood International*, *Goldman Sachs* and *Romero*. Tobias AJA who wrote the leading judgment distinguished each of those cases as having been decided purely on its own facts.¹⁵

McKeith was decided on 9 March 2016. Five days later the Full Court of the Federal Court published its decision in *Westpac Banking Corporation v Wittenberg*.¹⁶

The decision concerned claims by numerous former employees of the St George Bank for various payments consequent upon their termination of employment following the merger of St George with Westpac.

Buchanan J wrote the leading judgement. His Honour reviewed in detail the decisions and reasoning in *Riverwood International*, *Goldman Sachs* and *Romero* and appears¹⁷ to have agreed with Tobias AJA’s approach to each of those case: they were to be regarded as decided purely upon their own facts. His Honour reasoned:

At common law, the relationship of employment is based on contract ...

Being based on contract, the terms of the employment must be specified, or necessarily implied, concurrently with the commencement of the relationship, or by agreed variation thereafter. This basic concept, and the need for a mutual intention to create legal and enforceable relations based on the terms of the contract, does not easily accommodate notions of unilateral importation

¹⁴ (2016) NSWCA 36.

¹⁵ At [125].

¹⁶ [2016] FCAFC 33.

¹⁷ At [109].

*or modification or reworking after the relationship is commenced, simply based on developing but unstated and unagreed expectations.*¹⁸

His Honour noted that every contract of employment includes a term that the employee when performing work under the contract will comply with the lawful directions of the employer; and that such a term was implied as a matter of law because it was necessary to permit compliance by the employer with obligations to other employees and to third parties.¹⁹

In that context his Honour posited that in many contracts a clause expressly imposing an obligation on an employee to comply with policies of the employer was no more than a term which contemplated the employer may communicate its, his or her lawful directions by the publication from time to time of policies or manuals.

His Honour then reasoned that in any case where a contract expressly imposed an obligation upon an employee to comply with the provisions of policies or manuals as published by the employer from time to time it was unlikely that the term meant the employer undertook an obligation to also be bound. That was because a party reading a term that imposed an obligation on one party but not the other, might not be acting reasonably to conclude that the term was intended to impose the obligation on both parties. Further, there are difficulties in formulating the content of the contractual obligation of an employer to comply with a policy when that same employer has the contractual right to vary that policy unilaterally.

Rather, it was likely that there would be implied as a matter of fact a term that the employer would honour so much of those policies as, at any particular point in time, operated for the real and practical benefit of an employee and that the employer would not arbitrarily or capriciously withdraw any such term. His Honour noted that such an implied term would in many cases readily meet the usual tests for implication – certainty, necessity to give business efficacy, it goes without saying; and consistency with express terms.²⁰

While McKerracher J (who had been a member of the Court in *Romero*) left the question open, he generally agreed with Buchanan J's approach.²¹ White J on the other hand held that it was unnecessary to address the question and declined to do so.²²

Conclusion

It is difficult, on an objective theory of contract, to conclude that the contractual provisions in *Riverwood International* or *Goldman Sachs* which expressly imposed obligations to abide or comply upon the employee only, and reserved to the employer the capacity to unilaterally change or add to the policies with which

¹⁸ At [69] and [70].

¹⁹ At [77].

²⁰ At [110].

²¹ At [336] and [337].

²² At [344].

compliance was required, operated as a promise by the employer to comply with those policies or manuals.

The reasoning of the New South Wales Court of Appeal in *McKeith* and of the Full Court of the Federal Court in *Wittenberg* may reflect a closer attention by the Courts to the express words used and what the parties would reasonably have understood them to mean at the time of contract formation.

The ready incorporation of employer policies into contracts of employment based upon express terms that employees will comply with those policies is unlikely to occur in future cases.

That does not mean that employers will be free to disregard their policies or manuals, but rather that contracts will be construed in accordance with their express terms and with terms implied only when that is necessary.

The implied term proposed by Buchanan J in *Wittenberg* has much to commend it: if an employee is bound to comply with an employer's policies, in many cases the employer will be bound to honour those policies in so far as they confer real benefits upon employees from time to time, and not to amend those policies arbitrarily or capriciously to remove such benefits.

Serious Misconduct in the Opinion of the Employer

A third decision concerning an employment dispute between a Bank and a senior executive in March 2016 was *Bartlett V ANZ*²³.

The ANZ purported to summarily dismiss Mr Bartlett for serious misconduct. The misconduct was said to be creating and sending to a journalist a forged internal email.

There was no issue that the email had been forged and sent to the journalist. Mr Bartlett however maintained that he had nothing to do with it. The Court found that the ANZ had failed to establish that Mr Bartlett had anything to do with the forged email.

The contract of employment relevantly provided:

13. *If you fail to comply with the provisions of your employment agreement or any other ANZ performance requirements, ANZ may take disciplinary action which may include suspension with or without pay and, in certain circumstances, termination of your employment with ANZ (see clause 14). ...*

14.3(b) *ANZ may terminate your employment at any time, without notice, if, in the opinion of ANZ, you engage in serious misconduct, serious*

²³ [2016] NSWCA 30.

neglect of duty, or serious breach of any of the terms of this employment agreement.

The trial Judge had construed clause 14.3(b) in isolation. She held that it was sufficient to enliven the power of summary dismissal that the ANZ in fact held an honest opinion that the employee had engaged in serious misconduct; and it did not matter whether the employee had in fact engaged in that misconduct.

McFarlan JA (Meagher and Simpson JJA agreeing) reasoned that clauses 13 and 14 of the agreement needed to be read so that they operated together. Clause 13 contemplated disciplinary action, including termination of employment, only in circumstances where there had in fact been a failure to comply with the agreement or performance requirements. It was open to construe clause 14.3(b) as operating only in circumstances where there had in fact been misconduct or another breach of the agreement and where the Bank held the opinion that that misconduct or other breach was serious. Construction of the contractual instrument as a whole required that that construction be given to clause 14 – so that it worked harmoniously with clause 13. As a result the Bank was not authorised by the contract to summarily terminate the employment.

The Court of Appeal also held that Mr Bartlett's alternative argument was correct: that it was not sufficient that the opinion held by the Bank was honestly held; it was also necessary that it be reasonably held.

That conclusion was reached relying on authorities concerning commercial contracts conferring power on one party to make a decision affecting the other.

McFarlan JA applied the reasoning of Gummow J in *Service Station Association Limited v Bird Bennett & Associates Pty Limited*:²⁴

Where one party has an express power the exercise of which will significantly affect the interests of the other party (eg by cancellation of their supply contract) if the holder of the power is satisfied that a certain state of affairs exists, the words of the contract are fairly readily construed (and the more so when the parties have given such a power to a third party) as requiring a reasonable as well as honest state of satisfaction.

McFarlan JA also referred to the reasoning of the Court of Appeal in *Burger King Corporation v Hungry Jacks Pty Limited*²⁵ and *United Group Rail Services Limited v Rail Corporation of New South Wales*²⁶ in which there were found to be implied terms of reasonableness and good faith governing the exercise of a power conferred by the contract and conditioned upon the formation of an opinion by a party to the contract.

²⁴ (1993) 45 FCR 84.

²⁵ (2001) 69 NSWLR 558.

²⁶ (2009) 74 NSWLR 618.

As a result the Court found that if the power of summary termination depended only upon the opinion of the Bank that the employee had engaged in serious misconduct, the contract was nevertheless to be construed as requiring that such an opinion be both honestly and reasonably held.

That gave rise to the further question of the standard of review to be applied by a Court in determining whether an opinion as to serious misconduct is reasonably held. The Court applied the decision of the UK Supreme Court in *Braganza v BP Shipping Limited*²⁷ in holding that the standard was analogous to that which applies in administrative law and commonly referred to as *Wednesbury* unreasonableness.²⁸ Application of the *Wednesbury* standard invalidates a decision that is “so unreasonable that no reasonable decision maker would ever have come to it”. Reasonableness is assessed both by reference to the outcome and to the decision making process.

As a result the Court concluded that in forming an opinion under clause 14.3(b) of the contract of employment, the Bank was obliged to act reasonably, at least in the *Wednesbury* sense and at least so far as its process, as distinct from the result, was concerned.²⁹ The Court found that the Bank had not acted reasonably because of arbitrary restrictions on the scope of its investigation.

Conclusion

The resolution of each of the three cases considered in this paper turned upon the application of orthodox principles of contract law. If there were any doubt beforehand, the reasons of the High Court in *Commonwealth Bank of Australia v Barker* underline that the starting point for analysis of such disputes is those orthodox principles of contract law.

²⁷ [2015] UKSC 17.

²⁸ *Associated Provincial Pictures Houses Limited v Wednesbury Corporation* [1948] 1 KB 223 at 233 – 234.

²⁹ At [49].