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New grounds for employees to sue employers for breach of contract

In an Australian first, a superior court has held that there are implied conditions in a contract of employment that the employer owes the employee a duty of good faith and a duty of trust and confidence.

Russell v Trustees of the Roman Catholic Church for the Archdiocese of Sydney

**NSW Supreme Court, 19 February 2007, Rothman J
[2007] NSWSC 104**

Background

The plaintiff, David Russell, was dismissed on 31 January 2003 from his duties as Director of Music at St Mary's Cathedral, following dismissal of criminal charges in 2000 and an internal investigation by the Roman Catholic Church (the Church) into alleged sexual misconduct.

In February 2003 Mr Russell commenced proceedings in the NSW Industrial Relations Commission under the *Industrial Relations Act 1996* (NSW). On 1 June 2004, Deputy President Harrison found that the termination was harsh, unreasonable and unjust, and ordered reinstatement with restitution of wages and continuity of service for all purposes. Mr Russell continued his employment from 1 June 2004.

Mr Russell incurred substantial legal costs in the Commission proceedings. He was not awarded those costs.

Mr Russell commenced his Supreme Court proceedings in March 2006. He sought damages for breach of contract, in particular for breach of allegedly implied terms of good faith and/or mutual trust and confidence. Alternatively he sought damages for wrongful dismissal. Among other damages, he claimed the legal costs which he had incurred in the Commission proceedings, being \$350,000.00 (including interest).

Summary of decision

In conclusion, Rothman J found that:

- the contract of employment between the Church and Mr Russell had an implied duty of good faith
- the contract also had an implied duty that the Church would not, without proper and reasonable cause, conduct itself in a manner calculated or likely to destroy or seriously damage the relationship of confidence and trust between the parties
- the Church had breached the implied duties and had wrongfully dismissed Mr Russell but that no damage was sustained as a result of the breaches.

Rothman J therefore ordered a verdict for the defendants and ordered that the plaintiff pay the defendants' costs in the Supreme Court (not the Commission).

Implied duties found to exist

Rothman J ruled that there was an implied duty of good faith and an implied duty of trust and confidence in the employment contract between the Church and Mr Russell.

The implied duty of good faith and the implied duty of trust and confidence are well accepted in England (*Mahmud v Bank of Credit and Commerce International (BCCI)* [1998] AC 20).

Rothman J considered that previous Australian case law had not ruled that the implied duty of good faith exists and had not ruled at an appellate level that the implied duty of trust and confidence exists, although there was some existing judicial support at lower levels.

Implied duty of good faith

The duty was described by Rothman J as follows:

... the rights and/or duties reposed in either the employer or the 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. But all the while, the parties have the capacity to exercise their rights in their own interests. [118]

His Honour held at [112] that the duty of good faith is not a duty of utmost good faith and that it is something less than a fiduciary duty.

On this analysis, the duty of good faith is a mutual duty owed both by employer and employee. However, for the purposes of this decision, it was only necessary for the court to rule that the employer owed the duty to the employee.

Implied duty of trust and confidence

Rothman J held that the duty was a duty, without reasonable and proper cause, not to conduct oneself in a manner calculated or likely to destroy or seriously damage the relationship of confidence and trust between the employer and employee.

His Honour held that the duty is mutual and is an aspect of the trust and confidence which is essential for the employment relationship. He held that the duty of trust and confidence is an implied duty which cannot be excluded from a contract of employment.

Assessing whether duties breached

Rothman J applied a balancing exercise in assessing whether the duties had been discharged. For example, his Honour said at [160] that the implied duties require a balance, in good faith, of the interests of the employer against adverse effects it may have on the employee.

The court had regard, for example, to the interest of the Church in protecting the children in its care and to the entitlement of the Church to terminate Mr Russell's employment if satisfied that the continued employment of Mr Russell presented for it an unacceptable risk of injury or harm to the children in its care.

Effect of implied duties on termination on reasonable notice

If the Church had exercised its common law right to terminate the contract on reasonable notice, this would not have involved any breach of the implied duties. Rothman J said at [141] that:

[a]lmost by definition, the implied duty, not to act to destroy the relationship of trust and confidence, will not interfere with the right of a party to a contract of employment to terminate the contract.

Effect of implied duties on investigation of misconduct

The implied duties extended to the manner in which the investigation of Mr Russell was conducted. Rothman J held at [164] that the Church had a duty to ensure that the investigation was carried out with 'prudence, caution and diligence'.

One of the key deficiencies identified by Mr Russell was that the key evidence upon which this decision was made was the evidence of 'Mr X' who was only interviewed on the telephone and not face-to-face. On this matter Rothman J held at [164]:

Given the Church's resources and infrastructure, it should have, as a matter of prudence, caution and diligence, and taking into account the significant prejudicial effect of any such investigation, interviewed Mr X face-to-face. It was a breach of the Church's duties to do otherwise.

Having regard to the cross-examination of Mr X in the Commission proceedings, Rothman J was satisfied that breach of this duty would have made no difference to the outcome and therefore no damages were payable in respect of this breach.

Wrongful dismissal

The court held that it was open to the Church to be satisfied that Mr Russell was a real and unacceptable risk to the children in its care and that the Church was entitled to terminate the employment of Mr Russell on that basis.

The court held that Mr Russell had been wrongfully dismissed because the Church had purported to pay compensation in lieu of notice. Under the implied terms of the employment contract the Church was only entitled to give reasonable notice of termination and could not pay an amount in lieu of notice. The Court found that no damage was suffered as a result of the breach.

The court ruled that Mr Russell had no entitlement to compensation for the \$350,000 in legal expenses incurred in the Commission proceedings, in part because any award of such damages would be inconsistent with the legislation relating to the Commission proceedings.

Further, the court found that damage to reputation had followed the media coverage and not the dismissal itself. The court also stated that there was not sufficient evidence on which to base damages claims for the 'injured feelings' that Mr Russell complained of.

Implications for agencies

It has been well established for a long time in Australian law that employees, including APS employees, have a duty of good faith and fidelity (or loyalty and fidelity) to the employer, although the content of the duty is not clear (*Bennett v President, Human Rights and Equal Opportunity Commission* [2003] FCA 1433; see AGS *Litigation Notes* No. 11, 22 October 2004).

Australian Government agencies have a long history and practice of acting as a model employer. However, the decision in *Russell* reinforces the need for agencies to act honestly and reasonably, and with prudence, diligence, caution and due care, when exercising employer powers and entitlements, or otherwise dealing with employees. It is now clear that a failure to do so can have legal consequences.

Text of the decision is available at:

http://www.austlii.edu.au/au/cases/nsw/supreme_ct/2007/104.html

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