

CONTRACTUAL RIGHTS AND REMEDIES FOR DISMISSED EMPLOYEES AFTER THE 'EMPLOYMENT REVOLUTION'

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*[In recent decades, recognition of the social reality of employment has transformed the way in which courts determine actions for breach of the employment contract. In construing the express and implied terms of the contract, as well as in awarding damages, courts have accepted that the employment bargain extends beyond the mere exchange of remuneration for services. The employer, like the employee, is generally also obligated to act in accordance with the expectations of care, trust and fairness that underpin the employment relationship. The notable exceptions to this 'employment revolution' are the contractual rights and remedies available to dismissed employees. In Australia, contractual dismissal actions are subject to unique restrictions that derive from the 1909 decision of the House of Lords in *Addis v Gramophone Co Ltd*. This article critically analyses the nature and impact of these restrictions and considers the likely consequences of removing them.]*

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I INTRODUCTION

For over a century, the decision of the House of Lords in *Addis v Gramophone Co Ltd* ('*Addis*')¹ has constrained the award of damages for dismissal in breach of contract and occupied 'an entirely pivotal role, more than is normally recognised,'² in the law of dismissal. Although the High Court of Australia has never considered *Addis* in the context of dismissal,³ trial and intermediate courts have generally applied the decision in the terms of the headnote to the reported case to preclude a dismissed employee from recovering 'compensation for the manner of the dismissal, for his injured feelings, or for the loss he may sustain from the fact that the dismissal of itself makes it more difficult for him to obtain fresh employment' ('the headnote rules').⁴ These rules have been applied in place of ordinary contractual principles of construction, causation and remoteness, to restrict both the damages available for wrongful dismissal⁵ and the extension of implied contractual obligations to the manner of dismissal.

As a consequence, the common law protection provided to dismissed employees is 'strictly limited'.⁶ If an employee is dismissed in breach of a

¹ [1909] AC 488.

² Mark Freedland, *The Personal Employment Contract* (Oxford University Press, 2003) 357.

³ But see *Baltic Shipping Co v Dillon* (1993) 176 CLR 344, 361 (Mason CJ), 395 (McHugh J) ('*Baltic*'), which considered *Addis* in support of the general rule that damages for distress arising from breach of contract are not recoverable. See also *Cowell v The Rosehill Racecourse Co Ltd* (1937) 56 CLR 605, 632 (Dixon J); *Byrne v Australian Airlines Ltd* (1995) 185 CLR 410, 429 (Brennan CJ, Dawson and Toohey JJ) ('*Byrne*').

⁴ *Addis* [1909] AC 488, 488. See, eg, *Lennon v South Australia* [2010] SASC 272 (2 September 2010) [676]–[688] (Layton J) ('*Lennon*'); *Russell v The Trustees of the Roman Catholic Church for the Archdiocese of Sydney* (2008) 72 NSWLR 559, 572 [54]–[55] (Basten JA) ('*Russell (Appeal)*').

⁵ Wrongful dismissal is used here in the traditional sense, to refer to dismissal without sufficient notice in circumstances not justifying summary dismissal: *Automatic Fire Sprinklers Pty Ltd v Watson* (1946) 72 CLR 435, 449–51 (Latham CJ); *Byrne* (1995) 185 CLR 410, 427–8 (Brennan CJ, Dawson and Toohey JJ).

⁶ United Kingdom, Royal Commission on Trade Unions and Employers' Associations, *Report* (1968) 141 [522] ('*Donovan Report*').

contractual requirement to provide notice,⁷ he may recover damages for the remuneration and associated pecuniary benefits he would have earned during the notice period, less any amount he actually earned or could reasonably have earned in alternative employment.⁸ 'Beyond this, the employee has no legal claim at common law, whatever hardship he suffers as a result of his dismissal.'⁹

Since *Addis* was decided, statutory unfair dismissal laws have significantly increased the scope and accessibility of legal remedies for dismissed employees.¹⁰ However, contractual damages continue to play an important role in Australian dismissal law. Contract law remains the primary source of redress for many dismissed employees, particularly higher income and professional employees, who are generally ineligible to bring statutory unfair dismissal claims.¹¹ For these employees, the headnote rules constitute significant obstacles to the recovery of both pecuniary and non-pecuniary losses caused by dismissal. The recent increase in attempts by dismissed employees to challenge or circumvent *Addis* is a testament to this fact and to the perceived inadequacy of the current rules governing the contractual damages available to dismissed employees.¹²

⁷ See, eg, *Rogan-Gardiner v Woolworths Ltd [No 2]* [2010] WASC 290 (22 October 2010) [146]–[147] (Hall J) ('*Rogan-Gardiner*'). See also *Fair Work Act 2009* (Cth) ss 117, 123.

⁸ See generally Freedland, above n 2, 363–4.

⁹ *Donovan Report*, above n 6, 141 [522].

¹⁰ The current statutory unfair dismissal scheme is contained in pt 3-2 of the *Fair Work Act 2009* (Cth). For a comprehensive analysis of the history and development of statutory dismissal remedies, including under the current scheme, see Breen Creighton and Andrew Stewart, *Labour Law* (Federation Press, 5th ed, 2010) 627–60. In relation to the accessibility of unfair dismissal remedies, see also Jennifer Acton, 'Where Have All the Cases Gone? Voluntary Resolution of Unfair Dismissal Claims' (Paper presented at the ALLA National Conference, Adelaide, 19 November 2010).

¹¹ Section 382 of the *Fair Work Act 2009* (Cth) provides that a person is protected from unfair dismissal if they have completed the minimum employment period and are either covered by a modern award, an enterprise agreement or earn less than the high income threshold set by the regulations. Regulation 2.13 of the *Fair Work Regulations 2009* (Cth) sets out a formula for calculating the high income threshold, indexed each financial year. For the financial year starting 1 July 2012, that threshold was \$123 300: Fair Work Ombudsman, *Termination of Employment Fact Sheet* (16 December 2011) <<http://www.fairwork.gov.au/resources/fact-sheets/conditions-of-employment/Pages/termination-of-employment-fact-sheet.aspx>>. For further explanation of the requirements for eligibility to bring statutory unfair dismissal claims, including the meaning of 'unfair dismissal' see Carolyn Sappideen et al, *Macken's Law of Employment* (Lawbook, 7th ed, 2011) 438–54.

¹² See, eg, *Burazin v Blacktown City Guardian Pty Ltd* (1996) 142 ALR 144, 147, 153–4 (Wilcox CJ, von Doussa and Marshall JJ); *Aldersea v Public Transport Corporation* (2001) 3 VR 499, 509–11 [56]–[66] (Ashley J); *New South Wales v Paige* (2002) 60 NSWLR 371,

From the perspective of plaintiff employees, the principal difficulty with the headnote rules is that they engender a narrow view of the employment contract — as a purely commercial exchange of remuneration for services. This narrow view is at odds with the ‘social reality’¹³ of employment, which entails a holistic bargain encompassing personal and relational as well as financial dimensions. Broussard J of the Supreme Court of California has remarked that an individual ‘usually does not enter into employment solely for the money; a job is status, reputation, a way of defining one’s self-worth and worth in the community.’¹⁴ In a similar vein, Lord Hoffman has noted that ‘a person’s employment is usually one of the most important things in his or her life. It gives not only a livelihood but an occupation, an identity and a sense of self-esteem.’¹⁵

In areas other than dismissal, judicial awareness of the benefits of employment has led to a transformation in the common law approach to the employment contract. In construing the express and implied terms of the contract, as well as in awarding damages for breach, courts have accepted various non-remunerative aspects of the employment bargain.¹⁶ Most notably, courts in recent years have been increasingly willing to augment the express terms of the employment contract with general implied obligations of good faith and fair dealing that protect the employee from harsh or unjust treatment.¹⁷ However, this ‘employment revolution’¹⁸ has been excluded in

396–400 [134]–[155] (Spigelman CJ); *Nikolich v Goldman Sachs J B Were Services Pty Ltd* [2006] FCA 784 (23 June 2006) 91–2 [315]–[319] (Wilcox J); *Naidu v Group 4 Securitas Pty Ltd* (2006) 150 IR 203, 208–9 [19]–[27] (Adams J); *Russell v The Trustees of the Roman Catholic Church for the Archdiocese of Sydney* (2007) 69 NSWLR 198, 238 [179]–[184] (Rothman J) (*‘Russell (Trial)’*); *McDonald v Parnell Laboratories (Aust) Pty Ltd* (2007) 168 IR 375, 400 [91]–[93] (Buchanan J); *Downe v Sydney West Area Health Service [No 2]* (2008) 71 NSWLR 633, 686–7 [439]–[440] (Rothman J); *Russell (Appeal)* (2008) 72 NSWLR 559, 569 [41]–[43], 572–3 [55]–[56] (Basten JA); *McDonald v South Australia* (2008) 172 IR 256, 336–7 [471]–[478] (Anderson J); *Quinn v Gray* (2009) 184 IR 279, 286 [28]–[30] (Byrne J) (*‘Quinn’*); *Rogers v Millennium Inorganic Chemicals Ltd* (2009) 229 FLR 198, 214 [86]–[87] (Lucev FM) (*‘Rogers’*); *Lennon* [2010] SASC 272 (2 September 2010) [676]–[681] (Layton J); *Rogan-Gardiner* [2010] WASC 290 (22 October 2010) [192] (Hall J).

¹³ *Johnson v Unisys Ltd* [2003] 1 AC 518, 539 [35] (Lord Hoffmann) (*‘Johnson’*).

¹⁴ *Foley v Interactive Data Corporation*, 765 P 2d 373, 407 (Cal Sup Ct, 1988).

¹⁵ *Johnson* [2003] 1 AC 518, 539 [35] (Lord Hoffmann).

¹⁶ See generally Douglas Brodie, ‘Legal Coherence and the Employment Revolution’ (2001) 117 *Law Quarterly Review* 604. See also *Edwards v Chesterfield Royal Hospital NHS Trust* [2012] 2 WLR 55, 80–1 [83]–[87] (Lord Phillips) (*‘Edwards’*).

¹⁷ See, eg, *Hem v Cant* (2007) 159 IR 113, 118 [20]–[22] (Finkelstein J); *Honda Canada Inc v Keays* [2008] 2 SCR 362, 387–91 [50]–[58] (Bastarache J for McLachlin CJ, Bastarache, Binnie, Deschamps, Abella, Charron and Rothstein JJ), 400–1 [81]–[82], 413–14 [114]

Australia from cases of dismissal because of the apparently restrictive and binding authority of *Addis*. Actions for dismissal in breach of contract are therefore subject to unique limitations which do not apply to other actions for breach of the employment contract or for breaches of contract more generally.

This article undertakes a systematic doctrinal analysis of the effect that the decision in *Addis* and its subsequent interpretation in Australia has had on the recovery of contractual damages for dismissal. Academic recognition of the central role that *Addis* has played in employment law is certainly not new. Mark Freedland, in his seminal work *The Personal Employment Contract*, argues persuasively that *Addis* has cemented in English employment law a 'nexus of mutually self-sustaining ideas' relating to a) the unrestricted power of employers to terminate an employment contract by notice; and b) the limitations placed on 'wrongfulness' and damages in connection with wrongful dismissal.¹⁹ Writing extrajudicially almost two decades ago, Justice Peter Gray was critical of the '[c]ontinued blind adherence to the limits imposed by the House of Lords in *Addis* on damages which can be recovered by an employee dismissed in breach of contract'.²⁰ Other commentators have also examined the various influences that *Addis* has exerted on the common law of employment in Canada, New Zealand and the United Kingdom.²¹

However, while there has been some recognition of the importance of *Addis* in Australia,²² no academic commentator has previously analysed the

(LeBel J for LeBel and Fish JJ); *Whelan v Waitaki Meats Ltd* [1991] 2 NZLR 74, 89 (Gallen J); *Malik v Bank of Credit & Commerce International SA (in liq)* [1998] AC 20, 37 (Lord Nicholls), 48 (Lord Steyn) ('*Malik*').

¹⁸ *Johnson* [2003] 1 AC 518, 539 [36] (Lord Hoffmann).

¹⁹ Freedland, above n 2, 359. See generally at 356–62.

²⁰ Justice Peter R A Gray, 'Damages for Wrongful Dismissal: Is the Gramophone Record Worn Out?' in Ron McCallum, Greg McCarry and Paul Ronfeldt (eds), *Employment Security* (Federation Press, 1994) 41, 50.

²¹ In the English context see, eg, Nathan East, '*Addis v Gramophone*: Time to Change the Tune?' (2001) 22 *Business Law Review* 278; Sappideen et al, above n 11, 419–23. For comparison of the English and Canadian law on *Addis* see Judy Fudge, 'The Spectre of *Addis* in Contracts of Employment in Canada and the UK' (2007) 36 *Industrial Law Journal* 51; Douglas Brodie, 'The Beginning of the End for *Addis v The Gramophone Company*?' (2009) 38 *Industrial Law Journal* 228. For extensive analysis of the role of *Addis* in New Zealand employment law see New Zealand Law Commission, *Aspects of Damages: Employment Contracts and the Rule in Addis v Gramophone Co*, Report No 18 (1991). See also Alan Geare, 'Legal Rights of Employees in the Event of Dismissal: The New Zealand Situation' (2007) 23 *International Journal of Comparative Labour Law and Industrial Relations* 267.

²² See eg, Sappideen et al, above n 11, 423–5; Joellen Riley, *Employee Protection at Common Law* (Federation Press, 2005) 87; Adrian Brooks, 'The Good and Considerate Employer: Devel-

body of Australian wrongful dismissal cases purportedly applying *Addis* or considered the impact of the *Addis* headnote rules on other contractual causes of action for dismissal. In addressing this lacuna, this article provides a comprehensive investigation of the case law concerning *Addis* over the last 20 years and draws on this to identify and then critically assess the effects of the headnote rules on Australian dismissal law. The article also utilises relevant cases from New Zealand, Canada and England to provide insight into potential problems and future developments in this area of the law.

In doing so, the article aims to answer the following central question: is retention of the *Addis* headnote rules justified, and, if not, what is the likely consequence of discarding them? In order to evaluate the headnote rules, consideration is given to two core criteria identified by the High Court as justifying the application of common law rules: first, the precedential basis of the rules;²³ and secondly, their ‘connection with more fundamental doctrines and principles.’²⁴ This inquiry is concerned solely with the relevance of *Addis* to employment law, namely with the determination of contractual damages available to dismissed employees as against their former employers. A consideration of any collateral effects of *Addis* on the general law of contract is beyond the scope of this investigation, as is the consideration of other statutory or common law remedies for dismissal.

The article is divided into six principal parts. Following this introduction, Part II examines the precedential basis of the headnote rules and their influence on Australian dismissal law. Beginning with a review of the decision in *Addis*, Part II argues that the headnote rules do not accurately represent the ratio of the decision, and that, as a result, the justification for relying on the headnote as a matter of precedent is greatly undermined.

Nevertheless, Part III contends that the headnote rules have exerted a controlling influence over the law of dismissal. Despite some inconsistencies in the application of the rules, it is contended that the rules have had two significant effects on the law of dismissal. The ‘direct effect’ limits dismissal damages to the loss of pecuniary benefits that would have been earned by the dismissed employee during the notice period. The ‘indirect effect’ restricts the

opments in the Implied Duty of Mutual Trust and Confidence’ (2001) 20 *University of Tasmania Law Review* 29, 64–7 (on the specific issue of whether damages for injured feelings are available for breach of the implied term of mutual trust and confidence).

²³ *Farah Constructions Pty Ltd v Say-Dee Pty Ltd* (2007) 230 CLR 89, 150–2 [134]–[135] (Gleeson CJ, Gummow, Callinan, Heydon and Crennan JJ).

²⁴ *Imbree v McNeilly* (2008) 236 CLR 510, 526 [45] (Gummow, Hayne and Kiefel JJ).

application of implied contractual terms such as mutual trust and confidence to dismissal.

Given the lack of precedential basis for the headnote rules, Part IV then assesses whether their application is otherwise justifiable on the basis of their connection with more fundamental principles of contractual doctrine. Part IV demonstrates that retention of the *Addis* headnote rules undermines the doctrinal coherence of contract and employment law, by imposing on the parties an artificial interpretation of the employment contract that fails to recognise the social realities of modern employment. The indirect effect subverts accepted principles of construction and leads to inconsistent and illogical outcomes for plaintiff employees, while the direct effect contradicts the compensatory objective of contractual damages. Part IV concludes that there is no principled justification for the headnote rules.

In light of this conclusion, Part V considers the likely consequences of abandoning the headnote rules. It contends that once the impediments of the headnote rules are removed, dismissal law will be able to develop in a natural and coherent manner. This will involve the extension of the implied term of mutual trust and confidence to dismissal and the assessment of damages for dismissal in breach of contract in accordance with ordinary contractual damages principles. These developments would improve the contractual protection afforded to dismissed employees by providing a basis for assessment of contractual dismissal damages that fully reflects the nature of the employment bargain.

Finally, drawing together the precedential and more fundamental doctrinal deficiencies of the headnote rules, the article concludes that a new approach to awarding contractual dismissal damages is warranted. Overturning the headnote rules would facilitate the development of doctrinally coherent principles for assessing dismissal damages and would bring the common law of dismissal into line with the modern realities of the employment relationship.

II THE *ADDIS* RATIO

The natural starting point for an inquiry into the restrictions on contractual damages available to dismissed employees is the decision in *Addis*. *Addis* has undoubtedly had a profound effect on the development of dismissal law, both within Australia and across the common law world. However, while the general historical significance of the case is impossible to deny, there is still considerable debate regarding the correct ratio of *Addis*. Freedland has remarked on the case that '[n]o sooner was it decided and reported than an

unending controversy broke out as to what, precisely, it had decided.²⁵ This Part attempts to resolve this controversy and thus determine whether the headnote rules genuinely embody the ratio of *Addis*.

Addis concerned a plaintiff who was employed as manager of the defendants' business in Calcutta, India. The terms of employment included the payment of salary and a commission on trade done, and provision for dismissal with six months' notice. The defendants gave the plaintiff six months' notice, but simultaneously effectively removed him from his position in a clear breach of contract.²⁶ The circumstances of this removal involved the defendants instructing their bank that the plaintiff was no longer entitled to represent them and appointing a successor to immediately take over the plaintiff's duties.²⁷ Consequently, the plaintiff was prevented from working for the defendant throughout the six month notice period. As a result of the manner of his dismissal, the plaintiff lost standing in the commercial community of Calcutta and presumably experienced pain and distress.²⁸

At trial, the plaintiff was awarded damages for wrongful dismissal in addition to six months' salary and commission 'in respect of the harsh and humiliating way in which he was dismissed'.²⁹ The issue on appeal to the House of Lords was whether, in assessing damages for wrongful dismissal, the jury was permitted to take into account 'circumstances of harshness and oppression accompanying the dismissal and any loss sustained by the plaintiff from the discredit thus thrown upon him'.³⁰ In a decision that has been 'much discussed'³¹ and 'much muttered against',³² five of the six Law Lords, all of whom delivered separate speeches, answered this question in the negative. The plaintiff's damages were thus confined to the salary and commission which he would have earned had he been permitted to work out the notice period.³³

²⁵ Freedland, above n 2, 357. See also *Edwards* [2012] 2 WLR 55, 62–3 [19]–[21], 70 [43] (Lord Dyson JSC).

²⁶ *Addis v Gramophone Co Ltd* [1909] AC 488, 489–90 (Lord Loreburn LC).

²⁷ *Ibid* 504 (Lord Shaw).

²⁸ *Ibid* 493 (Lord Atkinson), 504 (Lord Shaw).

²⁹ *Ibid* 493 (Lord Atkinson).

³⁰ *Ibid* 497 (Lord Collins).

³¹ *Malik* [1998] AC 20, 38 (Lord Nicholls).

³² Brooks, above n 22, 57.

³³ *Addis* [1909] AC 488, 490–1 (Lord Loreburn LC), 492 (Lord James), 496–7 (Lord Atkinson), 502 (Lord Gorell), 504–5 (Lord Shaw).

More than a century later, the ratio of *Addis* is still a contentious issue in employment law.³⁴ The decision has often been cited in terms of the headnote to the reported case. As such, *Addis* has come to stand for the proposition that a wrongfully dismissed employee cannot recover ‘compensation for the manner of his dismissal, for his injured feelings, or for the loss he may sustain from the fact that the dismissal of itself makes it more difficult for him to obtain fresh employment.’³⁵ However, only Lord Loreburn LC expressed his reasons in these terms.³⁶ Although three of the other Law Lords concurred with His Lordship’s speech, each of them offered additional reasons for their decision.³⁷ As Lord Reid has remarked, ‘[c]oncurrence with the speech of a colleague does not mean acceptance of every word which he has said. If it did there would be far fewer concurrences than there are.’³⁸

A close examination of the speeches of the other Law Lords reveals the inaccuracy of the headnote as a reflection of the case’s ratio. Crucially, and perhaps surprisingly, none of the Law Lords other than Lord Loreburn LC framed the issue in terms of whether the plaintiff could recover ‘compensation’ for ‘loss’. Lord Gorell considered that damages awarded to the plaintiff for ‘the manner in which discharge took place’ were not referable to ‘the money loss to the plaintiff of losing the benefit of the contract.’³⁹ Lord Atkinson and Lord Collins (in dissent) viewed the plaintiff’s claim as one for exemplary damages⁴⁰ while Lord James and Lord Shaw categorised the award as one for aggravated damages.⁴¹

The meanings intended to be conveyed by their Lordships’ use of the terms ‘exemplary’ and ‘aggravated’ are not entirely clear. Aggravated and exemplary damages have their genesis in tort law and describe damages directed to distinctly different ends. Aggravated damages are compensatory in nature. They ‘are a form of general damages, given by way of compensation for injury to the plaintiff, which may be intangible, resulting from the

³⁴ See, eg, Freedland, above n 2, 359.

³⁵ *Addis* [1909] AC 488, 488; *Malik* [1998] AC 20, 38 (Lord Nicholls); *Johnson* [2003] 1 AC 518, 526 [3] (Lord Steyn). See, eg, *Russell (Appeal)* (2008) 72 NSWLR 559, 572 [55] (Basten JA).

³⁶ *Addis* [1909] AC 488, 491; *Johnson* [2003] 1 AC 518, 526 [3] (Lord Steyn).

³⁷ *Addis* [1909] AC 488, 492 (Lord James), 493 (Lord Atkinson), 505 (Lord Shaw).

³⁸ *Broome v Cassell & Co Ltd* [1972] AC 1027, 1087, quoted with approval in the context of *Addis* in *Johnson* [2003] 1 AC 518, 530 [15] (Lord Steyn).

³⁹ *Addis* [1909] AC 488, 501–2 (Lord Gorell).

⁴⁰ *Ibid* 493 (Lord Atkinson), 497, 500–1 (Lord Collins).

⁴¹ *Ibid* 492 (Lord James), 504 (Lord Shaw).

circumstances and manner of the wrongdoing.⁴² They ‘take account of intangible injuries and by definition will generally augment damages assessed under the general rules relating to the assessment of damages.’⁴³ By contrast, exemplary damages ‘are intended to punish the defendant, and presumably to serve one or more of the objects of punishment — moral retribution or deterrence.’⁴⁴ They constitute a windfall for the plaintiff, since they are not referable to the plaintiff’s loss.

Despite these distinct usages, the Law Lords in *Addis* used these terms interchangeably to refer to damages which were not compensatory.⁴⁵ Their meaning therefore appears to be akin to the modern concept of exemplary or punitive damages. The same is true of Lord Gorell’s description of damages for ‘the manner of the plaintiff’s dismissal’ as not referable to ‘money loss’.⁴⁶

The rejection of non-compensatory damages in a claim for breach of contract is certainly not remarkable and reflects the contemporary view in both England and Australia that exemplary damages are not available in contract.⁴⁷ It is arguable that the ratio of *Addis* is simply a reaffirmation of that general rule.⁴⁸ However, this conclusion in no way justifies the headnote, which is directed to the preclusion of compensatory damages for ‘loss’, rather than to restricting exemplary damages.

Another possible ratio for the case, expressly stated by some of the Lords and hinted at by others, is that the plaintiff’s claim was essentially one for defamation and, as such, was not cognisable in an action for breach of contract.⁴⁹ Sir Frederick Pollock, writing contemporaneously, explains the

⁴² *New South Wales v Ibbett* (2006) 229 CLR 638, 646 [31] (Gleeson CJ, Gummow, Kirby, Heydon and Crennan JJ). See also *Uren v John Fairfax & Sons Pty Ltd* (1966) 117 CLR 118, 149 (Windeyer J).

⁴³ *Vorvis v Insurance Corporation of British Columbia* [1989] 1 SCR 1085, 1099 (McIntyre J for Beetz, McIntyre and Lamer JJ).

⁴⁴ *Uren v John Fairfax & Sons Pty Ltd* (1966) 117 CLR 118, 149 (Windeyer J). See also at 129–30 (Taylor J).

⁴⁵ See, eg, *Addis* [1909] AC 488, 492 (Lord James) equating damages ‘on the ground that there has been an aggravation’ with the ‘exemplary or vindictive damages’ considered by Lord Collins: at 497; 495–6 (Lord Atkinson); 504 (Lord Shaw).

⁴⁶ *Ibid* 502.

⁴⁷ *Butler v Fairclough* (1917) 23 CLR 78, 89 (Griffith CJ); *Whitfeld v De Lauret & Co Ltd* (1920) 29 CLR 71, 81 (Isaacs J); *Gray v Motor Accident Commission* (1998) 196 CLR 1, 6–7 [12]–[13] (Gleeson CJ, McHugh, Gummow and Hayne JJ); *Rookes v Barnard* [1964] AC 1129, 1226–7 (Lord Devlin).

⁴⁸ *Quinn* (2009) 184 IR 279, 282 [10]–[11] (Byrne J); *Malik* [1998] AC 20, 51 (Lord Steyn).

⁴⁹ *Addis* [1909] AC 488, 493 (Lord Atkinson), 501–2 (Lord Gorell). Other Law Lords indicated that the action was better brought in tort: at 492 (Lord James), 502–3 (Lord Shaw).

decision on this basis.⁵⁰ The failure of the plaintiff's case might therefore be referable to a poor choice of taxonomy, rather than to the substance of the claim. Lord Atkinson in particular was critical of the 'unscientific form' in which the pleadings were framed and 'the loose manner in which the proceedings at the trial were conducted.'⁵¹ In any event, this interpretation of the case is also inconsistent with the terms of the headnote, which makes no reference to tort or defamation.

Ultimately, the decision in *Addis* does not have a single clear ratio. The decision is best explained as a result of a combination of concerns regarding both the need to maintain the compensatory as opposed to punitive purpose of contractual damages and the need to preserve distinctions between the principles governing actions in contract and tort. However, the lack of consistent terminology throughout the various speeches makes the enunciation of either of these concerns in terms of a precise rule problematic.

What is clear is that neither of these broad concerns supports the adoption of the rules set out in the headnote. The headnote rules purport to restrict damages, not by reference to punitive purposes or concurrent tortious liability, but on the basis of the cause (the manner of dismissal) or the nature of the loss (injured feelings and reduced employment prospects). As a result of this disconnect between the reasoning of the majority of the *Addis* Law Lords and the headnote, the headnote rules do not have any solid foundation in legal precedent. At most, these rules represent the decision of a single Law Lord, delivered without reference to legal authority or doctrinal principle.⁵² This conclusion seriously undermines the justification for applying the headnote rules to dismissal cases. The rules are not the result of binding legal precedent, but merely a historical accident in the way the *Addis* decision was reported.

Despite this, more than a century later, the *Addis* headnote continues to constrain the law of dismissal. As such, it is no longer sufficient to simply distinguish *Addis*, or reinterpret the decision in terms of exemplary damages or defamation. Writing in 2001, Lord Steyn remarked that 'the statement of the law encapsulated in the controversial headnote has exercised an influence over this corner of the law for more than 90 years.'⁵³ Any critique of the

⁵⁰ Sir Frederick Pollock, 'Notes' (1910) 26 *Law Quarterly Review* 1, 2.

⁵¹ *Addis* [1909] AC 488, 493.

⁵² See generally Gray, above n 20, 43–4; Freedland, above n 2, 358–9.

⁵³ *Johnson* [2003] 1 AC 518, 526 [3].

headnote rules in the modern context must therefore contend with the large body of subsequent cases applying them.

III LEGAL EFFECTS OF THE HEADNOTE RULES

An examination of contractual dismissal cases in Australian jurisdictions over the past 20 years demonstrates the pivotal role that the *Addis* headnote rules have played in the development of dismissal law in this country. Although the *Addis* headnote rules have never been considered by the High Court in connection with dismissal,⁵⁴ trial and intermediate appellate courts have consistently treated them as binding rules governing the award of contractual dismissal damages. This Part examines the effects that application of the headnote rules has had on the development of Australian dismissal law. Two distinct effects are identified and analysed: the direct effect restricting damages; and the indirect effect restricting the availability of contractual causes of action.

A *The Direct Effect: Restricted Damages for Wrongful Dismissal*

The direct effect of the headnote rules is the placement of a series of restrictions on recovery of damages for dismissal in breach of contract. Pursuant to the headnote rules, a dismissed employee is prevented from recovering in contract for the pecuniary losses associated with damage to reputation⁵⁵ and psychiatric injury,⁵⁶ as well as non-pecuniary damages for mental distress, hurt and humiliation.⁵⁷ These restrictions apply regardless of whether such loss was caused by a breach of the employment contract or was within the reasonable contemplation of the parties at the time of entering the

⁵⁴ As far as the author is aware, the only recitation of the headnote rules by a member of the High Court occurs in *Baltic* (1993) 176 CLR 344, 395 (McHugh J).

⁵⁵ *Russell (Appeal)* (2008) 72 NSWLR 559, 572 [54]–[55] (Basten JA).

⁵⁶ There is no entitlement to damages for personal injury resulting from dismissal: *Aldersea v Public Transport Corporation* (2001) 3 VR 499, 518 [117] (Ashley J)). See also *Johnson* [2003] 1 AC 518, 541 [44]–[46] (Lord Hoffmann); *New South Wales v Paige* (2002) 60 NSWLR 371, 400 [154]–[155] (Spigelman CJ), which held that an employer's duty of care does not extend to dismissal proceedings.

⁵⁷ *Lennon* [2010] SASC 272 (2 September 2010) [676], [688] (Layton J); *Rogan-Gardiner* [2010] WASC 290 (22 October 2010) [119]–[120] (Hall J), quoting *Russell (Appeal)* (2008) 72 NSWLR 559, 574–5 [63]–[65] (Basten JA).

contract.⁵⁸ Consequently, damages for wrongful dismissal are limited to the salary and associated pecuniary benefits the employee would have earned during the notice period, less any amount he actually earned or could reasonably have earned in connection with the duty to mitigate.⁵⁹ Such benefits include ‘commissions, pension rights and other *promised* benefits such as training or promotion.’⁶⁰ The risk of any other losses caused by dismissal in breach of contract is therefore borne by the employee. To justify or mandate this result, courts have interpreted and applied the headnote in two ways.

The first approach treats the *Addis* headnote as a rule or principle which in itself conclusively determines the availability of damages for wrongful dismissal. For example, in *Lennon v South Australia*, Layton J relied on the headnote to conclude that ‘the weight of authority in Australia suggests that damages for distress and humiliation or injury to reputation are not recoverable [for wrongful dismissal].’⁶¹ The ‘*Addis* principle’ has also been cited to preclude recovery for ‘damages for distress occasioned by the wrongful termination of an employment contract, ... includ[ing] the manner of termination’⁶² and ‘loss of reputation ... invoked in a commercial sense to include difficulty in obtaining alternative employment’.⁶³

In contrast, the second approach views *Addis* as a remoteness case, which delineated the boundaries of recovery for dismissed employees under the *Hadley v Baxendale* (‘*Hadley*’)⁶⁴ principles. This interpretation of *Addis* is surprising, given that, as illustrated in Part II, the Law Lords in *Addis* did not view the plaintiff’s claim as compensatory and so did not seek to determine whether the alleged loss was too remote to sound in damages. Francis Dawson has remarked that:

⁵⁸ See *Baltic* (1993) 176 CLR 344, 363–4 (Mason CJ), 367–9 (Brennan J). See below Part V(B). For recent discussion of this point in England see *Edwards* [2012] 2 WLR 55, 79–80 [80]–[81] (Lord Phillips PSC). Interestingly, in that case Lord Mance JSC also suggested that the *Addis* principle may in fact be one of causation rather than remoteness: at 81–2 [91].

⁵⁹ See, eg, *Dyer v Peverill* (1979) 2 NTR 1, 5, 7 (Muirhead J); *Rogan-Gardiner* [2010] WASC 290 (22 October 2010) [224] (Hall J).

⁶⁰ *McDonald v South Australia* (2008) 172 IR 256, 336 [474] (Anderson J) (emphasis added). In Australia, the employee cannot recover for discretionary benefits. But see *Clark v Nomura International plc* [2000] IRLR 766.

⁶¹ [2010] SASC 272 (2 September 2010) [688].

⁶² *Aldersea v Public Transport Co* (2001) 3 VR 499, 511 [66] (Ashley J).

⁶³ *Russell (Appeal)* (2008) 72 NSWLR 559, 572 [55] (Basten JA).

⁶⁴ (1854) 9 Ex 341; 156 ER 145.

it is tempting to view *Addis* as turning on an application of *Hadley v Baxendale*, thus leaving the way open for the case to be distinguished in subsequent cases. A careful reading of their Lordships' speeches in *Addis* lends no countenance to this view ...⁶⁵

Nevertheless, this approach has gained considerable traction. In Australia, the remoteness interpretation of *Addis* can be traced to the decision in *Burazin v Blacktown City Guardian Pty Ltd* ('*Burazin*').⁶⁶ In that case, the plaintiff was dismissed in 'unusual exacerbating circumstances' which included being 'forcibly removed from the premises by two police officers' and having unjustified written and verbal allegations made about her capacity and conduct.⁶⁷ The Court held that the plaintiff could recover statutory compensation for the distress and humiliation occasioned by the circumstances of her dismissal,⁶⁸ so that it was unnecessary to determine whether such damages were also available at common law. However, in the course of their reasons, the judges discussed both *Hadley* and *Addis* and indicated their view that *Addis* had decided that damages for distress arising from wrongful dismissal were too remote for recovery in contract.⁶⁹ The remoteness interpretation of the *Addis* headnote rules has been referred to or applied in a number of subsequent cases.⁷⁰

Despite its lack of textual foundation, from the point of view of doctrinal consistency, the remoteness interpretation is to be preferred. Rather than creating a new set of rules governing contractual damages for dismissal, the reasoning of the *Burazin* Court attempts to understand *Addis* within a traditional contractual damages framework.⁷¹ However, this objective is

⁶⁵ Francis Dawson, 'General Damages in Contract for Non-Pecuniary Loss' (1983) 10 *New Zealand Universities Law Review* 232, 242.

⁶⁶ (1996) 142 ALR 144.

⁶⁷ *Ibid* 145, 156 (Wilcox CJ, von Doussa and Marshall JJ).

⁶⁸ *Workplace Relations Act 1996* (Cth) s 170EE, as repealed by *Workplace Relations and Other Legislation Amendment Act 1996* (Cth) sch 6 item 5. Subsection 392(4) of the *Fair Work Act 2009* (Cth) specifically excludes from the award of compensation for unfair dismissal 'compensation for shock, distress or humiliation, or other analogous hurt, caused to the person by the manner of the person's dismissal.'

⁶⁹ *Burazin* (1996) 142 ALR 144, 151 (Wilcox CJ, von Doussa and Marshall JJ). See generally at 148–53.

⁷⁰ See, eg, *Downe v Sydney West Area Health Service [No 2]* (2008) 71 NSWLR 633, 686–7 [439] (Rothman J); *Aldersea v Public Transport Corporation* (2001) 3 VR 499, 518 [112], [115]–[117] (Ashley J); *McDonald v South Australia* (2008) 172 IR 256, 336 [471]–[472], 337 [477]–[478] (Anderson J).

⁷¹ *Burazin* (1996) 142 ALR 144, 147–8, 151 (Wilcox CJ, von Doussa and Marshall JJ).

frustrated by the subsisting view that the *Addis* headnote represents a general rule, governing remoteness in *all* dismissal cases, rather than merely an illustration of the application of the *Hadley* principles to particular facts. Consequently, the delineation of liability in dismissal cases does not respond to changing social contexts and factual scenarios and is therefore inconsistent with the *Hadley* focus on the damages that were in the reasonable contemplation of the particular parties upon entering the contract.⁷²

These two broad restrictive approaches to the application of *Addis* demonstrate the confusion and uncertainty that the decision, and in particular the headnote rules, has generated in the law of wrongful dismissal. As far as the plaintiff employee is concerned, however, it makes little difference whether the headnote rules are applied as binding in themselves, or as illustrative of the proper application of the principles of contractual remoteness to dismissal. In both guises, the direct effect of the headnote rules is that an employee's right to recovery for loss occasioned by wrongful dismissal is restricted; at most the employee can recover wages and associated pecuniary benefits that would have been earned during the applicable notice period.

B *The Indirect Effect: Restricted Contractual Causes of Action*

In an attempt to overcome the restrictive effect of the headnote rules on wrongful dismissal damages, a number of employee plaintiffs have pleaded breach of implied contractual duties in connection with dismissal.⁷³ In *New South Wales v Paige*, Spigelman CJ noted that '[i]n recent years the authority of *Addis v Gramophone Co* has been challenged, but not undermined, by creative use of implied terms, notably the obligation of mutual trust and confidence.'⁷⁴ These alleged implied terms are directed to regulating the manner of dismissal, and thus aim to bring the type of conduct countenanced in *Burazin* within the scope of the employer's legal liability. However, this strategy has been barred by the indirect effect of the headnote rules.

The indirect effect hinges on the preclusion in the *Addis* headnote of 'compensation for the manner of the dismissal' ('the manner rule'). Australian courts have generally interpreted this preclusion broadly, to effectively

⁷² But see *Quinn* (2009) 184 IR 279, 286 [29]–[30] (Byrne J).

⁷³ See, eg, *Lennon* [2010] SASC 272 (2 September 2010) [166] (Layton J); *Rogan-Gardiner* [2010] WASC 290 (22 October 2010) [126]–[127] (Hall J); *Rogers* (2009) 229 FLR 198, 222 [119]–[121] (Lucev FM).

⁷⁴ (2003) 60 NSWLR 371, 396 [134], cited with approval in *McDonald v Parnell Laboratories (Aust) Pty Ltd* (2007) 168 IR 375, 399 [85] (Buchanan J).

prevent recovery of compensation for losses arising from the employer's actions in connection with either the antecedent processes⁷⁵ or actual carrying out⁷⁶ of the dismissal. Beginning with the assertion that such damages are not recoverable, this process of reasoning leads to the conclusion that there can be no legal obligation to prevent such loss.⁷⁷ Indirectly, the restriction of damages under the manner rule has thus militated against the recognition of implied contractual duties in connection with dismissal.⁷⁸

The most prominent example of this indirect effect is the stultifying influence that the manner rule has had on the application of implied contractual terms of good faith, and mutual trust and confidence, to dismissal. Although courts have sometimes dealt with these terms separately, it is likely that they represent a single contractual duty⁷⁹ requiring employers to 'not, without reasonable and proper cause, conduct themselves in a manner calculated or likely to destroy or seriously damage the relationship of confidence and trust between the parties.'⁸⁰ This implied duty is a comparatively recent development in Australian law, which has yet to be conclusively affirmed by the High Court.⁸¹ Nevertheless, with the exception of dismissal, the duty of mutual trust and confidence is now generally recognised as implied in law in all employment contracts,⁸² regardless of the intention of the parties.⁸³

⁷⁵ Such as investigatory proceedings leading to dismissal: *New South Wales v Paige* (2002) 60 NSWLR 371, 377 [24], 400 [155] (Spigelman CJ); *Russell (Appeal)* (2008) 72 NSWLR 559, 573–5 [58]–[66] (Basten JA); *Rogan-Gardiner* [2010] WASC 290 (22 October 2010) [120] (Hall J). But see *Rogers* (2009) 229 FLR 198, 217–18 [100]–[103] (Lucev FM).

⁷⁶ Such as abuse or false allegations: *Burazin* (1996) 142 ALR 144, 145, 151 (Wilcox CJ, von Doussa and Marshall JJ).

⁷⁷ See also Freedland, above n 2, 354.

⁷⁸ See also *New South Wales v Paige* (2002) 60 NSWLR 371, 377 [24], 400 [155] (Spigelman CJ), where the duty of care in tort was found not to extend to investigatory proceedings leading to dismissal; *Shaw v New South Wales* [2012] NSWCA 102 (19 April 2012) [122]–[127] (Barrett JA), where the duty was found not to extend to decision-making processes leading to dismissal.

⁷⁹ *Russell (Appeal)* (2008) 72 NSWLR 559, 567 [30]–[32] (Basten JA).

⁸⁰ *Courtaulds Northern Textiles Ltd v Andrew* [1979] IRLR 84, 85 (Arnold J). See, eg, *Lennon* [2010] SASC 272 (2 September 2010) [180] (Layton J); *Rogan-Gardiner* [2010] WASC 290 (22 October 2010) [125] (Hall J).

⁸¹ There is support for the duty in obiter from the High Court: *Koehler v Cerebos (Australia) Ltd* (2005) 222 CLR 44, 55 [26] (McHugh, Gummow, Hayne and Heydon JJ); *Concut Pty Ltd v Worrell* (2000) 176 ALR 693, 706 [51] (Kirby J).

⁸² *Lennon* [2010] SASC 272 (2 September 2010) [176]–[177] (Layton J); *Rogan-Gardiner* [2010] WASC 290 (22 October 2010) [125]–[126] (Hall J); *Rogers* (2009) 229 FLR 198, 222 [119]–[120] (Lucev FM); *Quinn* (2009) 184 IR 279, 282–3 [13]–[14] (Byrne J); *Downe v Sydney West Area Health Service [No 2]* (2008) 71 NSWLR 633, 666 [326]–[328] (Roth-

However, Australian courts have proved reluctant to consider the term in the context of dismissal. The source of this reluctance was highlighted by Basten JA in *Russell v The Trustees of the Roman Catholic Church for the Archdiocese of Sydney*, commenting that ‘it is unclear to what extent the breach of such a term may permit relief by way of damages, consistently with the principle in *Addis* ... precluding damages for the manner of wrongful dismissal’.⁸⁴ Other courts have also consistently refused to recognise obligations of trust and confidence in connection with dismissal — relying, at least in part, on the manner rule and the purported authority of *Addis*.⁸⁵

Thus the indirect effect of the headnote rules, and in particular the manner rule, is that implied contractual obligations which otherwise govern the employment relationship are not applied to actions connected with dismissal. While the employer may have a duty not to damage or destroy trust and confidence during the course of the employment relationship, this obligation is apparently extinguished where the actions are undertaken in anticipation of dismissal. Consequently, the conduct involved in *Burazin* is necessarily consistent with the employer’s contractual obligations,⁸⁶ even though similar conduct unconnected with dismissal may well breach the employment contract.⁸⁷

man J); *Russell (Trial)* (2007) 69 NSWLR 198, 229–30 [125]–[129] (Rothman J); *Perkins v Grace Worldwide (Aust) Pty Ltd* (1997) 72 IR 186, 191 (Wilcox CJ, Marshall and North JJ). See *Russell (Appeal)* (2008) 72 NSWLR 559, 561 [1] (Giles JA), 568 [33] (Basten JA), 576 [73] (Campbell JA); *South Australia v McDonald* (2009) 104 SASR 344, 389–90 [231]–[233] (Doyle CJ, White and Kelly JJ). But see *Wright v Groves* [2011] QSC 66 (1 June 2011) [53] (Lyons J), where it was concluded that Australian law in this area is unsettled. See also *Aldersea v Public Transport Corporation* (2001) 3 VR 499, 513 [74]–[75] (Ashley J); *Dye v Commonwealth Securities Ltd* [2012] FCA 242 (16 March 2012) [600]–[602] (Buchanan J) where reservations were expressed as to the existence of the term.

⁸³ See generally *Breen v Williams* (1996) 186 CLR 71, 103 (Gaudron and McHugh JJ). See also *Shaw v New South Wales* [2012] NSWCA 102 (19 April 2012) [45]–[46] (Barrett JA).

⁸⁴ (2008) 72 NSWLR 559, 568 [34]. But see *Shaw v New South Wales* [2012] NSWCA 102 (19 April 2012) [119] (Barrett JA).

⁸⁵ See, eg, *Rogers* (2009) 229 FLR 198, 217–22 [101]–[120] (Lucev FM); *Quinn* (2009) 184 IR 279, 286 [28]–[30] (Byrne J); *Rogan-Gardiner* [2010] WASC 290 (22 October 2010) [119]–[120] (Hall J).

⁸⁶ See text accompanying above n 66.

⁸⁷ See, eg, *Walker v Northumberland County Council* [1995] 1 All ER 737, 759–60 (Colman J); *Moore v Bude-Stratton Town Council* [2001] ICR 271, 287 [45] (Lindsay J), which involved unjustified allegations regarding competency and conduct; *RDF Media Group plc v Clements* [2008] IRLR 207, 219 [118], 220 [125], 221 [132] (Livesey QC), which involved public vilification or humiliation).

C Statutory Exclusion: An Explanation for Restricted Causes of Action?

It is necessary here to deal with another basis which has been suggested to warrant the exclusion of mutual trust and confidence from dismissal — that is, inconsistency with the statutory provisions of the unfair dismissal scheme. In *Johnson v Unisys Ltd* (*Johnson*), the House of Lords held that a dismissed employee could not claim damages in either tort or contract for loss caused by the manner of dismissal, because the unfair dismissal provisions of the *Employment Rights Act 1996* (UK) c 18 evinced an intention to preclude the recovery of common law damages in these circumstances.⁸⁸ Notwithstanding significantly different statutory regimes, *Johnson* has been considered or applied in several Australian decisions to support similar conclusions.⁸⁹

This reliance by Australian courts on *Johnson* is difficult to justify. In the first place, the rationale for the decision itself is highly questionable. As Freedland has remarked:

If [*Johnson*] is a genuine attempt to comply with the design of the unfair dismissal legislation, it is rather surprising to have regarded Parliament, when it introduced a set of statutory protections for workers with regard to dismissal, as intending, indeed as enjoining, that the common law should not, in the future, develop parallel protections as part of the implied content of their personal work or employment contracts.⁹⁰

Secondly, and more importantly, *Johnson* turned on the particular statutory dismissal scheme implemented by the *Employment Rights Act 1996* (UK) c 18 and bears no relevance to the current Australian unfair dismissal scheme contained in the *Fair Work Act 2009* (Cth). As Joellen Riley has contended, although in the context of an earlier version of the unfair dismissal laws, the Australian provisions ‘do not expressly or even impliedly constrain the

⁸⁸ [2003] 1 AC 518, 526 [2] (Lord Nicholls), 546 [66] (Lord Hoffmann), 550 [80] (Lord Millett). Following the more recent decision of the English Supreme Court in *Edwards* [2012] 2 WLR 55, it is now clear that the ‘*Johnson* exclusion area’ is not confined to implied common law obligations. In that case, the Court held, with Baroness Hale JSC dissenting, that damages were not recoverable for breach of contract in relation to the manner of dismissal even where the breach was of an express contractual term regulating the disciplinary proceedings leading to dismissal: at 69–70 [40]–[41], 72 [49] (Lord Dyson JSC), 78 [75], 81 [86]–[88] (Lord Phillips PSC), 82 [94] (Lord Mance JSC), 89 [120] (Baroness Hale JSC), 98 [150] (Lord Kerr JSC).

⁸⁹ See, eg, *New South Wales v Paige* (2002) 60 NSWLR 371, 396–400 [135]–[155] (Spigelman CJ); *Aldersea v Public Transport Corporation* (2001) 3 VR 499, 511 [61]–[66] (Ashley J); *Rogan-Gardiner* [2010] WASC 290 (22 October 2010) [118] (Hall J).

⁹⁰ Freedland, above n 2, 343.

jurisdiction of courts of common law and equity in determining contract disputes.⁹¹ The scheme is not directed to curtailing the employee's common law rights,⁹² but to the maintenance of minimum standards for low and middle income dismissed employees.⁹³ Consequently, the employee's contractual rights are unaffected by statute.⁹⁴

The Australian unfair dismissal provisions thus provide no basis for excluding the implied duty of mutual trust and confidence from dismissal, particularly where, as with the majority of cases considered here, the statutory dismissal scheme does not even apply to the dismissed employee. The result in *Johnson*, and its popularity with Australian courts, is in reality a further example of the indirect effect of *Addis*, illustrative of the pervasive view that damages for the manner of dismissal are not available at common law.

D *The Combined Effect: Limited Contractual Protection*

The combined result of the direct and indirect effects of the headnote rules is that the contractual protection accorded to dismissed employees is arbitrarily restricted by reference to predetermined limits. Both in establishing breach and demonstrating compensable loss, dismissed employees must contend with a unique set of headnote rules which do not apply to other contracting parties. Moreover, the weight of authority suggests that these restrictions do not apply only to causes of action based on the fact and manner of the dismissal itself, but also where injury is sustained during antecedent processes connected with dismissal, such as disciplinary or investigative proceedings.

As Justice Gray has remarked, employers in this instance are treated as 'a privileged class of contracting parties'⁹⁵ with uniquely limited liability. The only contractual cause of action available to a dismissed employee is a claim

⁹¹ Riley, above n 22, 92. See also Mark Irving, 'Damages Arising from the Manner of an Employee's Dismissal' (2003) 16 *Australian Journal of Labour Law* 1, 5–8.

⁹² Section 725 of the *Fair Work Act 2009* (Cth) prohibits a person from making an unfair dismissal application (under s 729) or other statutory dismissal applications under ss 726–8, 730–1 where an application or complaint has been made under another law by or on behalf of that person in relation to the dismissal. Section 732(2) defines 'application or complaint under another law' as an application or complaint made under a law of the Commonwealth, a state or territory. Section 725 thus expressly contemplates that a person may have multiple rights of action in respect of a dismissal including, presumably, rights at common law.

⁹³ See generally *ibid* ss 61, 139.

⁹⁴ See also Joydeep Hor and Louise Keats, *Managing Termination of Employment: A Fair Work Act Guide* (CCH, 2nd ed, 2009) ch 7.

⁹⁵ Gray, above n 20, 41.

for wrongful dismissal, being dismissal without the contractually required notice, and the only damages recoverable are for loss of the notice period remuneration. Any other losses associated with injuries such as damage to reputation or psychiatric injury are not compensable in contract,⁹⁶ irrespective of whether these losses are of a pecuniary or non-pecuniary nature. The headnote rules therefore place the burden of these losses on the employee, regardless of the implied agreement between the parties or the type of damages that might reasonably have been contemplated as a natural result of dismissal in breach of contract. A remark of Lord Steyn is apposite here: ‘One is entitled to pose the question: why was the contract of employment singled out for a special rule to the disadvantage of employees?’⁹⁷ Given the lack of precedential basis for these special rules, it is necessary to consider whether the headnote rules are otherwise justifiable.

IV DOCTRINAL DIFFICULTIES

Having established the lack of a precedential basis for the headnote rules in Part II, this Part considers whether the rules can be justified because of their connection with more fundamental doctrines and principles of contract law. The concept of ‘connection’ is understood in the sense of consistency or coherence. In particular, this Part assesses whether the direct and indirect effects of the headnote rules delineate liability in a manner that is consistent with existing contractual principles of construction and compensatory damages.

A The Indirect Effect and Construction of the Employment Contract

It will be recalled from Part III that, as a result of the indirect effect of the headnote rules, courts have excluded the implied term of mutual trust and confidence from applying to the antecedent processes and actual carrying out of dismissal. As a matter of doctrinal consistency, it is therefore apposite to consider whether this exclusion is a defensible construction of the employment contract as it relates to dismissal.

⁹⁶ See *New South Wales v Paige* (2002) 60 NSWLR 371, 400 [155] (Spigelman CJ), where it was suggested that the law of tort should not be extended into matters concerning the creation and termination of contracts of employment.

⁹⁷ *Johnson* [2003] 1 AC 518, 531 [17].

At its most basic, contractual construction is the ‘process used to determine and give effect to the intention of the parties’.⁹⁸ The ‘institution of contract’ is premised on the assumption that the ‘parties are empowered to create a charter of their rights and obligations inter se’.⁹⁹ As such, construction is integral to the assessment of liability in contract law. Parties are bound by the terms of the contract, and liability arises where a party fails to comply with those terms.

There are a number of evidentiary and legal rules governing the process of construction, which are largely beyond the scope of this article.¹⁰⁰ However, central to this analysis is the role that terms implied in law play in construction of contracts. In the absence of express exclusion,¹⁰¹ terms implied in law are implied into all contracts of a definable class,¹⁰² regardless of the intention of the parties.¹⁰³ McHugh and Gummow JJ have described the nature of these terms as generally reflecting ‘the concern of the courts that, unless such a term [is] implied, the enjoyment of the rights conferred by the contract would or could be rendered nugatory, worthless, or, perhaps, be seriously undermined.’¹⁰⁴

Terms implied in law have assumed a uniquely central role in the construction of employment contracts. Adrian Brooks observes that:

The common law of employment resides to a very large extent in the implied terms of the contract. The law sees these terms as so inherently a feature of ‘employment’ that they will be implied into all employment contracts in default of express provision.¹⁰⁵

The central role of implied terms is necessitated by the typically open-ended nature of the employment bargain.¹⁰⁶ Riley notes that parties to an employ-

⁹⁸ J W Carter, ‘Commercial Construction and Contract Doctrine’ (2009) 25 *Journal of Contract Law* 83, 84.

⁹⁹ *Baltic* (1993) 176 CLR 344, 369 (Brennan J).

¹⁰⁰ See generally Carter, above n 98.

¹⁰¹ See generally *Castlemaine Tooheys Ltd v Carlton & United Breweries Ltd* (1987) 10 NSWLR 468, 490–3 (Hope JA).

¹⁰² *Byrne* (1995) 185 CLR 410, 420 (Brennan CJ, Dawson and Toohey JJ), 448 (McHugh and Gummow JJ).

¹⁰³ *Breen v Williams* (1996) 186 CLR 71, 103 (Gaudron and McHugh JJ).

¹⁰⁴ *Byrne* (1995) 185 CLR 410, 450. See also *Nullagine Investments Pty Ltd v The Western Australian Club Inc* (1993) 177 CLR 635, 647–8 (Brennan J), 659 (Deane, Dawson and Gaudron JJ).

¹⁰⁵ Brooks, above n 22, 29.

¹⁰⁶ *Ibid.*

ment contract 'do not predict at the outset the precise terms of their deal. ... They rely instead on an expectation of cooperation.'¹⁰⁷ Consequently, where the employment relationship disintegrates, courts must look to the implicit agreement between the parties, rather than solely to the express terms of the contract, in order to delineate the extent and nature of the contractual bargain.

The implicit agreement of parties entering an employment contract is a product of social understandings of the nature and purpose of employment. As noted in the introduction to this article, the modern view of employment extends beyond the mere exchange of remuneration for services. In addition to remuneration, the employee gains marketable skills, experience and reputation, personal and financial security, and a sense of identity, dignity and involvement in the community.¹⁰⁸ While these benefits are difficult to define precisely within the contract, courts have given content to them through the implied term of mutual trust and confidence, which embodies the overarching expectation of parties to an employment contract that each will behave fairly and cooperatively in the exercise and fulfilment of their contractual powers and duties.¹⁰⁹

Accepting that the term of mutual trust and confidence now informs all employment relationships, there is no logical justification for excluding such a term from dismissal. The term is not directed to the perpetuation of the employment contract, but rather to regulation of the manner in which the employer's contractual powers are exercised.¹¹⁰ The non-remunerative interests that the implied term protects, such as reputation and mental security, are equally real, and potentially far more exposed, during the lead up to and actual carrying out of a dismissal. As Lord Steyn has remarked, the implied term 'aims to ensure fair dealing between employer and employee, and that is as important in respect of disciplinary proceedings, suspension of an employee and dismissal as at any other stage of the employment relationship.'¹¹¹

¹⁰⁷ Riley, above n 22, 47.

¹⁰⁸ See generally Hugh Collins, *Justice in Dismissal: The Law of Termination of Employment* (Oxford University Press, 1992) 9–23.

¹⁰⁹ See generally Brodie, 'Legal Coherence and the Employment Revolution', above n 16.

¹¹⁰ See Riley, above n 22, 76–7; Freedland, above n 2, 166. But see *Russell (Trial)* (2007) 69 NSWLR 198, 233 [141] (Rothman J) quoted with approval in *Rogan-Gardiner* [2010] WASC 290 (22 October 2010) [116] (Hall J).

¹¹¹ *Johnson* [2003] 1 AC 518, 537 [26].

To suggest that parties entering an employment contract implicitly assume that an employer may, consistently with the contract, treat the employee in any manner he chooses in connection with dismissal creates illogical distinctions in the application of the contract. By excluding mutual trust and confidence from dismissal, the indirect effect means that similar conduct, and indeed sometimes the same course of conduct, must be assessed on the basis of different rules, depending on the stage in the employment relationship at which it occurred.¹¹² Thus, for example, in *Gogay v Hertfordshire County Council*, Hale LJ observed the ‘strange result’ that the defendant employer would have been better off dismissing the employee than suspending her.¹¹³ The consequence of this distinction is that the employer’s liability is not dependent on the express or implied terms of the contract, or the nature of the injurious conduct, but on the proximity of the employer’s actions to dismissal.

The indirect effect of the headnote rules is thus at odds with the basic principle of contractual construction — that construction of the contract should reflect the implied as well as express understandings of the parties upon entering the contract. By imposing on the courts a construction of the employment contract which excludes consideration of the nature of the interaction between the parties in connection with dismissal, the headnote rules engender an unjustifiably restrictive view of the employment bargain. The employee’s enjoyment of the non-remunerative benefits conferred by the contract is potentially rendered worthless during the dismissal process by the employer’s unfettered discretion to treat the employee in whatever manner he or she deems fit. This narrow view does not depend on the express terms of the contract or the inherent aspects of employment embodied in the implied terms. As such, it fails to adequately reflect the social reality of the employment bargain as a contract imbued with obligations of fair treatment and cooperation that extend to all aspects of the employment relationship, including termination. It follows that, as a matter of construction, the manner of dismissal should be subject to the same implied obligations as other aspects of employment.

¹¹² See, eg, *Eastwood v Magnox Electric plc* [2005] 1 AC 503, 531 [39] (Lord Steyn) (*‘Eastwood’*).

¹¹³ [2000] IRLR 703, 711 [69]. In England, this is the result of statutory unfair dismissal legislation: *Johnson* [2003] 1 AC 518. See also *Eastwood* [2005] 1 AC 503, 523 [11] (Lord Nicholls).

B *The Direct Effect and Compensation in Contract*

In addition to the indirect effect, Part III also outlined the direct restrictions that the headnote rules have placed on recovery of damages for dismissal. This article now turns to consider whether these restrictions accord with the basic compensatory principles governing and justifying the award of contract damages.

As Mason CJ has noted in the context of contractual damages:

the fundamental principle on which damages are awarded at common law is that the injured party is to be restored to the position (not merely the financial position) in which the party would have been had the actionable wrong not taken place.¹¹⁴

In contract, the compensatory principle requires that a plaintiff be restored to the position he would have been in but for the breach, subject to the rules of contractual remoteness. Thus the High Court has consistently affirmed that ‘where a party sustains a loss by reason of a breach of contract, he is, so far as money can do it, to be placed in the same situation, with respect to damages, as if the contract had been performed.’¹¹⁵ This broad compensatory objective is not confined to merely restoring the remunerative benefits specified in the contract but rather encompasses all pecuniary losses sufficiently connected to the defendant’s breach.

In the context of dismissal, the question of compensation beyond the notice period remuneration has arisen in relation to three distinct heads of loss — loss of reputation, psychiatric injury and mental distress. Loss of reputation has generally been ‘invoked in a commercial sense’¹¹⁶ to refer to pecuniary losses associated with reduced future employment prospects.¹¹⁷ Such claims are not based on the fact of dismissal itself, which can be effected consistently with the employment contract,¹¹⁸ but on the breach associated with the dismissal, typically preventing the employee from working out the notice period.

¹¹⁴ *Baltic* (1993) 176 CLR 344, 362.

¹¹⁵ *Robinson v Harman* (1848) 1 Ex 850, 855; 154 ER 363, 365 (Parke B). For affirmation by the High Court see, eg, *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64, 80 (Mason CJ and Dawson J), 98 (Brennan J), 117 (Deane J), 134 (Toohey J), 148 (Gaudron J), 161 (McHugh J).

¹¹⁶ *Russell (Appeal)* (2008) 72 NSWLR 559, 572 [55] (Basten JA).

¹¹⁷ See generally *Malik* [1998] AC 20.

¹¹⁸ *Johnson* [2003] 1 AC 518, 539–40 [38]–[42] (Lord Hoffman).

There is nothing inherent in the nature of wrongful dismissal which would make a claim for pecuniary losses flowing from injury to commercial reputation factually untenable. Indeed, courts have sometimes recognised the existence of such injury sustained as a direct result of a failure of notice, either because of the lost opportunity to seek alternative employment from the superior bargaining position of current employment¹¹⁹ or because of the stigma cast on the employee by being peremptorily dismissed.¹²⁰ Moreover, compensation for commercial reputation loss is consistent with the award of compensatory damages in other actions for breach of the employment contract. The classic example of this is the award of damages to public performers and artists for loss of publicity associated with breach of an employment contract.¹²¹ It has also been suggested that loss of employment prospects associated with reputational injury will be recoverable in contract where an employer negligently prepares a reference during the course of employment.¹²²

In light of the demonstrable reality of commercial reputation loss, and the evident ability of employment contract law to remedy such losses under ordinary contractual principles, the application of a special rule precluding recovery of reputational loss in connection with dismissal is unjustified. As Justice Gray has remarked in this context, '[n]o question arises of defamation, nor of exemplary or aggravated damages. The issue is simply one of compensation for the results of a breach of a particular kind.'¹²³

Similar considerations pertain to the restriction pursuant to the headnote rules of pecuniary damages for psychiatric illness. While in practice such claims may face significant evidentiary hurdles because of the difficulties associated with establishing causation,¹²⁴ courts have long recognised that psychiatric injury is a real and compensable form of loss,¹²⁵ particularly in the

¹¹⁹ *Quinn* (2009) 184 IR 279, 282 [9]–[11] (Byrne J).

¹²⁰ *Whelan v Waitaki Meats Ltd* [1991] 2 NZLR 74, 90 (Gallen J). See also *Maw v Jones* (1890) 25 QBD 107, 109 (Lord Coleridge CJ), which involved a wrongfully dismissed apprentice. *Maw v Jones* was distinguished in *Addis*: [1909] AC 488, 493–4 (Lord Atkinson).

¹²¹ See, eg, *White v Australian & New Zealand Theatres Ltd* (1943) 67 CLR 266, 271–2 (Latham CJ), 275 (Starke J) 281–2 (Williams J); *Herbert Clayton & Jack Waller Ltd v Oliver* [1930] AC 209, 220 (Lord Buckmaster).

¹²² *Spring v Guardian Assurance plc* [1995] 2 AC 296, 335 (Lord Slynn). But see *Sullivan v Moody* (2001) 207 CLR 562, 580–1 [54] (Gleeson CJ, Gaudron, McHugh, Hayne and Callinan JJ).

¹²³ Gray, above n 20, 46. See also *Malik* [1998] AC 20, 39 (Lord Nicholls).

¹²⁴ See *Johnson* [2003] 1 AC 518, 542 [48] (Lord Hoffmann).

¹²⁵ *Tame v New South Wales* (2002) 211 CLR 317.

inherently personal and vulnerable context of the employment relationship.¹²⁶ Although perhaps rare in fact, there is no doctrinal reason that an employee should not also be able to recover where a breach of contract connected with dismissal caused the psychiatric injury. Such a claim is unlikely to be tenable on the basis of a bare breach of the notice term¹²⁷ but could conceivably be established on the basis of a contractual breach of the implied term of trust and confidence relating to the manner of dismissal and antecedent investigatory proceedings involving, for example, bullying, abuse or unjustified allegations.¹²⁸ Where an employee can establish the requisite connection between psychiatric injury and the employer's breach, the preclusion of damages is at odds with the fundamental compensatory objective outlined above.

In contrast, the issue of recovery for mental distress caused by breach of the employment contract is far less clear cut. As noted in Part III, the headnote rules have traditionally been applied to exclude this head of damages in dismissal cases. Such exclusion is potentially consistent with the principles governing contractual damages in other circumstances. In *Baltic Shipping Co v Dillon* ('*Baltic*') the High Court affirmed the 'general rule' that damages for mental distress are not available in an action for breach of contract, except where they proceed from physical inconvenience caused by the breach or where the object of the contract in question was to provide enjoyment, relaxation or freedom from molestation.¹²⁹

Notwithstanding the decision in *Baltic*, Justice Gray has opined that there is 'no reason in principle for excluding [mental distress] damages in the event of breach of employment contracts.'¹³⁰ It is certainly arguable that the employment contract falls into one or more of the *Baltic* exceptions, so that in the absence of the headnote rules, mental distress damages would be recover-

¹²⁶ See, eg, *Clunne v Nambucca Shire Council* (1995) 63 IR 304, 315 (Moore J); *Nikolich v Goldman Sachs J B Were Services Pty Ltd* [2006] FCA 784 (23 June 2006) [319] (Wilcox J); *Goldman Sachs JBWere Services Pty Ltd v Nikolich* (2007) 163 FCR 62, 63 (Black CJ), 65 (Marshall J), 66 (Jessup J).

¹²⁷ But see *Grout v Gunnedah Shire Council [No 2]* (1995) 58 IR 67, 75–6 (Moore J), where wrongful dismissal exacerbated the plaintiff's underlying psychological condition.

¹²⁸ See, eg, *Eastwood* [2005] 1 AC 503, 528 [27]–[29] (Lord Nicholls).

¹²⁹ (1993) 176 CLR 344, 365–6 (Mason CJ), 369–70 (Brennan J), 381 (Deane and Dawson JJ), 405 (McHugh J).

¹³⁰ Gray, above n 20, 47.

able.¹³¹ However, for the purpose of this inquiry it is sufficient to note that even if *Baltic* does preclude such recovery, this conclusion does not justify the headnote rule prohibiting compensation for ‘injured feelings’. Either this rule is inconsistent with *Baltic* or it is consistent but superfluous, since it merely replicates the *Baltic* precedent. In both circumstances, the doctrinal consistency of the law would be enhanced by removing the headnote rule and assessing mental distress damages for dismissal in accordance with the general contractual rules laid down by the *Baltic* Court.

The exclusion of specific heads of loss in dismissal cases cannot be justified on the basis of coherence with fundamental contractual principles. As Brodie has remarked, the purported application of *Addis* has formed ‘a barrier to contract [damages] fulfilling [their] normal compensatory function.’¹³² This barrier is unwarranted. It neither reflects the reality of losses associated with dismissal nor the broader legal conception of the employment contract as a bargain entitling the employee to recover not only remuneration, but any pecuniary losses which are sufficiently connected to the employer’s breach.

Insofar as the headnote rules prevent the award of pecuniary losses caused by injury to commercial reputation, and psychiatric injury, they are directly in conflict with the principles that govern damages for breach of other contractual relationships. While the prohibition on mental distress damages may not directly conflict with contractual doctrine, it is also unsupported by general contractual principles. As Lord Hoffman has noted, ‘the development of the common law should be rational and coherent. It should not distort its principles and create anomalies merely as an expedient to fill a gap.’¹³³ The direct restriction of dismissal damages under the headnote rules bears no rational connection to the compensation principle which otherwise guides the award of contractual damages. The headnote rules and their concomitant effects should therefore be abandoned to restore the doctrinal coherence of the law governing employment contracts and contract law more generally.

V NEW DIRECTIONS FOR DISMISSAL LAW

Accepting that the *Addis* headnote rules are flawed, the next logical step is to consider what alternative bases may be developed for determining the

¹³¹ See, eg, *Nikolich v Goldman Sachs J B Were Services Pty Ltd* [2006] FCA 784 (23 June 2006) [315]–[319] (Wilcox J); *Quinn* (2009) 184 IR 279, 286 [28]–[30] (Byrne J). But see *Burazin* (1996) 142 ALR 144, 151–2 (Wilcox CJ, von Doussa and Marshall JJ).

¹³² Brodie, ‘The Beginning of the End for *Addis v The Gramophone Company?*’, above n 21, 232.

¹³³ *Hunter v Canary Wharf Ltd* [1997] AC 655, 707.

contractual damages available to dismissed employees. A natural consequence of removing the headnote rules is that the principles which otherwise apply to the establishment of breach and award of damages under the employment contract will also extend to circumstances of dismissal. In particular, without the direct and indirect effects of the headnote rules, actions for dismissal in breach of contract can include actions based on breach of the implied term of mutual trust and confidence and involve the assessment of damages in accordance with standard contractual principles of causation, remoteness and mitigation. This Part considers the practical consequences of these developments, by first analysing the circumstances in which a dismissal may breach the implied duty of mutual trust and confidence and secondly examining the potential for plaintiff employees who establish a breach in connection with dismissal to recover damages.

A Dismissal in Breach of Mutual Trust and Confidence

Although the term of mutual trust and confidence has not previously been applied to the manner of dismissal, cases considering the term in other contexts provide useful indications of the practical obligations the term would impose on an employer effecting dismissal and, consequently, the circumstances in which a dismissed employee might establish breach of the implied term.

It is important to emphasise that the categories of conduct to which the implied term may apply are not closed. As the Full Court of the Supreme Court of South Australia noted in *South Australia v McDonald*, '[t]his seems inevitable given the open-ended nature of the way in which the duty is expressed.'¹³⁴ However, despite this, the term has been consistently interpreted in Australia as preventing the employer from treating employees unfairly. In the context of dismissal, this prohibition on unfair treatment would include an obligation on the employer to refrain from unsubstantiated allegations about an employee's behaviour¹³⁵ or competency,¹³⁶ bullying and humiliation,¹³⁷ public vilification,¹³⁸ discrimination,¹³⁹ and unjustified

¹³⁴ (2009) 104 SASR 344, 389 [232] (Doyle CJ, White and Kelly JJ).

¹³⁵ *Hem v Cant* (2007) 159 IR 113, 118 [20]–[22] (Finkelstein J) (involving unjustified accusations of theft); *Eastwood* [2005] 1 AC 503, 526–7 [24], 528 [27], 529 [34] (Lord Nicholls), 529 [35] (Lord Steyn) (where the employer fabricated evidence for sexual harassment claim against employee).

¹³⁶ See, eg, *Walker v Northumberland County Council* [1995] 1 All ER 737, 759–60 (Colman J).

¹³⁷ *Triggs v GAB Robins (UK) Ltd* [2007] 3 All ER 590, 598 [34] (Judge Clark).

verbal¹⁴⁰ or physical abuse.¹⁴¹ Engaging in such conduct in connection with dismissal would therefore constitute a breach of the employment contract, regardless of whether the dismissal was or was not also in breach of the requirement to provide notice. Additionally, without the need to contend with the artificial distinction created by the indirect effect, breach could be established in relation to a course of conduct culminating in dismissal.¹⁴²

A particular issue in the context of dismissal is whether the implied term imposes obligations of procedural fairness. Given that Australian courts have generally viewed the exclusion of damages under the manner rule as encompassing proceedings leading up to dismissal, this issue has received little attention. In *Morton v Transport Appeal Board [No 1]*, Berman AJ commented that ‘in deciding what conduct of an employer will damage or destroy mutual trust and confidence, the employee cannot complain that he or she was denied natural justice.’¹⁴³ Nevertheless, Berman AJ considered that the lack of any general obligation to provide procedural fairness did not prevent the Court from determining the procedural implications of the implied term where an investigation had in fact been conducted.¹⁴⁴

This approach accords with the inclusive language of the term, which applies broadly to restrict any conduct that seriously damages or destroys trust and confidence. Consequently, where an employee’s dismissal does include some form of proceedings, the term will require that these proceedings be conducted fairly, although not to the standard expected of a public body or police investigation.¹⁴⁵ However, the term operates only as a restraint on offensive conduct and does not impose any positive obligation on the

¹³⁸ *RDF Media Group plc v Clements* [2008] IRLR 207, 219–21 [112]–[133] (Livesey QC).

¹³⁹ *Thomson v Orica Australia Pty Ltd* (2002) 116 IR 186, 225 [147]–[148] (Allsop J) (employee demoted while on maternity leave).

¹⁴⁰ *Horkulak v Cantor Fitzgerald International* [2005] ICR 402, 407 [76]–[79] (Potter LJ for Potter, Carnwath and Bodey LJJ).

¹⁴¹ See *Western Excavating (ECC) Ltd v Sharp* [1978] 1 QB 761, 772 (Lawton LJ), which discusses sexual harassment.

¹⁴² See, eg, *Eastwood* [2005] 1 AC 503, 522 [6] (Lord Nicholls).

¹⁴³ (2007) 168 IR 403, 431 [164], cited with approval in *Lennon* [2010] SASC 272 (2 September 2010) 41 [179] (Layton J).

¹⁴⁴ *Morton v Transport Appeal Board [No 1]* (2007) 168 IR 403, 431–6 [163]–[203]. See also *King v University Court of the University of St Andrews* [2002] IRLR 252, 255 [20]–[21] (Lady Smith); *Eastwood* [2005] 1 AC 503, 528 [27]–[29] (Lord Nicholls).

¹⁴⁵ *Morton v Transport Appeal Board [No 1]* (2007) 168 IR 403, 430 [162] (Berman AJ).

employer to provide a hearing or investigation, or give reasons for dismissal.¹⁴⁶

It is the lack of any obligation to give reasons for dismissal which allows the term to apply consistently with the employer's right to dismiss the employee by notice. Given the role of implied terms as 'gap fillers', the obligation not to damage or destroy trust and confidence will not impinge on the express contractual rights of the employer.¹⁴⁷ As noted by Lord Hoffman in *Johnson*, this is a crucial consideration in applying the term to dismissal, because as a general rule 'the employer's right to dismiss the employee is strongly defended by the terms of the contract.'¹⁴⁸

Consequently, the term cannot impose a requirement for the employer to have a valid reason for dismissal, since this would prevent the employer exercising its dismissal right except where the reason arose.¹⁴⁹ Additionally, it will generally not be possible to imply the term into a contract containing detailed provision for the manner of dismissal,¹⁵⁰ including express exclusion of any employer obligations in respect of the manner of dismissal. The term 'does not interfere with the employer's right to terminate the employment contract according to its own terms.'¹⁵¹ For individuals employed under contracts which expressly or impliedly exclude obligations of trust and confidence, the establishment of breach in connection with dismissal will be confined to breach of the relevant express contractual terms.

¹⁴⁶ See, eg, *South Australia v McDonald* (2009) 104 SASR 344, 389–90 [233] (Doyle CJ, White and Kelly JJ). But see *Scally v Southern Health & Social Services Board* [1992] 1 AC 294, 306–7 (Lord Bridge), which imposed on the employer an obligation to inform an employee of pension rights).

¹⁴⁷ *Byrne v Australian Airlines Ltd* (1995) 185 CLR 410, 449–50 (McHugh and Gummow JJ), discussing terms implied in law). But see *Russell (Trial)* (2007) 69 NSWLR 198, 229–30 [125]–[128] (Rothman J).

¹⁴⁸ *Johnson* [2003] 1 AC 518, 540 [38].

¹⁴⁹ But see *ibid* 540–1 [42]–[47] (Lord Hoffman).

¹⁵⁰ See, eg, *South Australia v McDonald* (2009) 104 SASR 344, 391 [238]–[239], 398 [270]–[271] (Doyle CJ, White and Kelly JJ), where there was a statutory dismissal procedure.

¹⁵¹ Joellen Riley, 'The Boundaries of Mutual Trust and Good Faith' (2009) 22 *Australian Journal of Labour Law* 73, 80. But see Rothman J in *Russell (Trial)* (2007) 69 NSWLR 198, 229–30 [127], opining that 'if one sought to exclude, expressly, the relationship of trust and confidence, if it were a necessary and essential ingredient of employment, one may still have a contract, but it is unlikely to be a contract of employment.'

B Dismissal Damages under Ordinary Contractual Principles

Once breach is established in connection with dismissal, removal of the headnote rules considerably broadens the potential scope for recovery of damages. Part IV essayed the fundamental compensatory purpose of contractual damages. The plaintiff is ‘not entitled to be made whole’, but rather, to have that which was promised under the contract, or compensation for its loss.¹⁵² The compensatory purpose is qualified by rules relating to causation, remoteness and mitigation. A defendant is only liable for losses that were caused by the breach of contract, in the sense that the loss would not have occurred ‘but for’ the breach.¹⁵³ The presence of multiple causes of the loss, additional to the defendant’s breach, does not negate a finding of causation.¹⁵⁴

Following proof of causation, the extent of permissible recovery is governed by the oft-quoted *Hadley* rules of contractual remoteness. Damages are recoverable provided they may reasonably be considered as ‘arising naturally’ from the breach or ‘may reasonably be supposed to have been in the contemplation of both parties, at the time they made the contract, as the probable result of the breach of it.’¹⁵⁵ Damages may then be reduced by reference to the actions that the plaintiff did take, or could reasonably have taken, to mitigate the loss.¹⁵⁶

Applying these principles to the situation of dismissal in breach of contract yields a potentially far broader scope for recovery than that permitted under the headnote rules. As emphasised by the Supreme Court of Canada in *Fidler v Sun Life Assurance Co of Canada*, these rules make no distinction between the types of loss that may be recovered.¹⁵⁷ ‘The law’s task is simply to

¹⁵² *Vorvis v Insurance Corporation of British Columbia* [1989] 1 SCR 1085, 1107 (McIntyre J for Beetz, McIntyre and Lamer JJ).

¹⁵³ *March v E & M H Stramare Pty Ltd* (1991) 171 CLR 506, 515–16 (Mason CJ); *Bennett v Minister of Community Welfare* (1992) 176 CLR 408, 413 (Mason CJ, Deane and Toohey JJ), 418–19 (Gaudron J).

¹⁵⁴ *Fitzgerald v Penn* (1954) 91 CLR 268, 272–3 (Dixon CJ, Fullagar and Kitto JJ); *Monarch Steamship Co Ltd v Karlshamns Oljefabriker (A/B)* [1949] AC 196, 227 (Lord Wright).

¹⁵⁵ *Hadley* (1854) 9 Ex 341, 354; 156 ER 145, 151 (Alderson B for Parke, Alderson, Platt and Martin BB). See also *Burns v MAN Automotive (Aust) Pty Ltd* (1986) 161 CLR 653, 658 (Gibbs CJ), 667 (Wilson, Deane and Dawson JJ), 673 (Brennan J); *Hungerfords v Walker* (1989) 171 CLR 125, 140–4 (Mason CJ and Wilson J), 161 (Dawson J); *Commonwealth v Amann Aviation Pty Ltd* (1991) 174 CLR 64, 174 (McHugh J); *Baltic* (1993) 176 CLR 344, 367–8 (Brennan J).

¹⁵⁶ See, eg, *Dyer v Peverill* (1979) 2 NTR 1, 7–8 (Muirhead J). See generally Freedland, above n 2, 362–6.

¹⁵⁷ [2006] 2 SCR 3, 19–20 [44] (McLachlin CJ and Abella J).

provide the benefits contracted for, whatever their nature, if they were in the reasonable contemplation of the parties.¹⁵⁸ The remoteness test is inherently flexible and capable of expanding the boundaries of liability in response to both evolving societal understandings of cause and effect and the unique circumstances of a particular contract. Given this flexibility, it is inevitable that once the impediments of the headnote rules are removed, the scope for recovery of loss flowing from dismissal will respond to changing conceptions of the employment relationship. In particular, the heads of loss that may arise ‘naturally’ from breach of the term of mutual trust and confidence conceivably encompass both reputational injury¹⁵⁹ and psychiatric harm.¹⁶⁰

The potential flexibility of contractual remoteness in the area of dismissal is demonstrated by the case of *Quinn v Gray*, in which Byrne J upheld an arbitrator’s award of damages for wrongful dismissal which included provision for the value of the lost opportunity to seek alternative employment from a position of employment.¹⁶¹ Byrne J considered that *Addis* was confined to the question of exemplary damages and did not affect the award of compensatory damages. Although accepting that the usual measure of such damages was the remuneration that the employee had lost during the notice period, he concluded that ‘if further or other loss is demonstrated to flow from the breach, there is no reason why it should not be recoverable.’¹⁶² On the basis of ordinary contractual principles, damages therefore included compensation for the pecuniary losses associated with injury to commercial reputation.

A similar although more radical approach was adopted by the High Court of New Zealand in *Whelan v Waitaki Meats Ltd* (‘*Whelan*’).¹⁶³ The case concerned a competent employee in a managerial position, who was dismissed with a few days notice after 29 years of service.¹⁶⁴ Gallen J declined to follow *Addis* and held that, in the circumstances, the plaintiff’s employment contract contained implied terms to the effect that he ‘would be treated by his employer in such a manner as to enable him to retain his dignity within the community and not to have his status affected by a precipitate act open to

¹⁵⁸ *Ibid* 20 [44].

¹⁵⁹ See, eg, *Malik* [1998] AC 20, 37 (Lord Nicholls).

¹⁶⁰ See, eg, *Eastwood* [2005] 1 AC 503, 528 [29] (Lord Nicholls).

¹⁶¹ (2009) 184 IR 279.

¹⁶² *Ibid* 282 [11].

¹⁶³ [1991] 2 NZLR 74. See also *Ogilvy & Mather (New Zealand) Ltd v Turner* [1996] 1 NZLR 641, 653–4 (McKay J for Cooke P, Richardson, Gault, McKay and Thomas JJ); *Stuart v Armour-guard Security Ltd* [1996] 1 NZLR 484, 510–11 (McGechan J).

¹⁶⁴ *Whelan* [1991] 2 NZLR 74, 79 (Gallen J).

misinterpretation.¹⁶⁵ Given that the dismissal had breached these terms, Gallen J awarded \$50 000 for the ‘undue mental distress, anxiety, humiliation, loss of dignity and injury to feelings’ that the plaintiff ‘undoubtedly sustained as a direct result’.¹⁶⁶

Although the *Whelan* implied terms have not received any support in Australia, it is likely that, in the absence of the headnote rules, similarly broad mental distress damages could flow from a breach of mutual trust and confidence connected with dismissal. As Byrne J noted in *Quinn v Gray*, the object of mutual trust in the circumstance of dismissal is to provide peace of mind to the employee and freedom from molestation.¹⁶⁷ Consequently, the implied term appears to fit within the exceptions to the general rule outlined in *Baltic*, so that in appropriate circumstances damage for mental distress caused by the manner of dismissal may be recovered.

However, situations in which a dismissed employee could establish mental distress flowing from breach of the implied term are likely to be comparatively rare. This is because of the difficulty of demonstrating that the distress was caused by the breach, rather than the dismissal itself. This issue was considered by the Supreme Court of Canada in *Honda Canada Inc v Keays*.¹⁶⁸ The Court recognised ‘[an] expectation by both parties to the [employment] contract that employers will act in good faith in the manner of dismissal’¹⁶⁹ and opined that, in appropriate circumstances, the employee could recover compensation for mental distress caused by bad faith dismissal.¹⁷⁰ However, the Court emphasised that damages for ‘[t]he normal distress and hurt feelings resulting from dismissal are not compensable’, since at the time the employment contract is formed, ‘dismissal is a clear legal possibility’ meaning that liability for damage resulting from the dismissal itself would not be in the contemplation of the parties.¹⁷¹

¹⁶⁵ Ibid 89.

¹⁶⁶ Ibid 90.

¹⁶⁷ (2009) 184 IR 279, 285–6 [26]–[29].

¹⁶⁸ [2008] 2 SCR 362.

¹⁶⁹ Ibid 391 [58] (Bastarache J for McLachlin CJ, Bastarache, Binnie, Deschamps, Abella, Charron and Rothstein JJ). This expectation was suggested to arise as a result of the decision in *Wallace v United Grain Growers Ltd* [1997] 3 SCR 701, 742–3 [95]–[98] (Iacobucci J for Lamer CJ, Sopinka, Gonthier, Cory, Iacobucci and Major JJ).

¹⁷⁰ *Honda Canada Inc v Keays* [2008] 2 SCR 362, 391 [59] (Bastarache J for McLachlin CJ, Bastarache, Binnie, Deschamps, Abella, Charron and Rothstein JJ).

¹⁷¹ Ibid 390 [56].

C Overall Consequences: Compensation and Consistency

As the above analysis demonstrates, overturning the headnote rules could significantly broaden the potential liability of the employer in connection with dismissal. Without the direct and indirect effects of the headnote rules, there is no legal barrier to the application of mutual trust and confidence, and ordinary compensatory damages principles, to instances involving dismissal. The employer's obligation to refrain from unfair treatment of employees would therefore apply consistently to all actions under the employment contract. The employee would thus have contractual protection against conduct that undermines the non-remunerative benefits that employees derive from employment, such as reputation and self-esteem. Moreover, where a breach of mutual trust and confidence or another contractual term occurred in connection with dismissal, the employee could be compensated for losses sustained as a natural result of the wrong, in the sense of being placed in the position he would have been in but for the breach. Such losses could extend not only to payment of notice period remuneration, but commercial reputation and psychiatric injury damages and, in appropriate circumstances, mental distress damages.

It is important to emphasise, however, that this does not mean the employer's liability for dismissal is at large. Under the Australian conception of mutual trust and confidence, the employer is only required to refrain from unfair treatment and does not have any positive duty of fair dealing. Additionally, where breach does occur, establishing causation and damage is likely to prove problematic for many plaintiffs. The rules of contractual remoteness will still operate to limit the employer's liability to the damages that were in the reasonable contemplation of the parties upon entering the employment contract.¹⁷² Neither the extension of mutual trust and confidence nor contractual damages principles inhibits the employer's right to dismiss the employee with notice, provided the dismissal is not carried out in a harsh and unjust manner.

Removal of the headnote rules merely puts dismissed employees on the same legal footing as other contracting parties. By realigning the assessment of breach and quantification of damages for dismissal with the principles that otherwise govern the employment contract, claims for breach of the employment contract can be determined consistently with the social reality of the employment relationship and the compensatory objective of contractual damages. The terms of the employment contract may then be construed in

¹⁷² See generally the comments of Lord Steyn in *Malik* [1998] AC 20, 52.

accordance with the inherent obligations of fairness and cooperation that inform the modern employment relationship. While this adjustment has significant implications for dismissed employees, it does not require a radical upheaval in contract law. The expansion of mutual trust and confidence and existing contractual damages principles to dismissal is the incremental and natural result of dispensing with the headnote rules. If the effects of the headnote rules are removed, the common law can develop in a manner that allows for the coherent, principled assessment of contractual dismissal damages.

VI CONCLUDING REMARKS

Despite significant statutory reforms, the contract of employment continues to be the primary source of protection for many dismissed employees. In light of this, the restrictions imposed on contractual dismissal actions by the *Addis* headnote rules are of continuing social and legal relevance. This article has sought to provide a greater understanding of the nature of these restrictions and to critically assess whether their continued application is justified. Analysis of Australian cases applying *Addis* demonstrates the unique difficulties faced by plaintiff employees. Both in attempting to establish breach and recover loss, dismissed employees are subject to the direct and indirect effects of the headnote rules. This result is unwarranted. It is neither mandated by legal precedent nor supported by a connection with more fundamental principles of contractual doctrine.

The promulgation of the *Addis* headnote rules is largely the product of historical accident in the way the decision in *Addis* was reported. However, the rules have influenced dismissal law for over a century, and it is likely that their rejection in Australia must await a conclusive determination by the High Court. Should the headnote rules be overturned, the law of dismissal will then be able to develop in a doctrinally coherent manner, which facilitates the consistency of implied obligations governing the employment relationship and the compensatory objective of contractual damages. Removing the headnote rules would increase the legal protection afforded to those employees who fall outside the statutory unfair dismissal scheme and would realign the contractual rights of employees with other contracting parties.

Most importantly, these developments would constitute further legal recognition of the social reality of employment, as a relationship which extends beyond the exchange of remuneration for services and constitutes 'one of the defining features of people's lives'.¹⁷³

¹⁷³ *Johnson* [2003] 1 AC 518, 549 [77] (Lord Millett) quoting *Wallace v United Grain Growers Ltd* [1997] 3 SCR 701, 742 [94] (Iacobucci J for Lamer CJ, Sopinka, Gonthier, Cory, Iacobucci and Major JJ).