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Challenges to Law Firm Mandatory-Retirement Policies

By Gary Phelan and Cara E. Greene

A 2006 survey report indicated that 57% of law firms with 100 or more attorneys have mandatory retirement age policies. *See*, L. Jones "Pitfalls of Mandatory Law Firm Retirement," *National Law Journal*, May 24, 2006. But legal challenges to mandatory retirement policies at law firms are likely to become more common as baby boomers reach retirement age.

The debate over whether a law firm can have a mandatory retirement age has focused on the threshold question of whether the "partner" is deemed an "employer" or an "employee." For each class of lawyer, this article explores possible legal remedies.

ADEA Remedies for "Employees"

The *Age Discrimination in Employment Act* (ADEA), as its name implies, prohibits discrimination on the basis of age by employers against employees who are over the age of 40. The ADEA is straightforward in its prohibition of mandatory retirement policies: Involuntary retirement predicated on age is forbidden except in instances where age is a bona fide occupational requirement or the employee is a bona fide executive who retires pursuant to a plan with a minimal annual benefit of at least $44,000. *See*, 29 U.S.C. §§623(f), 631(c). Put simply, an employer cannot require an employee to retire simply because he or she has reached a certain age. *See*, *EEOC v. Johnson & Higgins, Inc.*, 91 F.3d 1529, 1540 (2d Cir. 1996); *Stipkala v. American Red Cross*, 215 F.3d 1327 (6th Cir. 2000) (unpublished) ("If an employer uses a mandatory retirement policy to force an employee to retire, the policy violates the ADEA unless the employer can establish that age is a *bona fide* occupational qualification.")

If a partner is *not* a bona fide partner under the legal principles discussed below, s/he may be protected by the ADEA as an "employee" and be able to challenge mandatory retirement on that basis.

Sidley Austin Case

In 2002, the Equal Employment Opportunity Commission (EEOC) filed an age discrimination charge against Chicago-based Sidley Austin Brown & Wood, claiming that the firm violated the ADEA by demoting 32 older equity partners to non-equity status and by implementing a mandatory retirement age policy.

After three years of legal skirmishing at the administrative level, the EEOC filed an ADEA lawsuit in the U.S. District Court in 2005. The trial court aptly noted that the case had "been of great interest not only to Sidley, but also to most other large law firms across the country." *EEOC v. Sidley Austin*, 406 F.Supp.2d 991, 995 (N.D. Ill. 2005).

As of this writing, the EEOC's lawsuit against Sidley Austin has not yet provided guidance to the profession. It is clear, however, that partnerships are not exempt from the ADEA, nor are partners automatically excluded from the protections of the ADEA. *See*, *EEOC v. Sidley Austin*, 315 F.3d 696, 702 (7th Cir. 2002). A law firm's characterization of an individual as a partner certainly does not answer the question, because a partner is not always an employer. *Id.* In fact, a person who is a partner for purposes of state partnership law may very well be an employee for purposes of discrimination law. *Id.* The crux of the issue, then, is whether a partner is an "employer" or "employee" under the ADEA. Help for making that distinction has been sought in related laws such as the American with Disabilities Act (ADA).

In *Clackamas Gastroenterology Associates, P.C. v. Wells*, 538 U.S. 440 (2003) (considering whether director-shareholder physicians were employees for purposes of ADA Title I, 42 U.S.C. §12201 *et. seq*.) the Supreme Court explained that, when deciding whether a partner might be considered an "employee" under federal employment discrimination statutes, the fundamental question is "whether the individual acts independently and participates in managing the organization, or whether the individual is subject to the organization's control." *Id.* at 449. According to the Supreme Court, when making that inquiry "the common-law element of control is the principal guidepost." *Id.* at 448. *Clackamas* endorsed the EEOC's six-factor test as being relevant to the inquiry:

1. Whether the organization can hire and fire the individual or set the rules and regulations of the individual's work;

2. Whether and, if so, to what extent the organization supervised the individual's work;

3. Whether the individual reports to someone higher up in the organization;

4. Whether and, if so, to what extent the individual is able to influence the organization;

5. Whether the parties intended that the individual be an employee, as expressed in written agreements or contracts; and

6. Whether the individual shares the profits, losses and liabilities of the organization.

Id. at 449-50 (citing EEOC Compliance Manual §605:0009).

The *Clackamas* factors are non-exhaustive. *Clackamas*, 538 U.S. 450, n.10. In the law firm context, there are many things that may be indicative of whether a partner is an employee for purposes of discrimination laws. By examining a partner's autonomy, authority and liability, we may determine to what degree the partner is subject to the firm's control and, in turn, whether he or she is an employer or employee.

A Partner's Autonomy

The first, second and third factors of the *Clackamas* test relate to the autonomy of a partner. Since control is the fundamental hallmark of an employer-employee relationship, autonomy is a strong indication of a bona fide partnership. The less authority and discretion a partner has over the terms of his or her employment, the more likely that he or she is an employee under the ADEA. *See, Caruso v. Peat, Marwick, Mitchell & Co.*, 664 F. Supp. 144 (S.D.N.Y. 1987) (*Caruso I*) (holding that partner of accounting and consulting firm was an employee under the ADEA and stating "the title 'partner' is not normally applied to an individual whose employment duties are unilaterally dictated by another member of a business").

In the law firm context, relevant indicia of control may include whether a partner must:

1. Submit a certain number of billable hours per month;
2. Submit daily time entries;
3. Obtain approval to introduce new clients;
4. Obtain approval to introduce new business from existing clients;
5. Obtain approval for "write-off" authorizations;
6. Obtain approval for marketing expenses;
7. Obtain approval for reimbursement of expense disbursements;
8. Work in an assigned practice area;
9. Meet assigned quarterly fee collection goals; and
10. Obtain approval before undertaking a legal course of action. Cf., *Hishon v. King & Spalding*, 467 U.S. 69, 80 n.3 (1984) (Powell concurring) (outlining decisions that should be made among the partnership).

The ability to terminate an individual's employment is a strong indication of control. *See, Zheng v. Liberty Apparel Co. Inc.*, 355 F.3d 61 (2d Cir. 2003) (considering whether defendant was joint employer under the FLSA). Therefore, to the extent that a partner summarily can be fired, he or she may not a bona fide partner at all. Under traditional partnership law, a partner may not be expelled from the partnership absent an expulsion provision in the partnership agreement. *See, Ehrlich v. Howe*, 848 F. Supp. 482, 490 (S.D.N.Y. 1994); *Beasley v. Cadwalader, Wickersham & Taft*, 1996 WL 449247, at 1 (Fla. Cir. Ct. Mar. 29, 1996) (interpreting New York law); *see also*, *Dawson v. White & Case*, 672 N.E.2d 589, 591-92 (N.Y. 1996) (without termination provision in partnership agreement, dissolution is the only method of removing a partner).

Even where an expulsion provision exists, expulsion pursuant to such a provision must be undertaken in good faith. *See*, *Winston & Strawn v. Nosal*, 664 N.E.2d 239, 240 (Ill. App. Ct. 1996) (citing *Bohatch v. Butler & Binion*, 905 S.W.2d 597, 602 (Tex. App. 1995)); *Holman v. Coie*, 522 P.2d 515, 523-24 (Wash. Ct. App. 1974) (expulsion provision contained no language requiring that expulsions be for cause, and court refused to imply a cause requirement). The more authority a firm has to fire an individual, the more indicative it is that the individual is not acting as an autonomous partner, but as an employee under the control of the firm. *See*, *Caruso I*, 664 F. Supp. at 149 ("The typical firm may not fire a partner or otherwise terminate his employment merely because of disappointment with the quantity or quality of his work, but may only remove the partner in extraordinary circumstances.")

A Partner's Authority

A true partnership contemplates that "decisions important to the partnership normally will be made by common agreement or consent among the partners." *Hishon*, 467 U.S. at 80 (1984) (Powell concurring).

Conversely, the less authority a partner exercises, the less likely it is that the partner is exempt from the protections of the ADEA. *See, Smith v. Castaways Family Diner,* 453 F.3d 971 (7th Cir. 2006).

Many law firms have a highly centralized management structure where the majority of partners have little if any say in the day-to-day operations of the firm. *See, Clackamas*, 538 U.S. at 446 ("Today there are partnerships that include hundreds of members, some of whom may well qualify as 'employees' because control is concentrated in a small number of managing partners.") Many partners are thus "relegated to the position of an employee subject to the virtually absolute, unilateral control of the Management Committee." *Simpson v. Ernst & Young,* 100 F.3d 436, 442 (6th Cir. 1996). In *Simpson*, the Sixth Circuit concluded that a partner was covered under the ADEA — reasoning, in part, that the plaintiff, a partner of a large accounting firm, had no authority to direct or participate in the admission or discharge of partners or other firm personnel, did not participate in determining partners' or other personnel's compensation, and could not participate in annual performance reviews. *Id.* at 441-42.

Even though partners may be able to vote in firm elections, or even elect the members of the managing committee, this alone is not enough to place partners in an "employer" role. For instance, in *Caruso v. Peat, Marwick, Mitchell & Co.*, 717 F. Supp. 218 (S.D.N.Y. 1989) (*Caruso II*), the court held that a principal in a large accounting firm could still be considered an "employee" under the ADEA even though he could vote in firm elections. The court reasoned that the issues decided in those elections were "largely decided by upper level management, which merely presented its decisions for ratification by the employees who voted." *Id.* at 222.

A Partner's Liability

The final factor in the *Clackamas* test addresses the monetary compensation of a partner. "Partners typically receive their compensation as a percentage of their firm's profits, rather than in the form of a fixed hourly wage or weekly salary." Caruso I, 664 F. Supp. at 149 ("Profit sharing is the primary attribute of partnership.") (citing A. Bromberg, *Crane and Bromberg on Partnership* 66 (1968); *see also, Tenney v. Insurance Company of North America,* 409 F.Supp. 746, 749 (S.D.N.Y.1975) ("the pro rata sharing of profits and losses of the enterprise" is a "significant indicia of the existence of a partnership"). Non-equity partners, then, likely would fall within the confines of the ADEA.

Many partners do share in their firm's profits, losses and liabilities, and make a capital investment in the firm. These facts alone, however, do not support a conclusion that a partner falls outside the protections of the ADEA. For example, in *Sidley Austin*, the demoted equity partners made capital contributions to the firm, had capital accounts which averaged about $400,000 each, were liable for the firm's debts, and their income included a share of the firm's profits. *Sidley Austin*, 315 F.3d at 699. Nevertheless, the Seventh Circuit rejected the defendant's argument that the 32 demoted partners were not "employees" under the ADEAn — reasoning, in part, that the firm's executive committee could fire them, demote them, and raise and lower their pay. *Id.* Similarly, in *Simpson,* the court found that despite liability for firm losses, the partner was simply "an employee with the additional detriment of having promised to be liable for the firm's losses." 100 F.3d at 442.

REMEDIES FOR BONA FIDE PARTNERS

Under ADEA, a bona fide partner is an "employer" and therefore not protected from mandatory retirement policies. Such a partner may still be able to challenge the policy, however, under state or local statutes or under common law.

Statutes

State or city anti-discrimination laws may have a broader definition of "employee" than that in ADEA. For example, the New York City Human Rights Law extends its coverage to any "person." N.Y. Admin. Code §8-107(a); *Jowers v. DME Interactive Holdings, Inc.*, 2003 WL 230739 (S.D.N.Y. Feb. 4, 2003) (NYCHRL applies to "natural persons" who "carry out the work in furtherance of the employer's business enterprise").

Common Law and Code of Professional Responsibility

A “bona fide” partner without any statutory protection against discrimination may also argue under common law that the firm breached its fiduciary duty and its covenant of good faith and fair dealing when it terminated him or her based on age. As recently observed:

> Finally, a word of warning for law firms that observe the Sidley proceedings and conclude that the lack of guidance can be viewed as acquiescence. Partnership creates a fiduciary relationship. Thus if the Sidley case finally concludes that large law firm partners are “employers” for purposes of anti-discrimination laws, the fiduciary relationship itself could encompass a prohibition against discrimination based on the duty of good faith and fair dealing in the context of partner expulsions.

B. Plevin and J. Wang, “When is a Partner Not a Partner,” *New York Law Journal* (May 22, 2006).

No case law squarely holds that terminating a law firm partner on a discriminatory basis is a breach of fiduciary duty. In New York, however, the foundation for that argument has been laid. There is “an implied term of good faith” in all partnership agreements in New York. *Gold Medical Group v. Webber*, 41 NY. 2d 680, 684 (1977). In *Meinhard v. Salmon*, 249 N.Y. 458(1928), Justice Cardozo remarked that the fiduciary duty among partners is a duty of “finest loyalty” and “honor most sensitive.” *Id.* at 463-64.

In *Beasley v. Cadwalader, Wickersham & Taft*, 1996 WL 449247 (Fla. Cir. CT. March 29, 1996), *rev’d in part on other grounds,* 1998 WL 405919 (Fla Dist. Ct. App. July 22, 1998), the court, while interpreting New York law, held that the law firm violated its fiduciary duty when it expelled the plaintiff and other partners in a downsizing effort to provide financial gain to other partners. *Id.* at 5-6. (After Cadwalader had a difficult financial year in 2004, several younger, more productive partners at the firm were upset with their compensation. *Id.* at 2. Cadwalader partner Robert Link told the management committee in a memo that, if changes were not made quickly, he was going to leave the firm and that many of the other “Young Turks” would soon follow. *Id.* As a result, the Management Committee adopted “Project Right Size” that was aimed at identifying less productive partners for elimination from the partnership by increasing the shares of more productive partners and decreasing the shares of less productive partners. *Id.* In upholding the plaintiff's breach of fiduciary duty claim, the court explained that:

> These facts compel the conclusion that the management committee breached its fiduciary duty to Beasley. This was not a situation where the management committee was merely fulfilling its management function. Rather, it was participating in a clandestine plan to wrongfully expel some partners for the financial gain of the other partners. Such activity can not be said to be honorable, much less to comport with the punctilio of an honor. *Id.* at 6.

After concluding that a law firm partner was not an "employee" under ERISA, the court in *Ehrlich v. Howe*, 848 F. Supp 482 (S.D.N.Y. 1994), concluded that the partner stated a breach of fiduciary duty claim when it excluded him from secret meetings where it voted to expel him from the partnership. *Id.* at 490-92.

The district court in *Simpson v. Ernst & Young*, 850 F. Supp. 648 (S.D.Ohio 1994), *aff'd*, 100 F.3d 436 (6th Cir. 1996), emphasized that the legal obligation of a fiduciary duty obligated partners to treat each other with "the highest degree of fidelity, loyalty and fairness in their mutual dealings" and to avoid falling back on the "morals of the marketplace" when dealing with each other. *Id.* at 656.

A law firm also violates the fiduciary duty amongst partners if the firm terminates a partner for a reason that violates the Code of Professional Responsibility. Section 1200.3 of New York State Disciplinary Rules of the Code of Professional Responsibility states that "a lawyer or law firm shall not … discriminate in the practice of law, including in hiring, promoting or otherwise determining conditions of employment, on the basis of age, race, creed, color, national origin, sex, disability, marital status or sexual orientation."

In *Weider v. Skala*, 80 N.Y. 2d 628 (1992), for example, the New York Court of Appeals relied upon the lawyer's ethical obligations to carve out a rare exception to New York's firmly entrenched employment-at-will doctrine. The plaintiff claimed that he was terminated because he reported another associate's ethical misconduct. The Court of Appeals concluded that there was a “distinctive relationship” between an attorney and a law firm because the lawyer’s duties as an associate of the firm and as an attorney are “so closely linked as to be incapable of separation.” *Id.* at 635. Weider endorsed the plaintiff’s argument that there was an implied understanding that was:

> [S]o fundamental to the relationship and essential to its purpose as to require no expression: that both the associate and the firm in conducting the practice will do so in accordance with the ethical standards of the profession. Erecting or countenancing disincentives to compliance with the applicable rules of professional conduct … would subvert the central professional purpose of his relationship with the firm — the lawful and ethical practice of law.

Id. at 636.

The Court of Appeals emphasized that the legislature delegated responsibility to the Appellate Division Departments to maintain ethics and competence standards. *Id.* The Code of Professional Responsibility codifies those standards of ethics and competence. *Id.* Just as there is an implied contract that a law firm will not terminate an associate for complying with that Code, there is an implied contract that a law firm will not terminate an attorney — whether a partner or an associate — for reasons that would violate the Code of Professional Responsibility. *Id.*

CONCLUSION

Although the majority of large law firms may endorse mandatory retirement age policies, the legality of such policies is far from certain. Furthermore, the support mandatory retirement policies enjoy in large firms does not necessarily resonate throughout the profession. Over the next few years, lawyers generally and employment law practitioners specifically will be grappling with the legal issues raised when some baby boomer lawyers are told “it’s time” and they respond, “I don’t think so.”

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