Masters or Servants?

EEOC continues to target age-based partnership restrictions.

BY KEVIN LAURI, FELICE EKELMAN AND SAMANTHA ABYESEKERA

On Jan. 28, 2010, the venerable firm of Kelley Drye & Warren was hit with an age discrimination suit by the Equal Employment Opportunity Commission on behalf of its partners aged 70 and above. The complaint alleges that under Kelley Drye’s partnership agreement, attorneys reaching the age of 70 must (1) give up their equity interest in the firm; (2) relinquish their authority to manage or significantly influence the firm; and (3) be compensated via a wholly discretionary bonus payment decided upon by the firm’s executive committee.

The situation Kelley Drye finds itself in is not new. In 2007, Sidley Austin paid $27.5 million to end an age discrimination suit brought by the EEOC on behalf of 32 former partners. That settlement certainly reverberated within the large law firm community in the following months, as Dewey & LeBoeuf, Pillsbury Winthrop Shaw Pittman, Cadwalader, Wickersham & Taft, and others eliminated their age-based limitations on partnership status.

Whether Kelley Drye is forced to follow in Sidley’s footsteps and enter into a costly settlement remains to be seen, but one thing is certain: the outcome of the case will turn on whether Kelley Drye’s “partners” are truly partners, and not employees, such that they are exempt from the Age Discrimination in Employment Act.

That issue has far-reaching implications not just for law firms, but for all professional partnerships.

THE TEST OF A ‘TRUE PARTNER’

Analysis of whether an individual is a true partner or just an employee begins with Clackamas Gastroenterology Associates v. Wells, 538 U.S. 440 (2003), the U.S. Supreme Court case that held that the common law “element of control” standard governs. At issue in the case was whether a former bookkeeper could sue a medical clinic in Oregon for disability discrimination under the Americans With Disabilities Act.

The clinic, organized as a professional corporation, would not meet the 15-employee threshold to invoke the jurisdiction of the ADA unless the four doctors who owned it as shareholders and directors were counted as employees. The Court solely relied on the EEOC guidelines’ six-factor test for determining whether a partner is an employee:

1. whether the firm can hire or fire the individual or set the rules and regulations of the individual’s work;
2. whether and to what extent the firm supervises the individual’s work;
3. whether the individual reports to someone higher in the organization;
4. whether and to what extent the individual is able to influence the firm;
5. whether the parties intended that the individual be an employee, as expressed in written agreements or contracts; and
6. whether the individual shares in the profits, losses, and liabilities of the organization.

New York courts have consistently applied the EEOC factors endorsed by Clackamas. For example, Rodal v. Anesthesia Group of Central New York, 2006 U.S. Dist. LEXIS 98111 (N.D.N.Y. Jan. 23, 2006), was remanded in light of Clackamas.

The Northern District there held that a physician alleging disability discrimination was an employer because his work was largely unsupervised; he did not report to anyone higher within the group; he influenced the group by overseeing the residency program, representing the group at national meetings, developing equipment modification procedures, and supervising the group’s business office; and, he drew a salary based on his equal share of the group’s profits and losses.

The fact that plaintiff had an employment agreement that specified grounds for termination and that his daily schedule was, in large part, determined by a rotating daily supervisor failed to detract from his employer status.

And in Fitzgibbon vs. Putnam Dental Associates, P.C., 368 F. Supp. 2d 339 (S.D.N.Y. 2005), the Southern District applied the Clackamas factors in holding that a dentist who was the sole shareholder of a professional corporation was clearly not an employee for the purposes of meeting Title VII’s 15-employee minimum. It does not appear, however, that courts in the Second Circuit have applied the Clackamas factors in the law firm context.

But courts in other circuits have. In Solen v. Kaplan, 398 F.3d 629 (2005), the Seventh Circuit held that the managing partner of a small law firm who held one-quarter of its voting power, exercised substantial control over the allocation of profits and the elevation of new partners, and further, served as the trustee of the firm’s 401(k) account was an employer.

Although plaintiff argued that the powers given to him by the partnership agreement were meaningless because he was supervised by the other partners and consulted with his fellow partners before making decisions, the court held that his evidence “may demonstrate that he was passive, but it does not show he was powerless.”

In Panepucci v. Honigman Miller Schwartz and Cohn, LLP, 408 F. Supp. 2d 374 (E.D. Mich. 2005), a Michigan district court declined to dismiss a law firm partner’s gender discrimination claims because she alleged that she was regularly reviewed and evaluated by more senior partners, her voting rights were largely a sham because dissent resulted in adverse consequences, and her compensation was determined by a subjective evaluation of her performance made by a small compensation committee.

Judge Richard Posner’s opinion in EEOC v. Sidley Austin Brown & Wood, 315 F.3d 1696 (7th Cir. 2002), as to whether an EEOC subpoena could be enforced on jurisdictional grounds, left open the issue of whether those in the title of partner were really employees. Although the decision pre-dated Clackamas, the court noted that despite there being over 500 equity partners, all decision-making authority resided in a 36-member, unelected committee.

Judge Posner was not persuaded by Sidley’s argument that the entire partnership directed the firm because the committee exercised its “absolute power by virtue of delegation by the entire partnership in the partnership agreement.” Nor was profit-and loss-sharing dispositive, as courts regularly found shareholders of professional corporations to be employees for the purposes of federal anti-discrimination laws.

WEIGH THE ISSUES CAREFULLY

Regardless of title, in order to be a “true partner,” individuals must work independently, be relatively free
from supervision, oversee significant aspects of firm administration, and be able to express their opinions on the direction of the firm and exercise real decision-making authority without fear of repercussions.

Law firms and other professional partnerships would be well served to address their partnership policies now, not just because of renewed targeting by the EEOC, but because the baby boomer population that entered professions in 1980 is beginning to reach an age where mandatory, age-based retirement will be a significant and recurring issue.

Some argue that there are benefits to mandatory retirement/de-equitization provisions, and that may indeed be true. Such provisions may, in some part, encourage smoother transitions between partners and the continuance of client relationships, as well as leadership by younger partners.

But such abstract benefits should be carefully and cautiously weighed against the attendant risk that policies based solely on age are easy targets for future legal challenges. Should a firm seek to maintain such policies based solely on age are easy targets for future legal challenges. Should a firm seek to maintain such provisions, it should take measures to ensure that partners are not actually employees under the law. The following steps should be helpful:

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  - Ensure that, to the extent authority is vested in partners, definitions require professional partnerships, at the very least, to do the following:
  - Hold regular meetings where voting and other decision-making takes place,
  - Ensure that, to the extent authority is vested in a smaller executive committee, the committee reports to the general partnership and is regularly elected.

The more prudent approach is to institute alternatives to age-based policies, which are triggered by objective criteria such as productivity, quality of work and business generation.

Even assuming, however, that a firm's age-based retirement/de-equitization policies pass muster such that partners exercise the requisite element of control and are foreclosed from bringing claims while partners, the issue of how a firm could defend against a former partner's claim, brought in his or her capacity as an employee, that his significant loss in compensation, if the business goal is the transition of clients from older "partners" to younger ones, whether productivity is questionable.

The EEOC proposes revising 29 C.F.R. §1625.7(b) to set forth a non-exhaustive list of six factors to consider in determining whether an employment practice is based on reasonable factors other than age. Those factors are:

1. whether the employment practice and the manner of its implementation are common business practices;
2. the extent to which the factor is related to the employer's stated business goal;
3. the extent to which the employer took steps to define the factor accurately and to apply the factor fairly and accurately (e.g., training, guidance, instruction of managers);
4. the extent to which the employer took steps to assess the adverse impact of its employment practice on older workers;
5. the severity of the harm to individuals within the protected age group, in terms of both the degree of injury and the numbers of persons adversely affected, and the extent to which the employer took corrective steps to minimize the severity of the harm, in light of the burden of undertaking such steps; and
6. whether other options were available and the reasons the employer selected the option it did.

The reasonableness standard adopted above is less burdensome than the business necessity test ("[u]nlike the business necessity test, which asks whether there are other ways for the employer to achieve its goals that do not result in a disparate impact on a protected class, the reasonableness inquiry includes no such requirement."). Nevertheless, it remains the employer's burden to establish that the practice was reasonably designed to further a legitimate business purpose, and administered in a way that reasonably achieves that purpose. Smith, 544 U.S. at 243.

Although much remains unclear with respect to mandatory retirement/de-equitization policies, the EEOC's case against Kelley Drye, as well as its proposed definition of employers' affirmative defense, emphasize the reality that such policies continue to present a costly risk to professional partnerships.

- Document the institution of facially neutral policies, including the various options considered. To the extent the firm does research into the policies adopted by other firms in the industry, that research may be helpful in supporting the affirmative defense. Consider keeping and preserving meeting minutes with respect to such decisions if it is not standard practice to do so.
- Articulate a legitimate purpose behind such policies, and make sure that purpose is actually served by the policy. If the stated business goal is the assurance that all firm "partners" contribute equally, consequences for failing to meet productivity standards must be applied to younger individuals as well as older ones. But if the business goal is the transition of clients from older "partners" to younger ones, whether that purpose is served by a restriction tied to productivity is questionable.
- Document the firm's consideration of the impact of facially neutral partnership restrictions on older "partners." It may be a good idea to also proactively examine the policies' effect on female "partners" who take maternity leave.

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CRAFTING PARTNERSHIP POLICIES

Whether facially neutral policies, tied to productivity or ability to bring in new clients, for example, may be seen as having a disparate impact on older "partners" found to actually be employees,