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Weighing Lawyer Employment Agreements In Mass.

Law360, New York (March 19, 2009) -- Depending upon the jurisdiction, lawyers are prohibited either by Rule 5.6 of the Rules of Professional Conduct or by Canon 2, DR 2-108(A) of the Model Code of Professional Responsibility from entering into agreements (other than agreements concerning retirement benefits) that restrict their ability to practice law following the termination of their relationship with their firm.

Because the underlying purpose of these rules is to protect client choice of counsel, courts have interpreted the rules to prohibit lawyers not only from agreeing to be bound by traditional noncompete agreements, but from agreeing to be bound by other agreements that impose financial disincentives on departing attorneys for representing clients that they had previously represented while working at their prior firm.

Given the potential significant financial implications of such a restriction to departing lawyers and their former law firms, the scope of the rule has occasionally been tested over the years.

Most recently, the Massachusetts Supreme Judicial Court issued a decision that has broad implications for the types of post-employment restrictions that law firms will be permitted to impose, and thus to which withdrawing lawyers may find themselves subject in the future.

The case is Pierce v. Morrison Mahoney LLP, 452 Mass. 718 (2008). At issue in that case was a forfeiture provision in a partnership agreement requiring all partners who withdrew from the firm (regardless of whether they competed or not) to forfeit their right to payments for distributions of the firm’s profits. Id. at 722-23.

To best understand the ruling in Pierce, it is helpful to consider the context in which the case arose. Specifically, the forfeiture provision analyzed in Pierce replaced a “forfeiture-for-competition” provision that had itself been the subject of a separate action before the Massachusetts Supreme Judicial Court over a decade earlier.

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The prior case was Pettingell v. Morrison, Mahoney & Miller, 426 Mass. 253 (1997).[1] Although the provision at issue there did not impose an outright ban on competition, it was nevertheless an "agreement that 'impose[d] adverse consequences on a withdrawing partner' who competed with the law firm."[2] Pierce, 452 Mass. at 719 (quoting Pettingell, 426 Mass. at 256).

Most troubling to the Supreme Judicial Court, however, was that "the provision did not impose such adverse consequences on a withdrawing partner who did not compete with the firm." Id.

As a result of this disparate treatment, the court "reasoned that such a provision would 'discourage a lawyer who leaves a firm from competing with it,' which 'would tend to restrict a client or potential client's choice of counsel.'"[3] Id. at 724 (quoting Pettingell, 426 Mass. at 257).

Based on this conclusion, the Pettingell court invalidated the forfeiture-for-competition provision, albeit noting in dicta that "[a] law firm's legitimate interest in its survival and well-being might justify a limitation on payments to a withdrawing partner in particular circumstances ..." Pettingell, 426 Mass. at 258.

The Pettingell decision is similar to cases from the majority of other courts, as well as to a subsequent decision by the Supreme Judicial Court invalidating an agreement that required departing lawyers (for a specified period after leaving the firm) to share profits received from work that they performed for former firm clients.

The common thread in all of these cases is an agreement that was an absolute ban on competition or that imposed different fates on departing lawyers based upon whether they competed.[4]

Pierce is different. It joins a small group of cases involving an agreement that neither prohibited competition nor imposed a financial penalty tied to competition.

Instead, the agreement in Pierce imposed a straight forfeiture of certain rights (to payments) based simply on the fact that the lawyer had withdrawn from the firm.

In distinguishing prior cases invalidating other post-employment restrictions, the Supreme Judicial Court focused on the fact that, under the current agreement, "the fate of a lawyer who voluntarily withdraws and competes with [his or her prior law firm] for its clients is precisely the same as the fate of a lawyer who voluntarily withdraws and does not ..." Pierce, 426 Mass. at 726.

Instructively, the court did not rely on (and therefore seems to have gone further than contemplated by) its dicta in Pettingell contemplating financial disincentives when necessary to protect a law firm's survival or well-being. Pettingell, 426 Mass. at 258. The Pierce decision instead turns solely on the absence of disparate treatment.

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The significance of this absence is, according the Supreme Judicial Court, that the agreement “does nothing to ‘shrink the pool of qualified attorneys from which clients may choose.’” Id. (quoting Eisenstein v. David G. Conlin, P.C., 444 Mass. 258, 262 (2005)).

Thus, the agreement does not limit client choice — the protection of which is the primary purpose of rule 5.6. Id.

While the Supreme Judicial Court recognized that the agreement creates substantial disincentives for lawyers to withdraw from the law firm, it was unpersuaded by those disincentives, as “[t]he purpose of rule 5.6 is not to protect lawyer mobility.” Id.

Given that most states have adopted rule 5.6 (or DR 2-108(A)) and that there is a dearth of cases to fully establish and define the limits of those rules, Pierce has potentially broad reaching implications that extend not just to Massachusetts, but to lawyers and law firms throughout the country.[5]

In this regard, Pierce is one of only a handful of cases to address the issue of a straight forfeiture, and may be the only case to uphold such restrictions while simultaneously rejecting forfeiture-for-competition provisions.

In so doing, Pierce has drawn a bright-line test for other courts to follow based solely on the relative treatment of departing lawyers who compete and those who do not compete.[6]

The Supreme Judicial Court’s decision in Pierce may, however, be short-lived. Specifically, soon after the decision issued, the Massachusetts House of Representatives began considering two bills that would change the noncompete landscape in Massachusetts.

One such bill would eliminate noncompete agreements altogether, albeit having questionable impact on Pierce. The other, however, adopts a more balanced approach to noncompete agreements, and includes specific restrictions on forfeiture agreements.

This latter bill requires all forfeiture agreements to be in writing, disclosed at least two weeks in advance of their effective date, supported by reasonably adequate consideration, and related to the harm caused to the employer, which harm must threaten the continued viability of the employer and result from something other than increased competition.

What the Massachusetts Legislature does with the pending legislation and whether other states follow suit remains to be seen.

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[1] The law firm, Morrison Mahoney LLP had previously been known as “Morrison, Mahoney & Miller.”

[2] The adverse consequences were the forfeiture of certain payments relating to the firm’s profits.

[3] Other courts have rejected similar arguments, reasoning that such a restriction does not prohibit competition, but instead merely reduces the money that the lawyer will make. See, e.g., Fearnow v. Ridenour Swenson Cleere & Evans PC, 213 Ariz. 24, 138 P.3d 723 (2006).

[4] Although some prior decisions from other states have addressed forfeiture provisions, they arose in the context of an appeal from an arbitral award, where there were other strong public policies at issue (i.e., the enforceability of arbitral awards).

[5] The decision also has implications for other professions where the proscriptions on noncompetes are similarly designed to protect someone other than the professional. Thus, for example, under the Pierce rationale, physicians, who — in the name of patient choice — are prohibited from entering into noncompete agreements, arguably will no longer be insulated from forfeiture provisions like that at issue in Pierce.

[6] Curiously, the Supreme Judicial Court did not analyze or even mention the reasonableness of the forfeiture, as prior case law suggests is a prerequisite to the enforcement of a forfeiture agreement. See Kroeger v. The Stop & Shop Companies Inc., 13 Mass. App. Ct., 310, 311-12 (1982).

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