LOS ANGELES COUNTY BAR ASSOCIATION

PROFESSIONAL RESPONSIBILITY AND ETHICS COMMITTEE

FORMAL OPINION NO. 460

(AUGUST 20, 1990)

SUMMARY: **RESTRICTIVE RETIREMENT PAYMENTS: A partnership agreement does not violate the provisions of Rule 1-500, California Rules of Professional Conduct [derived from former Rule 2-109], prohibiting agreements restricting the right of a member to practice law, if it requires the member to forego or defer a bona fide retirement payment solely on the basis of his or her continued practice of law.**

AUTHORITIES CITED: Rule 1-500, California Rules of Professional Conduct, Business & Professions Code Section 16600, Muggill v. Rueben H. Donnelley Corp., 62 Cal.2d 239, 42 Cal.Rptr. 107, 398 P.2d 147 (1965), Cohen v. Lord, Day & Lord, 75 N.Y.2d 95, 551 N.Y.S.2d 157 (1989), Gray v. Martin, 63 Ore. App. 173, 663 P.2d 1285 (1983), Miller v. Foulston, Siefkin, Powers & Eberhard, 246 Kan. 450, 790 P.2d 404 (1990).

The Committee's opinion has been requested concerning the provisions of the following partnership agreements:

Partnership Agreement A permits payment to any attorney employee withdrawing from the firm of the employee's vested percentage of $100,000. In addition to such amounts, if the employee permanently retires from the practice of law, the employee's vested percentage is increased by $400,000. The term "permanent retirement" is not defined and is assumed to be determined at the time of termination and intending the cessation of all legal activities at the time of termination.

Partnership Agreement B permits payments of a fixed retirement compensation upon withdrawal from the firm to attorney employees of at least age 45, on a sliding scale with increased payments based on the employee's age on the date of retirement. However, if the employee is less than 60 years of age, and continues at any time prior to age 60 and after termination to practice law for compensation in any legal activity except with firm B or in a judicial or public capacity, the payments are suspended until the employee reaches age 60.

Subsection (A) of Rule 1-500 of the California Rules of Professional Conduct provides that:

> (A) A member shall not be a party to or participate in offering or making an agreement, whether in connection with the settlement of a lawsuit or otherwise, if the agreement restricts the right of a member to practice law.

The public policy supporting Rule 1-500(A) is to ensure that the client's right to counsel of his or her choice is not interfered with by restrictive covenants not-to-compete entered into between lawyers.[1]

The threshold issue presented is whether Rule 1-500(A) is applicable to the partnership agreements.[2] The Committee is of the opinion that the mere agreement to pay or suspend the payment of retirement compensation contingent upon a member's ceasing to practice law upon withdrawal from the partnership constitutes a prohibited restrictive

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[1]See: Volume 1, Proposed Rules and Legislative History, Proposed Amendments to the Rules of Professional Conduct, Commission for the Revision of the Rules of Professional Conduct, July, 1987, Page 11. The Commentary states: "Any agreement which restricts the right of a member to practice law after leaving a firm not only limits that member's professional autonomy but also the right of a client to choose a lawyer." See also: Cohen v. Lord, Day & Lord, 75 N.Y.2d 95, 551 N.Y.S.2d 157 (1989) where the highest court of the state of New York held with respect to similar version of the rule that "The purpose of the rule is to ensure the public has the choice of counsel;" and Miller v. Foulston, Siefkin, Powers & Eberhard, 246 Kan. 450, 790 P.2d 404 407 (1990) holding that "The purpose behind the [Rule] is to protect the public's right 'to select and repose confidence in lawyers of their choice without restriction by providing full availability of legal counsel.'"

[2]The Committee expresses no opinion on ERISA and its applicability to the issues presented.

agreement within the purview of Rule 1-500(A).[3] The Committee has considered an alternative construction of Rule 1-1500(A) that would limit the Rule's applicability to only those agreements which expressly prohibit the practice of law and interpret the Rule as not barring mere financial disincentives as presented in the partnership agreements at issue here. Such an interpretation has been rejected by other jurisdictions[4] and the Committee does not find it persuasive.

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[3]In Muggill v. Rueben H. Donnelley Corp., 62 Cal.2d 239, 42 Cal.Rptr. 107, 398 P.2d 147 (1965), the California Supreme Court held that a provision in a retirement plan providing that payments shall be suspended or terminated in the event the retired employee entered into a competitive business with the employer, restrains the retired employee from engaging in a lawful business and was, therefore, void under Business & Professions Code Section 16600's prohibition of contracts restraining anyone from engaging in a lawful profession, trade or business. The prohibitions contained in Section 16600 and Rule 1-500 are similar in nature, although the public policy purpose of Rule 1-500 the Committee believes is to foster public access to counsel, while the purpose of Section 16600 is directed at a public policy to promote the rights of the individual not to be restrained in carrying on a livelihood. Contra., Smith V. CMTA-IAM Pension Trust et al., 654 F.2d 650 (9th Cir. applying California law, 1981), upholding suspension of retirement payments as not a restrictive agreement subject to Section 16600's prohibition based upon lines of authority providing that agreements restraining contact with existing customers of an employer for a limited period of time do not restrain an employee from engaging in a profession, trade or business and a statutory exception for the purchase of a business. As Rule 1-500 is more narrowly drawn and proscribes any agreement that restricts the right of a member to practice law, Smith was not considered applicable to Rule 1-500. Based on Muggill, it is clear that making payments contingent upon a member ceasing to practice law is a restrictive agreement within the ambit of Rule 1-500.

[4]Cohen v. Lord, Day & Lord, 75 N.Y.2d 95, 551 N.Y.S.2d 157 (1989) and Gray v. Martin, 63 Ore. App. 173, 663 P.2d 1285

Subsection (B) of Rule 1-500 contains exceptions to the general prohibition set forth in Subsection (A) as follows:

> (B) Nothing in paragraph (A) of this rule shall be construed as prohibiting such a restrictive agreement which:
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> (1) Is a part of an employment, shareholders', or partnership agreement among members provided the restrictive agreement does not survive the termination of the employment, shareholder, or partnership relationship, or
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> (2) Requires payments to a member upon the member's retirement from the practice of law.

(1983). The rationale of the court in Cohen is particularly persuasive in discussing this issue:

> Defendants argument that the Disciplinary Rule does not prohibit financial disincentives is also rejected by the plain portion of the rule exempting agreements among partners dealing with retirement benefits. The general rule of statutory construction that meaning and effect should be given to all language of a statute or rule is apt here. Words are not to be rejected as superfluous where it is practicable to give each a distinct and separate meaning [citations omitted]. Presumably, if financial penalties were not "restraints" within the meaning of the rule, there would be no need to exempt the specific category of financial arrangements dealing with retirement. (Emphasis added.)

The discussion to Subsection (B) of Rule 1-500 indicates that there is a limited exception to the public policy set forth in Subsection (A) as follows:

> Paragraph (B) permits a restrictive covenant in a law corporation, partnership, or employment agreement. The law corporation shareholder, partner, or associate may agree not to have a separate practice during the existence of the relationship; however, upon termination of the relationship (whether voluntary or involuntary), the member is free to practice law without contractual restriction except in the case of retirement from the active practice of law. (Emphasis added.)

The prior Rule 2-109, from which Rule 1-500 was derived, with respect to Subsection (B)(2), provided: "requires payments to a member of the State Bar upon his permanent retirement from the practice of law." (Emphasis added.)

Partnership Agreement A does not violate the provisions of Rule 1-500 as its terms are literally within the exception permitted under Subsection (B)(2), permitting payments to a member upon the members' retirement from the

practice of law. Partnership Agreement A further requires some vested retirement payments to all withdrawing members regardless of whether the member is practicing law, going onto the bench, going into government service, which does not primarily consist of the practice of law or some other employment, albeit on a substantially reduced basis if the member does practice law.

Does Partnership Agreement A indirectly violate Rule 1-500 because the retiring partner receives substantially more compensation than a member who does not retire? Since all retiring partners are treated equally no matter what their chosen occupation would be subsequent to terminating their relationship with the firm, and the exception of Subsection (B)(2) expressly permits payments based on a members retirement from the active practice of law, it is the opinion of this Committee that the provisions do not violate Rule 1-500. It appears that Partnership Agreement A attempts to recompense any withdrawing member with vested retirement benefits, but to pay more to retiring partners whose economic need would understandably be greater. The rule expressly authorizes this practice.

Partnership Agreement B is different than Partnership Agreement A only to the extent of the incentive created for a member to retire. Under Partnership Agreement

B, the member's retirement payments are suspended for an otherwise terminating member who practices law elsewhere after termination until such time as the terminating member ceases to practice law. Under Partnership Agreement A, the determination of whether the member receives the increased benefits of a retiring partner is made at the time the member retires, with such rights being forfeited if the member does not retire at the time of termination.

The Committee is of the opinion that the mere suspension of retirement payments to the member under Partnership Agreement B if he continues to engage in the practice of law after termination is a restrictive agreement proscribed by Rule 1-500(A). The Committee does not see these differences as relevant to whether the partnership agreements fit into the Subsection (B)(2) exception for retirement payments.

The exception under Subsection (B)(2) permissively allows a restriction based on whether a member retires from the active practice of law. It is noted that the new Rule 1-500 dropped the requirement that the member must have "permanently" retired. This change indicates that the determination can be an ongoing one. The provisions of Partnership Agreement B do not work a forfeiture as to payments to the member under the agreement, but rather, preserve the rights of the member to such retirement payments, albeit postponing such right to payment until the

member ceases to practice law. While the present value of such payments are diminished because the member elects to continue the active practice of law, this result is within the exception permitted by Subsection (B)(2).

However, Partnership Agreement B does permit a member to receive payments if the member goes on to the bench, practices law for a public agency, or if the member continues to practice law after the age of 60. By defining retirement to include some form of the practice of law, does Partnership Agreement B fall outside the exception permitted by Subsection (B)(2)?

There is no question that it is permissible to provide for payments if the member goes on the bench, as that would not be engaging in the practice of law. The focus of inquiry then, is whether the retirement payments can be made contingent upon retirement that is something less than the complete cessation of the active practice of law, such as permitting a member to continue to practice after reaching age 60 or entering an office of public service and continuing to practice law. The fact that an agreement defines retirement to be less restrictive than the complete cessation of the practice of law should not be a reason for its violation of Rule 1-500, provided that such less restrictive bona fide definitions of retirement and the agreement as a

whole, viewed on a case by case basis, do not violate the public policy of the Rule by proscribing the practice of law or representation of clients. In each of the less restrictive circumstances under Partnership Agreement B's definition of retirement the right of the member to practice law is not being restricted and clients would not be precluded from seeking the member's services (in the case of public service if they otherwise qualify under the public agency rules). Therefore, the definition of retirement under Partnership Agreement B is within the 1-500(B)(2) exception.

In conclusion, it is the opinion of this Committee that a partnership agreement which makes retirement payments contingent upon whether the member continues to practice law does not violate Rule 1-500(A)'s prohibition against restrictions upon the right to practice law.

This opinion is advisory only. The Committee acts only on specific questions submitted ex parte, and the opinions are based only on the facts set forth and the questions presented.