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Restrictions on an Attorney's Right to Practice

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by Grace M. Giesel

In Kentucky and in other states, relationship agreements such as partnership agreements and employment agreements legally may contain restrictions on competition if the parties to the agreements are not lawyers.[1] Covenants not to compete are recognized as a valid tool that can be used for the protection of otherwise vulnerable interests as long as the competition restriction is reasonable.[2]

The story is very different for restrictions involving lawyers. In Kentucky, as is true in other states, a lawyer cannot enter into an employment or other agreement if that agreement restricts the right of a lawyer to practice law. Rule 5.6(a) of the Kentucky Rules of Professional Conduct (Kentucky Supreme Court Rule 3.130 (5.6(a))) states:

A lawyer shall not participate in offering or making:

(a) a partnership or employment agreement that restricts the right of a lawyer to practice after termination of the relationship, except an agreement concerning benefits upon retirement.[3]

Thus, a typical covenant not to compete, if entered into by an attorney, whether the attorney is an in-house attorney or an attorney in a law firm, is unethical.[4] An attorney entering into such an arrangement is subject to discipline.

In addition, courts generally refuse to enforce such contracts because they are contrary to public policy. As the New Jersey Supreme Court stated in *Jacob v. Norris, McLaughlin & Marcus*,[5] the rules of professional conduct for attorneys "establish the state's public policies with respect to attorney conduct."[6]

Why is the rule for attorneys different? The first indication that a restriction on an attorney's right to practice was improper came in American Bar Association (ABA) Formal Opinion 300 in 1961.[7] In that Opinion, the ABA Committee on Professional Ethics seemed to base its disapproval of restrictive agreements on a desire to further professionalism of attorneys and to promote autonomy of attorneys. The Opinion stated that restrictive agreements were "an unwarranted restriction on the right of a lawyer to choose where he will practice and inconsistent with our professional status."[8]

In the 1980s, as states adopted the ABA Model Rules, another rationale became important: the protection of client autonomy in choosing a lawyer. The comments to the current Model Rule 5.6 and the comments to the Kentucky version of Rule 5.6 both note that restrictions on a lawyer's right to practice "limits the freedom of clients to choose a lawyer."[9] The *Restatement (Third) of the Law Governing Lawyers* expresses a substantially similar rationale. It states: "The rationale for the rule is to prevent undue restrictions on the ability of present and future clients of the lawyer to make a free choice of counsel."[10]

Direct Restrictions

Clearly, any direct limitation on an attorney's right to practice, such as a traditional covenant not to compete forbidding the practice of law in competition with the other signatory to the agreement, would violate Rule 5.6(a). For example, in *Dowd & Dowd, Ltd. v. Gleason*[11], the Illinois Supreme Court refused to enforce an agreement which provided that departing lawyers would not solicit firm clients without firm approval.

Indirect Restrictions (Financial Disincentives)

In recent years, courts have evaluated whether more indirect restrictions might also violate Rule 5.6(a). Usually these provisions impose financial penalties for competing. Courts generally agree that such provisions also violate Rule 5.6(a).[12] A typical case is *Eisenstein v. Conlin*.[13] The Supreme Judicial Court of Massachusetts refused to enforce a partnership agreement because it violated Rule 5.6(a). The partnership agreement required departing lawyers to pay a portion of fees earned after departure if the fees related to current or former clients of the departed firm. The court noted that enforcement of the provisions would discourage departing lawyers from competing with the firm and thus would restrict a potential client's choice of counsel.

A recent but unusual case is *Fearnow v. Ridenour, Swenson, Cleere & Evans, P.C.*[14] The Arizona Supreme Court evaluated a partnership agreement which required a departing lawyer to tender his stock in the corporation without compensation if he competed with the firm. Departing lawyers not competing with the firm would receive compensation in exchange for tender of the stock. The Court was of the opinion that Rule 5.6(a) did not prohibit financial disincentives to competition. The Court determined that "[s]uch agreements, as in the case with restrictive covenants between other professionals, should be examined under the reasonableness standard."[15]

The Retirement Arrangement Exception

With this background of general prohibition, Rule 5.6(a) also contains an exception. If the agreement restraining the attorney's right to practice is really an "agreement concerning benefits upon retirement," Rule 5.6(a) does not disapprove of it. The rationale of the exception for retirement restrictions is that a retiring attorney would not be available to clients anyway. Thus, restricting a retiring attorney's right to practice has little effect on lawyer availability and would not infringe upon the client's right to choose an attorney. Unfortunately, the Rule does not define an "agreement concerning benefits upon retirement." In *Borteck v. Riker, Danzig, Schere, Hyland & Perretti LLP*,[16] the Supreme Court of New Jersey evaluated an agreement that provided that a departing capital partner was entitled to a share of the firm's "net worth." The agreement provided that the amount was to be paid in the first twelve months after departure. The agreement also provided that a departing capital partner was entitled to "retirement" benefits under certain conditions, including the condition that the partner maintain retired status during the period the retirement benefits were paid to the departed partner. The Court concluded that the agreement had "sufficient indicia of a bona fide retirement arrangement"[17] and so was enforceable because it fit within the exception in Rule 5.6(a) for retirement plans. The Court focused on three factors in determining whether the agreement was a retirement arrangement within the exception of Rule 5.6(a): the presence of minimum age and service requirements, separate provisions for withdrawal for retirement and withdrawal for other purposes, and the length of time the benefits are to be paid. The Court noted that the agreement at issue had minimum age requirements, the benefits paid were related to years of service, the agreement had benefit calculation formulas and a specified term for payouts, and the agreement provided that the benefits were to continue to the partner's estate if the partner died before the term of the payout had elapsed. The Court also noted that the agreement dealt with retirement payments separately from other types of payments.

Likewise, in *Donnelly v. Brown, Winick, Graves, Gross, Baskerville, Schoenebaum & Walker*,[18] the Iowa Supreme Court enforced

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an agreement that had an age-service year requirement for payment. The Court held that the agreement was a retirement provision and thus permitted by Rule 5.6(a). The agreement was enforceable because it did not contradict public policy. The agreement required the attorney to not engage in the private practice of law.

Professor Robert Hillman of the University of California-Davis School of Law has identified four factors as indicators of a permissible retirement restriction under Rule 5.6(a). Professor Hillman identifies the presence of minimum age and service conditions as the most important factor in finding that a restrictive provision is one dealing with retirement and thus permissible and enforceable. Second, Professor Hillman notes that retirement provisions should be separate from provisions dealing with a lawyer's departure for other reasons. Third, Professor Hillman notes that payments over an extended period of time supports a conclusion that the arrangement is a retirement one though payments over a short period of time does not mean that the arrangement does not address the retirement situation. Professor Hillman deems this factor relevant but not dispositive. Finally, Professor Hillman notes that if the firm or employing entity makes ancillary benefits available to the departed lawyer, the arrangement looks more like a retirement arrangement, and a court might be more likely to enforce it. The ancillary benefits provided might be life insurance, health insurance, staff support, and a place to work upon occasion. Note that these are benefits that firms have traditionally provided to retiring lawyers.[19]

Conclusion

Kentucky courts have not yet spoken to the issues raised by Rule 5.6(a). The Rule itself makes clear that any direct restriction on the right of an attorney to practice law is unethical and thus will be unenforceable in any court. Most courts of other jurisdictions have reached the same result with regard to indirect restrictions such as financial disincentives to competition. The only permissible restriction on an attorney's right to practice is one that is part of a retirement agreement. While courts and commentators have provided some guidance on defining a retirement agreement, no standard definition exists. Attorneys must recognize, therefore, the uncertain nature of the ethics and enforceability of any restrictive agreement.

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Endnotes

1. *See Hall v. Willard & Woolsey, P.S.C.*, 471 S.W.2d 316 (Ky. 1971).

2. *See Porter v. Hospital Corp. of America*, 696 S.W.2d 793 (Ky. App. 1985). *See generally* Grace M. Giesel, 15 Corbin on Contracts Chapter 80 (Perillo, ed. 2003).

3. Kentucky Supreme Court Rule 3.130 (5.6(a)). The *Restatement (Third) of the Law Governing Lawyers* states the same rule. *See* Restatement (Third) of the Law Governing Lawyers § 13(1) (2000).

4. *See* ABA Formal Op. 94-381 (1994) (Rule 5.6(a) applied to in-house attorneys).

5. 607 A.2d 142 (N.J. 1992).

6. *Id.* at 146.

7. For a great discussion of the history of the prohibition, *see* Linda Sorenson Ewald, *Agreements Restricting the Practice of Law: A New Look at an Old Paradox*, 26 J. Legal Prof. 1 (2001-02)

8. ABA Formal Op. 300 (1961).

9. ABA Model Rules of Professional Conduct, Rule 5.6, cmt. 1 (2006); Kentucky Supreme Court Rule 3.130 (5.6) cmt. 1.

10. Restatement (Third) of the Law Governing Lawyers § 13(1) cmt. b (2000).

11. 693 N.E.2d 358 (Ill. 1998).

12. *See, e.g., Anderson v. Aspelmeier, Fisch, Power, Warner & Engberg*, 461 N.W.2d 598 (Iowa 1990) (competition causes forfeiture of departing partner's interest).

13. 827 N.E.2d 686 (Mass. 2005).

14. 138 P.3d 723 (Ariz. 2006).

15. *Id.* at 729.

16. 844 A.2d 521 (N.J. 2004).

17. *Id.* at 526.

18. 599 N.W.2d 677 (Iowa 1999).

19. *See* Robert W. Hillman, *Ties that Bind and Restraints on Lawyer Competition: Restrictive Covenants as Conditions to the Payments of Retirement Benefits*, 39 Ind. L. Rev. 1 (2005). ■