

Who counts?: The United States Supreme Court cites "control" as the key to distinguishing employers from employees under federal employment antidiscrimination laws

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Columbia Business Law Review



ARTICLE

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EMPLOYMENT ANTIDISCRIMINATION LAWS
STEPHANIE GREENE & CHRISTINE NEYLON O'BRIEN

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WHO COUNTS?: THE UNITED STATES SUPREME COURT CITES “CONTROL” AS THE KEY TO DISTINGUISHING EMPLOYERS FROM EMPLOYEES UNDER FEDERAL EMPLOYMENT ANTIDISCRIMINATION LAWS

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I. INTRODUCTION

When an individual makes a decision to sue her employer under federal laws prohibiting discrimination in the workplace, she might not expect some of the hurdles that can prevent her case from going forward. First, the individual must be an “employee” as that term is defined by the relevant antidiscrimination laws and the case law

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interpreting the term "employee." Second, the business entity that employs the claimant must be an employer covered by the statute in question. Determining whether an individual is an employee entitled to the protection of federal antidiscrimination laws or whether the employer is subject to such laws is not always easy to ascertain. The language of the statutes provides no instruction and courts have taken different approaches to defining the terms "employee" and "employer." In deciding *Clackamas Gastroenterology Associates, P.C. v. Wells*, the Supreme Court has answered several questions that have troubled lower courts about "who counts" as an employee or an employer in suits brought under federal antidiscrimination laws.¹

Individuals alleging discrimination under Title VII of the Civil Rights Act of 1964 ("Title VII"), the Americans with Disabilities Act ("ADA"), and the Age Discrimination in Employment Act ("ADEA"), may bring suit only if they are employees and the entity they work for is a covered employer. These statutes use the same language, defining the term "employee" as "an individual employed by an employer" and the term "employer" as "a person engaged in an industry affecting commerce" having fifteen, twenty, or more employees, depending on the statute, "for each working day in each of 20 or more calendar weeks in the current or preceding calendar year."² The statutes indicate that only employees are protected, but the statutes offer no guidance on how to determine when an individual is an employee entitled to protection or which individuals should be counted as employees for purposes of the statutory minimum.

¹ 123 S. Ct. 1673 (2003).

² 42 U.S.C. § 12111(4) (2000); 29 U.S.C. § 630(f) (2000); 42 U.S.C. § 2000e(f) (2000). The number of employees required to establish jurisdiction under federal statutes differs depending on the statute. For example, under Title VII and the ADA, an employer is a "covered entity" only if it has at least fifteen employees. See the definition of "employer." Title VII, 42 U.S.C. § 2000e(b) (2000). Twenty employees comprise the jurisdictional threshold for an employer under the ADEA. 29 U.S.C. § 630(b) (2000). State antidiscrimination legislation, while not the subject of this paper, often requires far fewer employees to establish jurisdiction.

Threshold issues involving the definition of employee under federal antidiscrimination laws usually occur in two situations. First, a business entity may use the statutory minimum as a defense, maintaining that it is not a covered entity because it does not have the requisite number of employees. In these “counting” cases, the dispute revolves around whether various individuals “count” towards the threshold number of employees required for covered employer status. Second, the definition of employee is crucial when the claimant serves a role that could arguably be characterized as either an employer or an employee. In such cases, a partner in a partnership or a shareholder in a professional corporation may argue that she is entitled to sue because she is an employee within the meaning of the statute. The business entity may counter that the individual is not an employee, but an employer who is not entitled to sue under the antidiscrimination laws. Similar questions may arise regarding major shareholders in general corporations. Although courts have yet to address the covered employee status of individuals in other forms of business organizations, such as limited liability partnerships (LLPs) and limited liability companies (LLCs), such cases would involve the same issues.³ With no help from the circular definitions provided by the statutes, the courts have struggled to find consistent definitions for the term “employee.” This task has become particularly difficult as forms of business organization continue to evolve and businesses choose their organizational form for a variety of reasons.

Should shareholders in a professional corporation or partners in a general partnership count as employees for establishing jurisdiction over an employer under the federal discrimination statutes? Should these same parties be protected as employees entitled to bring discrimination

³ See generally Daniel S. Kleinberger, “Magnificent Circularity” and the Churkendoose: LLC Members and Federal Employment Law, 22 OKLA. CITY U. L. REV. 477 (1997). The term “churkendoose” refers to a hybrid animal in children’s literature which the author compares to the hybrid entity of a limited liability company. *Id.* at 482 n.14.

claims under these statutes? In *Clackamas Gastroenterology Associates, P.C. v. Wells*, the United States Supreme Court considered whether physicians in a professional corporation who performed services for the corporation and who also owned and managed the business were employees to be counted towards the fifteen-employee threshold required by the ADA.⁴ In determining that the individuals in question were more like employers than employees, the Court held that the common law of agency is the appropriate source to fill gaps in the statutory definition of the term "employee."⁵ In its decision, the Court endorsed factors listed by the Equal Employment Opportunity Commission ("EEOC") in its Compliance Manual which distinguishes employees from employers based on "whether the individual is subject to the organization's control."⁶ The EEOC's Compliance Manual applies the same "factors to be considered with regard to coverage of partners, officers, members of boards of directors, and major shareholders."⁷ Thus, in recognizing the EEOC factors, the Court endorsed a method of evaluating an individual's employment status as employee or employer not only in the professional corporation, as was the case in *Clackamas*, but also in various other forms of business organization. Moreover, the Court's decision indicates that the EEOC factors will also be used to determine whether partners, shareholders, or other individuals of uncertain status, may bring claims under the antidiscrimination laws.⁸

The importance of the outcome in the *Clackamas* case for employment discrimination purposes is clear. Businesses, such as *Clackamas Gastroenterology*, that sit on the borderline of the size threshold for statutory coverage, are

⁴ 123 S. Ct. 1673 (2003).

⁵ *Id.* at 1679. The Court remanded the case to the Court of Appeals for the Ninth Circuit for further proceedings consistent with its opinion. *Id.* at 1681.

⁶ See EQUAL EMPLOYMENT OPPORTUNITY COMM'N, COMPLIANCE MANUAL § 2-111(A)(1)(d) (2000), available at <http://www.eeoc.gov/docs/threshold.html> [hereinafter EEOC COMPLIANCE MANUAL].

⁷ *Id.*

⁸ See *infra* notes 56-63 and accompanying text.

impacted by the Court's interpretation of who qualifies as a covered employee under the federal statutes. Figures from the Small Business Administration in 1999 indicate that more than 332,540 firms in the United States have between fifteen and twenty-four employees.⁹ Because the Court's decision pertains to all federal employment antidiscrimination laws, a business that expects to be shielded from compliance with these laws must be aware of the number of individuals in its firm that count as employees.¹⁰ The decision is also important for individuals such as partners, officers, members of boards of directors, and major shareholders who wish to bring discrimination claims.

This article analyzes the issues posed and the conclusions reached by the Supreme Court in the *Clackamas* case and the extent to which the Court's decision has resolved several questions regarding employer and employee status. Part II explains the different approaches taken by the circuit courts of appeal in determining who qualifies as an employee under the federal statutes that led to the United States Supreme Court's review of the circuit split. Part III sets forth the facts, history, and holding of the *Clackamas* case in detail. In Part IV, this article analyzes the extent to which the Court answered three questions that have troubled the lower

⁹ See Brent Hunsberger, *Clinic Victory in Suit Opens Door to Claims*, THE OREGONIAN, Apr. 23, 2003, at A01.

¹⁰ 29 U.S.C. § 630(f) (2000). A ruling on who is a "covered employee" under the ADA will also apply to the status of "covered employee" under the other federal antidiscrimination statutes. Some of the other statutes have higher thresholds, such as a twenty employee minimum under the ADEA, and fifty employees under the Family and Medical Leave Act. See Susan J. McGolrick, *Disabilities, Supreme Court to Consider Whether Shareholders Count as Employees Under ADA*, Daily Lab. Rep. (BNA) No. 191, at AA-1 (Oct. 2, 2002); *Supreme Court Ruling in Wells Case Will Have Broad Impact, Lawyer Says*, 24 DISABILITY COMPLIANCE BULL. No. 7, Oct. 18, 2002 (quoting Steven Seymour's brief for the petitioner, Clackamas, in which he noted that there were nearly 430,000 employers with between fifteen and nineteen employees in 1999, and that these employers employed more than three million workers with an annual payroll of more than ninety-three billion dollars).

courts. The first issue is whether the employer's form of organization or the claimant's title should impact how a court determines whether the federal antidiscrimination statutes apply. In exploring the decision's impact on this issue, this article examines several recent cases to illustrate how the Court's decision and reasoning will guide the lower courts.¹¹ The second issue concerns whether partners may be employees and the related issue of whether individuals may be both employers and employees for different purposes. The Court clearly rejected the conclusion that partners are always employers and the approach followed by lower courts of comparing an individual's role to that of a partner to determine his status. The third issue is whether courts should define the term "employee" in the same manner whether the case involves the status of a claimant or the status of individuals for counting purposes.

This article concludes that the Court's decision will go far to remedy the confusion over who qualifies as a covered employee under federal employment antidiscrimination laws because it applies uniformly to all forms of business organization. Although the EEOC factors endorsed by the Court leave room for speculation and some uncertainty as to how individuals will be categorized, the Court's decision, with its emphasis on control, should allow firms to better predict whether they are subject to the federal antidiscrimination laws and individuals to better assess whether they are entitled to the statutes' protections. The authors believe that amending the statutes to clarify whom the statutes intend to protect and how the size of a firm

¹¹ See *infra* Part IV (discussing *EEOC v. Sidley Austin, Brown, & Wood*, 315 F.3d 696 (7th Cir. 2002) (involving EEOC subpoena duces tecum to investigate possible age discrimination against partners)), *Schmidt v. Ottawa Med. Ctr., P.C.*, 322 F.3d 461 (7th Cir. 2003) (a professional corporation case where a physician shareholder claimant was held not to be an employee for purposes of ADEA coverage based on economic realities test); *Trainor v. Apollo Metal Specialties, Inc.*, 318 F.3d 976 (10th Cir. 2002) (a counting case wherein the court refused a motion for summary judgment where status of major stockholder as covered employee could establish jurisdiction for ADA purposes)).

should be determined for exemption purposes would be a better solution to the difficult issue of defining employers and employees under the statutes. Nevertheless, the Court's decision resolves inconsistencies in the lower courts' approaches to the issues and, with the assistance of the EEOC's guidelines, should provide more uniformity in outcome as well.

II. THE CIRCUIT SPLIT

The Supreme Court granted certiorari in the *Clackamas* case to resolve a split in the federal circuit courts of appeal regarding how to distinguish employers from employees for purposes of federal employment antidiscrimination laws. The circuit courts of appeal have taken two distinct approaches to determining whether shareholders in a professional corporation are employers or employees. The method referred to as the economic realities approach involves a case-by-case, fact-specific analysis of the relationship of the shareholders in question to the business entity.¹² The corporate form approach, however, determines the status of shareholders in a professional corporation as employees solely by virtue of the selected form of doing business. Nevertheless, circuits that follow the corporate form approach apply the same economic realities approach as other circuits in cases involving partnerships.

The circuits that follow the economic realities approach ignore the titles of the individuals in question and focus instead on the function that each individual performs in the business entity. In cases involving partners, the circuit courts of appeal agree that a partner is an employer, and not an employee, if he enjoys the traditional indicia of partnership—ownership, management, and profit sharing.

¹² For a detailed account of the development of the economic realities test in cases involving both partners and shareholders in a professional corporation, and the development of the corporate form approach, see Stephanie Greene & Christine Neylon O'Brien, *Partners and Shareholders as Covered Employees Under Federal Antidiscrimination Acts*, 40 AM. BUS. L.J. 781 (2003).

Analogizing to the cases involving partners, the Seventh, Eighth, and Eleventh Circuits have adopted the economic realities approach in deciding cases involving shareholders in a professional corporation. In *EEOC v. Dowd & Dowd Ltd.*, the Court of Appeals for the Seventh Circuit concluded that the three attorney shareholders in a law firm organized as a professional corporation could not be counted as employees to satisfy the jurisdictional minimum under Title VII.¹³ The term "economic realities test" evolved from language in the *Dowd* decision, as the court concluded that "the economic reality of the professional corporation in Illinois is that the management, control and ownership of the corporation is much like the management, control and ownership of a partnership."¹⁴

The Court of Appeals for the Eighth Circuit also used an economic realities approach to determine whether shareholders in a professional corporation should be included to determine the number of employees in a case in which an employee claimed discrimination under Title VII. In *Devine v. Stone, Leyton & Gershman, P.A.*, the court concluded that because they exercised management and control in the business, the shareholders were not employees.¹⁵ Evidence that the shareholder directors made all management decisions, received compensation based on the firm's profit in addition to bi-monthly salaries, made contributions to firm capital, and were responsible for firm debts, indicated that they were employers, not employees.¹⁶

The cases decided by the Seventh and Eighth Circuits both involved counting employees for purposes of meeting a statutorily required threshold. Nevertheless, the Court of Appeals for the Eleventh Circuit used the same economic realities approach to determine whether a shareholder in a professional corporation could himself bring a claim for discrimination, as an employee. In *Fountain v. Metcalf*,

¹³ 735 F.2d 1177, 1178-79 (7th Cir. 1984).

¹⁴ *Id.* at 1178-79.

¹⁵ 100 F.3d 78 (8th Cir. 1996).

¹⁶ *Id.* at 82.

Zima, & Co., P.C., the Court of Appeals for the Eleventh Circuit held that a shareholder of a professional corporation was not entitled to protection as an employee under the ADEA.¹⁷ In *Fountain*, the court followed the economic realities approach and focused on “the actual role played by the claimant in the operations of the involved entity and the extent to which that role dealt with traditional concepts of management, control and ownership.”¹⁸ The court held that the claimant was not an employee because he “shared in the firm’s profits, losses, and expenses; was compensated on the basis of a share in the firm’s profits; was liable for certain debts, obligations, and liabilities of the firm; and had a right to vote his thirty-one percent ownership”¹⁹

The Court of Appeals for the First Circuit also adopted the economic realities approach. Although the case, *Serapion v. Martinez*, involved the issue of whether a partner in a partnership was entitled to sue for discrimination as an employee under Title VII, the court adopted the same approach as the courts mentioned above in cases involving shareholders in professional corporations.²⁰ In *Serapion*, the court rejected a labeling approach, stating that “form should not be permitted to triumph over substance when important civil rights are at stake.”²¹ In developing a set of nonexclusive factors to distinguish employers from employees, the *Serapion* court looked to cases from other circuits involving both partnerships and professional corporations and to the factors on which those courts relied to determine an individual’s status and right to bring a federal discrimination claim.²² The court stated that

¹⁷ 925 F.2d 1398 (11th Cir. 1991).

¹⁸ *Id.* at 1400-01.

¹⁹ *Id.* at 1401.

²⁰ 119 F.3d 982 (1st Cir. 1997).

²¹ *Id.* at 988.

²² See *Simpson v. Ernst & Young*, 100 F.3d 436 (6th Cir. 1996) (plaintiff found to be an employee rather than a partner in an accounting firm, entitled to sue under ADEA due to lack of management participation, lack of voting power and lack of profit sharing); *Wheeler v. Hurdman*, 825 F.2d 257 (10th Cir. 1987) (plaintiff was a partner, not an

status determinations are made along a continuum, based on factors grouped under three broad categories—ownership, remuneration and management.²³ Looking at the “totality of the circumstances,” the court reasoned, these factors enable a court to make a status determination of whether an individual is an employer or an employee.²⁴

The cases decided by the Seventh, Eighth, and Eleventh Circuits, as well as the partnership case decided by the First Circuit, all focus on the role that the individual plays in the business to determine whether he is an employer or an employee. In these decisions, the courts have relied on the similarities between the functions of partners and shareholders. The Second and Ninth Circuits, however, have rejected this economic realities or functional approach, focusing instead on the form of the business entity. In *Hyland v. New Haven Radiology Associates, P.C.*, the plaintiff, alleging age discrimination under the ADEA, was one of a total of five shareholders who also served as officers and directors in a professional corporation.²⁵ The five members had equal shares in capital contribution, equal

employee, therefore not entitled to sue under Title VII or ADEA due to participation in profits and losses, exposure to liability, contribution to capital and voting rights); *Devine v. Stone, Leyton & Gershman, P.C.*, 100 F.3d 78 (8th Cir. 1996) (attorneys who were shareholder directors in a professional corporation were not employees under Title VII based on participation in setting firm policy, contributions to capital, liability for debts, and profit sharing); *Fountain v. Metcalf, Zima, & Co.*, 925 F.2d 1398 (11th Cir. 1991) (shareholder in accounting firm was not an employee entitled to bring ADEA claim due to compensation based on profits, liability for losses and debts, and voting rights).

²³ *Serapion*, 119 F.3d at 990 (providing relevant factors to consider under each of the three broad categories as follows: (1) ownership—“investment in the firm, ownership of firm assets, and liability for firm debts and obligations”; (2) remuneration—“whether (and if so to what extent) the individual’s compensation is based on the firm’s profits”; (3) management—“the right to engage in policymaking; participation in, and voting power with regard to, firm governance; the ability to assign work and to direct the activities of employees within the firm; and the ability to act for the firm and its principals”).

²⁴ *Id.*

²⁵ 794 F.2d 793, 794 (2d Cir. 1986).

voice in management, and equal share of the firm's profits and losses.²⁶ The court, however, focused not on the shareholder's role as owner and manager, but on the "contractual employment relationship voluntarily entered into by Hyland and the corporation."²⁷ Drawing a sharp distinction between partners and shareholders, the Court of Appeals for the Second Circuit emphasized the voluntary choice to do business as a professional corporation. This choice, the court concluded, precludes inquiry into how the individual functions within the entity, so that "every corporate employee is 'covered' for purposes of the ADEA and any inquiry regarding partnership status would be irrelevant."²⁸

²⁶ *Id.*

²⁷ *Id.* at 797.

²⁸ *Id.* at 798. In the later case of *Drescher v. Shatkin*, however, the Court of Appeals for the Second Circuit never referred to the *Hyland* case even though both cases involved the issue of who was an employee in a professional corporation. *Drescher v. Shatkin*, 280 F.3d 201 (2d Cir. 2002). Unlike *Hyland* where the plaintiff was a shareholder, *Drescher* was a counting case where a former employee's complaint alleging sexual harassment under Title VII was dismissed because of an inability to establish that the defendant, Shatkin, was an employer with fifteen or more employees. Plaintiff *Drescher* was hired as secretary to the sole director and shareholder at the medical and dental professional corporation. The purported harasser was one of the director's two sons both of whom worked at the professional corporation as a dentist or doctor. Plaintiff complained to the father about the son's conduct but was "rebuffed" and then fired. *Id.* at 202. Because the plaintiff in *Drescher* needed to show that the shareholder director counted as an employee in order for the court to have jurisdiction, the court applied the three part test from *EEOC v. Johnson & Higgins, Inc.*, 91 F.3d 1529, 1539 (2d Cir. 1996) for determining whether a director of a corporation is also an employee. *Drescher*, 280 F.3d at 203. The *Drescher* court noted that the question in *Johnson & Higgins* "was somewhat different" than in the instant case. See text discussion of *Johnson & Higgins* and three part test accompanying notes 82-98 *infra*. In *Drescher*, the Second Circuit noted that the director had reported to no one higher and had power to make and change rules and policies, as well as fire or control persons who might violate his rights. Consequently, Shatkin Sr. himself would not be eligible to sue under Title VII, despite the fact that he may be an employee "in the agency sense." *Drescher* 280 F.3d at 204. The court found that Shatkin

The Court of Appeals for the Ninth Circuit followed the lead of the Second Circuit in adopting a corporate form approach to determining who is an employee in a professional corporation. The history and outcome of *Clackamas* are detailed in the next section.

III. CLACKAMAS V. WELLS

A. The Facts

Bookkeeper Deborah Anne Wells was a full time employee of Clackamas Gastroenterology, an Oregon medical professional corporation, from 1986 to 1997.²⁹ Ms. Wells suffered from an autoimmune mixed connective tissue disorder, a condition that causes fatigue, resulting in substantial life impairment.³⁰ Wells maintained that she was able to perform the essential functions of her job, provided she had assistance in managing the books and payroll, accommodations that she alleged were reasonable and would have allowed her to do her job.³¹ Wells was demoted to receptionist and ultimately terminated while on a doctor-approved medical leave.³² She filed suit claiming that the practice had failed to make reasonable accommodations for her by not hiring an assistant, and not allowing her to leave work early.³³ The defendant employer insisted it was not a "covered entity" since the physician shareholders were like

Sr. was not an "employee" for purposes of Title VII and refused to rule that the definition of "employee" should change depending upon the context; that is, whether the status referred to a shareholder claimant or a shareholder who must count as an employee towards the jurisdictional minimum. *Id.* at 205-206. See discussion *infra* Part IV (C).

²⁹ See Joint Appendix at 9, *Clackamas Gastroenterology Assocs. v. Wells*, 123 S. Ct. 1673 (2003) (No. 01-1435), 2001 U.S. Briefs 1435 (Dec. 2, 2002) [hereinafter Joint Appendix].

³⁰ *Id.* at 9-10.

³¹ *Id.*

³² See *id.*; see also Brent Hunsberger, *Lawsuit May Effect Disability Act's Scope*, THE OREGONIAN, Oct. 19, 2002, at A01.

³³ Joint Appendix at 9-10.

partners and could not be counted as employees towards the fifteen employee requirement of the ADA. The medical practice contended that Wells, upset about being reassigned, voluntarily opted not to return from her medical leave.³⁴ Wells was entitled to bring a claim of discrimination under the ADA only if she could establish that there were at least fifteen employees in the business at the time the alleged discrimination occurred. Given the size of the medical practice, the status of the four physician shareholders was critical to her case.

B. The Judicial History

At the district court level, the medical practice Clackamas Gastroenterology relied on the economic realities test, successfully arguing that its four physician shareholders should be regarded as partners/employers and not as employees within the meaning of the ADA.³⁵ In choosing to apply an economic realities approach, the district court noted that labels will not answer questions about who is an employee, especially as new forms of business entities replace traditional forms.³⁶ The district court found that the physician shareholders were “employers who own and manage their own business.”³⁷ This conclusion was based on factors such as control of the management and operation of the medical practice, profit sharing in the form of annual bonuses, and personal liability for malpractice claims.³⁸ Eliminating the four physician shareholders from the tally of employees put the clinic beneath the fifteen employee threshold for covered entity status and prevented Ms. Wells from pursuing her discrimination claim.³⁹

³⁴ *Id.*

³⁵ *See* Wells v. Clackamas Gastroenterology Assocs., No. CV 99-406-AS, 2000 U.S. Dist. LEXIS 8590 (D. Or. Mar. 22, 2000) (citing 42 U.S.C. § 12111(4)-(5) (2000)).

³⁶ *Id.*

³⁷ *Id.* at *10.

³⁸ *Id.*

³⁹ *Id.*

On appeal, in a two-to-one decision, the Court of Appeals for the Ninth Circuit reversed, holding that the defendant professional corporation was a covered entity for purposes of the ADA because the physician shareholders were employees of the professional corporation. Consequently, the entity had more than the fifteen employees required to be subject to the ADA.⁴⁰ Using the corporate form approach, the court held that the physician shareholders were automatically employees.⁴¹ The court emphasized that the decision to incorporate is a voluntary one and that a professional corporation should not be able to have the “best of both possible worlds” by asserting its corporate status for tax and liability advantages while avoiding liability for employment discrimination.⁴² Active participation in management and operation of the medical practice as well as employment agreements further supported the employee status of the physician shareholders, according to the court.⁴³

Judge Graber dissented, agreeing with the district court that an economic realities test is preferable to an approach that relies on labels.⁴⁴ According to Judge Graber, an economic realities test would reveal that the physicians performed functions similar to those of partners, who are not counted as covered employees.⁴⁵ The dissent maintained that a professional corporation such as the defendant employer, as formed under Oregon law, has many attributes of a partnership.⁴⁶ While the physicians work for the business, they also sit on the board of directors that owns the professional corporation and share in the firm’s profits.⁴⁷

⁴⁰ *Wells v. Clackamas Gastroenterology Assocs.*, 271 F.3d 903 (9th Cir. 2001). The dissent by Judge Graber favored using an economic realities test which would have led to a conclusion that the physician shareholders were not “employees” within the meaning of the ADA. *Id.* at 906.

⁴¹ *Id.* at 905.

⁴² *Id.*

⁴³ *Id.* at 906.

⁴⁴ *Id.*

⁴⁵ *Id.* at 906-08.

⁴⁶ *Id.* at 907.

⁴⁷ *Id.* at 908.

Judge Graber reasoned that characteristics of ownership and profit sharing are both aspects typically associated with the partnership form, suggesting that the shareholder directors in the medical practice should not be counted as employees.⁴⁸

C. The United States Supreme Court

The Supreme Court, in a seven-to-two decision, rejected the corporate form approach that the Court of Appeals for the Ninth Circuit used to reach its conclusion that the physician shareholders were employees.⁴⁹ Although the Supreme Court did not refer to an economic realities test, the approach it chose bears some resemblance to the approach followed by the majority of the circuit courts of appeal, in that it requires courts to ignore titles or labels associated with either an entity or an individual and to focus instead on whether the individual whose status is disputed is in a position to manage or control the entity.⁵⁰

The Supreme Court began its analysis by considering cases in which it had construed the term “employee” where the statutes involved provided no meaningful definition of the term.⁵¹ The Court referred to its decisions in *Community for Creative Non-Violence v. Reid*⁵² and *Nationwide Mutual Insurance Co. v. Darden*,⁵³ cases in which the definition of “employee” was critical. In those cases, the Court stated that “when Congress has used the term ‘employee’ without defining it, we have concluded that Congress intended to describe the conventional master-servant relationship as

⁴⁸ See John Gibeaut, *Lawbeat, Supreme Court Report, Getting Down to Business: Limits of Professional Corporations Under Supreme Court Scrutiny*, A.B.A. J., Dec. 2002, at 32.

⁴⁹ *Clackamas Gastroenterology Assocs. v. Wells*, 123 S. Ct. 1673 (2003).

⁵⁰ *Id.* at 1680-81.

⁵¹ *Id.* at 1677-78.

⁵² 490 U.S. 730 (1989).

⁵³ 503 U.S. 318 (1992).

understood by common law agency doctrine.⁵⁴ In *Clackamas*, as in *Darden* and *Reid*, the Court cited the Restatement (Second) of Agency, which refers to a person whose work is “controlled or is subject to the right to control by the master.”⁵⁵ Although *Reid* and *Darden* involved different statutes and different contexts, the Court applied the principle announced in those cases of incorporating common law to fill gaps in defining the term “employee.” In *Clackamas*, the Court concluded that “the common-law element of control is the principal guidepost” in distinguishing employers from employees.⁵⁶

In focusing on the element of control, the *Clackamas* Court agreed with the approach taken by the EEOC in its Compliance Manual, which lists six factors to distinguish between the individual who “acts independently and participates in managing the organization” and individuals who are “subject to the organization’s control.”⁵⁷ The six factors listed by the EEOC to distinguish between employers and employees utilizes an approach similar to that taken in the *Darden* case, in which the Court recognized sixteen factors to distinguish between independent contractors and employees.⁵⁸ In adopting the EEOC’s six factors, the *Clackamas* Court was “persuaded by the EEOC’s focus on the common-law touchstone of control.”⁵⁹ The Compliance

⁵⁴ *Clackamas*, 123 S. Ct. at 1677-78 (citing *Darden*, 503 U.S. at 322-23 and quoting *Reid*, 490 U.S. at 739-40). Some lower courts were reluctant to employ the common law approach articulated in *Darden*, finding the case inapposite because the factors used to distinguish independent contractors from employees were distinct from those needed to distinguish employers from employees. See *Serapion v. Martinez*, 119 F.3d 982, 986 (1st Cir. 1997); *Wheeler v. Main Hurdman*, 825 F.2d 257, 271-72 (10th Cir. 1987).

⁵⁵ *Clackamas Gastroenterology Assocs. v. Wells*, 123 S. Ct. 1673, 1678 (2003) (citing *Darden*, 503 U.S. at 323-24; RESTATEMENT (SECOND) OF AGENCY § 220(2) (1958)).

⁵⁶ *Clackamas*, 123 S. Ct. at 1679.

⁵⁷ *Id.* at 1680 (citing EEOC COMPLIANCE MANUAL, *supra* note 6).

⁵⁸ *Darden*, 503 U.S. at 323-24.

⁵⁹ *Clackamas*, 123 S. Ct. at 1680 (citing *Skidmore v. Swift & Co.*, 323 U.S. 134 (1944)).

Manual lists the following six factors to consider in determining whether an individual is subject to the organization's control and, hence, an employee:

1. Whether the organization can hire or fire the individual or set the rules and regulations of the individual's work;
2. Whether and, if so, to what extent the organization supervises the individual's work;
3. Whether the individual reports to someone higher 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;
6. Whether the individual shares in the profits, losses, and liabilities of the organization.⁶⁰

With the EEOC definition of employee in mind, the Court provides a definition of employer as "the person, or group of persons, who owns and manages the enterprise. The employer can hire and fire employees, can assign tasks to employees and supervise their performance and can decide how the profits and losses of the business are to be distributed."⁶¹ As the *Darden* Court did with the sixteen factors to distinguish employees from independent contractors, the *Clackamas* Court instructs that the EEOC factors that distinguish employers from employees are to be considered as a whole, "with no one factor being decisive."⁶²

⁶⁰ EEOC COMPLIANCE MANUAL, *supra* note 6, pt. 2(III)(D).

⁶¹ *Clackamas*, 123 S. Ct. at 1680.

⁶² *Id.* at 1681 (quoting *Darden*, 503 U.S. at 324). Nonetheless, it should be noted that the common law of agency right to control is critical to the Court's analysis in *Clackamas*. The dissent protests that the majority opinion selects control over the work of others and "accords that factor

Using the EEOC's standards, the Court indicated that the physician shareholders in question did not appear to be employees of the clinic, finding that factors such as their control and operation of the clinic, profit sharing, and personal liability for malpractice claims weighed in favor of employer status.⁶³ Nevertheless, the Court remanded the case so that the record could be examined and the shareholder directors' status determined in accordance with the EEOC standards.⁶⁴

D. The Dissent

The two dissenting Justices began by noting that the Court has recognized that an individual may be both a proprietor and an employee of a business entity.⁶⁵ The dissent maintained that the physician shareholders, involved in daily care at the clinic, functioned as employees.⁶⁶ Furthermore, there is no reason to shelter the clinic from ADA compliance.⁶⁷

Although the dissenting Justices agreed with the majority that the common law of agency was the appropriate point of departure for determining who was an employee, they

overriding significance." *Clackamas*, 123 S. Ct. at 1681 (Ginsburg, J., dissenting).

⁶³ *Id.* at 1681.

⁶⁴ *Id.* at 1681 n.11 (stating that there may be evidence that would "support a contrary conclusion under the EEOC's standard" in that "the four director-shareholders receive salaries, must comply with standards established by the clinic, and report to a personnel manager").

⁶⁵ *Clackamas*, 123 S. Ct. at 1681 (Ginsburg, J., dissenting) (citing *Goldberg v. Whitaker House Coop., Inc.*, 366 U.S. 28, 32 (1961)).

⁶⁶ *Clackamas*, 123 S. Ct. at 1681.

⁶⁷ *Id.* As the dissent notes, changes in ownership stakes such as one shareholder selling his share in the business to become a "mere" employee should not affect the jurisdictional threshold because such a change would not change the size or magnitude of the operation. *Id.* at 1682. The dissent appears more disturbed that a non-shareholder former employee is unable to sue under the ADA (as opposed to a claimant shareholder being unable to sue) and that such a determination should be based upon how the character of the relationship between the doctors and the professional corporation is construed. *Id.* at 1683.

maintained that the Court accorded too much weight to "control over the work of others engaged in the business of the enterprise."⁶⁸ Control is but one factor in determining the employment relationship, according to the dissenting Justices.⁶⁹ The dissent interpreted the employment relationship differently from the majority opinion, finding that the doctors were employees serving the corporation as master.⁷⁰ Factors cited by the dissent that weigh in favor of characterizing the doctors as employees include the existence of employment contracts, under which they receive salaries and yearly bonuses, the fact that they worked at facilities owned or leased by the corporation, and the fact that the doctors must comply with corporate standards.⁷¹ Furthermore, the dissent noted that the physician shareholders are considered employees for other purposes, such as ERISA and Oregon's workers' compensation law.⁷²

IV. IMPACT OF THE *CLACKAMAS V. WELLS* DECISION

In deciding *Clackamas*, the United States Supreme Court resolved several issues that have been addressed differently by lower courts. The following sections illustrate how the Court's decision has answered several difficult questions that have appeared repeatedly in lower court decisions. The first subsection illustrates that the Court has chosen a method of defining employers and employees that encompasses all forms of business organization and how the Court's decision will necessitate change in the lower courts' approaches to cases involving employment status, especially those involving corporate directors, officers, and major shareholders. The second subsection explores the Court's references to the status of partners and its dicta that partners may, in some circumstances, be considered

⁶⁸ *Id.*

⁶⁹ *Id.*

⁷⁰ *Id.* at 1681.

⁷¹ *Id.* at 1682.

⁷² *Id.*

employees. The third subsection discusses the Court's conclusion that the definition of employee must be the same in all cases seeking to determine status under the federal antidiscrimination laws, whether the individuals in question are claimants or individuals whom a plaintiff seeks to count toward the statutory minimum.

A. Uniformity in Approach: One Test for All Forms of Business Organization

The Court's decision makes it clear that neither the form of business organization nor an individual's title determines coverage under the statutes. The Court stated, "[t]he mere fact that a person has a particular title—such as partner, director, or vice president—should not necessarily be used to determine whether he or she is an employee or a proprietor."⁷³ In adopting the EEOC's six factor test to determine who is an employee, and through other language in the opinion, the Court resolved the different approaches that circuit courts had taken to defining employees under the antidiscrimination laws. Reversing the decision of the Court of Appeals for the Ninth Circuit, the Supreme Court clearly rejected the corporate form approach followed by that circuit and the Second Circuit.⁷⁴ Although the Court's decision embraces factors similar to those adopted by courts following the economic realities approach, the emphasis on control as the decisive factor in determining whether an individual is an employer or employee should resolve disparities among the lower courts because they have used different factors to determine employee status or have weighted those factors differently.⁷⁵

⁷³ *Clackamas*, 123 S. Ct. at 1680.

⁷⁴ *See Wells v. Clackamas Gastroenterology Assocs.*, 271 F.3d 903 (9th Cir. 2001); *Hyland v. New Haven Radiology, P.C.*, 794 F.2d 793 (2d Cir. 1986).

⁷⁵ *Compare, e.g., Wheeler v. Main Hurdman*, 825 F.2d 257 (10th Cir. 1987) (applying economic realities test, court found that claimant was a partner, not an employee entitled to federal discrimination protection under Title VII, the ADEA, and the Equal Pay Act, despite the fact that

Because the EEOC factors extend to investigations not only of partners and shareholders in professional corporations, but also of officers, members of boards of directors, and major shareholders, courts will have to revise how they assess the employment status of such individuals. A case recently decided by the Court of Appeals for the Tenth Circuit as well as the cases on which the Tenth Circuit relied, illustrate that courts have looked at controversies involving major shareholders and officers and directors differently than cases involving partners in a partnership or shareholders in a professional corporation and that the *Clackamas* decision will change the approach to such cases and may impact the outcome of such cases as well.

The United States Court of Appeals for the Tenth Circuit considered whether a majority stockholder who has supervisory powers, performs services for the corporation, and does not answer to any higher authority in the corporation, is an employer or employee under the federal antidiscrimination laws. In *Trainor v. Apollo Metal Specialties, Inc.*, the plaintiff Trainor, the former general manager of Apollo Metal Specialties, Inc., sued Apollo and its majority stockholder, Mr. Pilgrim,⁷⁶ on ADA as well as state

she was one of 502 partners in a firm of 3570 individuals; her contribution to capital was relatively insignificant, .000058 share of the firm's total capital account; and she had little independence or decision making power), and *Serapion v. Martinez*, 119 F.3d 982 (1st Cir. 1997) (partner who had 4% equity interest in firm as opposed to 24% held by the other four partners and received approximately one-third less compensation was nevertheless an employer, not entitled to sue under Title VII), with *Simpson v. Ernst & Young*, 100 F.3d 436, 442 (6th Cir. 1996) (applying economic realities test the court found that the plaintiff's actual role in the partnership was closer to that of an employee than a partner employer based on the fact that he had "few, if any, meaningful attributes of a partner").

⁷⁶ The court initially noted that defendant, Mr. Pilgrim, is a majority stockholder, but later in the opinion, mentioned that Mrs. Pilgrim is an equal owner. Mr. and Mrs. Pilgrim were the sole stockholders of the corporation. There was some dispute as to whether initially there was a third owner, but the court ultimately found the stock ownership irrelevant to the existence of an employment relationship. 318 F.3d 976, 977, 983 at n.5 (10th Cir. 2002).

law discrimination claims, and common law causes of action.⁷⁷ The court categorized Mr. Pilgrim as “both an owner and a participant in a traditional employment relationship with the corporation.”⁷⁸ Mr. Pilgrim and his wife owned equal shares in all of the company’s stock, but he also performed services for Apollo for which he was paid a salary.⁷⁹

In deciding whether an owner could also be an employee for purposes of the federal antidiscrimination laws, the appellate court chose not to follow the economic realities analysis used in cases involving partners. The court reasoned that cases involving partners in a partnership were not helpful because of the “hallmark distinction between shareholders and partners” regarding liability for the firm’s debts and obligations.⁸⁰ Because cases involving professional corporations usually emphasize the similarity between partnerships and professional corporations, the court also disregarded cases involving shareholders in professional corporations.⁸¹ Concluding that neither cases involving partnerships nor professional corporations were relevant to cases involving major shareholders in a general corporation, the court looked to cases involving corporate officers or directors. The Tenth Circuit relied on a decision by the Court of Appeals for the Second Circuit in a case that involved the employment status of corporate directors.⁸² That case is worth noting, as the *Clackamas* decision changes both its approach and outcome.

In *EEOC v. Johnson & Higgins, Inc.*, the EEOC sought to determine whether the company’s mandatory retirement policy, which required that directors retire at age 60 or 62, violated the ADEA.⁸³ According to the firm, the directors were “owner-managers” but also continued to serve actively

⁷⁷ *Id.* at 978.

⁷⁸ *Id.* at 983.

⁷⁹ *Id.*

⁸⁰ *Id.* at 984-85.

⁸¹ *Id.* at 985.

⁸² *EEOC v. Johnson & Higgins, Inc.*, 91 F.3d 1529 (2d Cir. 1996).

⁸³ *Id.*

as officers and employees.⁸⁴ The directors were subject to an annual performance review by one of the six senior Board members and compensation was based on the firm's profits as determined by that review.⁸⁵ The district court found that the ADEA applied to the company's mandatory retirement policy because the directors were also employees of the company and the retirement policy required them to end not only their positions as directors but also their positions as officers or employees of the company.⁸⁶ On appeal, Johnson & Higgins relied on *Hyland v. New Haven Radiology Assocs.*, which stated that the corporate form precludes an inquiry into whether individuals employed by a corporation are like partners.⁸⁷ The Court of Appeals for the Second Circuit maintained that *Hyland* was still good law but that the question whether the directors were employees required an analysis different from that of partners or shareholders.⁸⁸

Employing what it termed "a somewhat nebulous 'common law agency' test of employment," the Second Circuit used the following three-prong test to determine whether the directors were employers or employees: (1) whether the director has undertaken traditional employee duties; (2) whether the director was regularly employed by a separate entity; and (3) whether the director reported to someone higher in the hierarchy.⁸⁹ Using this test, the court in *Johnson & Higgins* concluded that the directors were employees as a matter of law because they all performed traditional employee duties; they all worked full time for the

⁸⁴ *Id.* at 1532.

⁸⁵ *Id.*

⁸⁶ *Id.* at 1533.

⁸⁷ 794 F.2d 793 (2d Cir. 1986); *see supra* text accompanying notes 25-27.

⁸⁸ *EEOC v. Johnson & Higgins, Inc.*, 91 F.3d 1529, 1538-39 (2d Cir. 1996) (stating "[w]hile *Hyland* prevents J & H from claiming that its directors are 'partners,' that case does not preclude the argument that J & H should be exempt from the ADEA on account of their position as *directors*").

⁸⁹ *Id.* at 1539 (citing *Lattanzio v. Security Nat'l Bank*, 825 F. Supp. 86, 90 (E.D. Penn. 1993)).

corporation, not for a separate entity; and although the Board was the highest authority, each director reported to the senior members of the Board, who conducted annual performance evaluations.⁹⁰ The court conceded that directors took on additional policy-making responsibilities and that their compensation in the form of a percentage of annual profits was not consistent with a traditional employment relationship.⁹¹ Nevertheless, these factors were apparently less important than the employee-related criteria the court considered fulfilled by the directors. The court held that the mandatory retirement policy violated the ADEA because it required directors to retire as officers and managers employed by the firm, at the age of 60 or 62, in violation of the congressionally mandated minimum age of 65 for senior level employees.⁹²

Applying the three-prong test used by the Court of Appeals for the Second Circuit in *EEOC v. Johnson & Higgins*, the Court of Appeals for the Tenth Circuit in *Trainor* focused on the employment relationship that Mr. Pilgrim had with the corporation, specifically the fact that he performed services for the corporation and was paid for those services.⁹³ The fact that Mr. Pilgrim answered only to himself and not to a higher authority did not dissuade the court from finding that he could be an employee of the corporation. Based on his employment with the corporation, the court of appeals found that the district court had erred in concluding that Mr. Pilgrim was not an employee as a matter of law and remanded the case for further review.⁹⁴

Under the EEOC factors adopted by the Supreme Court in *Clackamas*, both Mr. Pilgrim and the directors in the *Johnson & Higgins* case would most likely be classified as employers rather than employees. As the dissenting judge pointed out in *Johnson & Higgins*, the three factors that the

⁹⁰ *Id.* at 1539-40.

⁹¹ *Id.*

⁹² *Id.* at 1540 (citing 29 U.S.C. § 631 (c) (2000)).

⁹³ *Trainor v. Apollo*, 318 F.3d 976, 987 (10th Cir. 2002).

⁹⁴ *Id.*

court focused on are not sufficient to evaluate the employment relationship.⁹⁵ According to the dissenting judge, Johnson & Higgins bestowed on its directors “privileges and powers held by few persons in the corporate world.”⁹⁶ The directors clearly fulfilled several of the EEOC factors that would indicate they acted independently and participated in managing the organization as employers rather than as employees subject to the organization’s control. Directors are elected with the express purpose of influencing the organization and they share in the profits of the organization, facts which would weigh in favor of employer status, according to the EEOC guidance.⁹⁷ Although the Second Circuit emphasized the fact that the directors were evaluated by the six senior members of the firm, this fact seems less important given that the corporation has approximately thirty-five directors in an organization that employs over 8,000 individuals worldwide.⁹⁸ As the dissenting judge insisted, the members of the board of directors were employers because they acted as owners and managers, reporting to no one other than themselves.⁹⁹

The EEOC factors are also more likely to lead to a conclusion that Mr. Pilgrim, the majority stockholder who also performed traditional employee duties, is an employer. For example, a court using the EEOC factors would have considered the fact that Mr. Pilgrim answered to no one but himself as significant in determining that he was able to act independently and was not subject to the organization’s control. The Tenth Circuit, however, did not weigh this factor in its decision. Furthermore, Mr. Pilgrim, as the majority stockholder, most likely could not be fired by the

⁹⁵ EEOC v. Johnson & Higgins, Inc., 91 F.3d 1529, 1544 (2d Cir. 1996) (Jacobs, J., dissenting).

⁹⁶ *Id.* at 1543.

⁹⁷ In a letter to the EEOC, Johnson & Higgins described those elected as directors as individuals who the Board believes “will contribute in a material way to the future success of the firm.” *Id.* at 1532.

⁹⁸ *See id.*

⁹⁹ *Id.* at 1545.

corporation, nor was his work subject to rules and regulations of the organization, all factors which the EEOC guidelines recognize as supporting employer status.¹⁰⁰

Both the Court of Appeals for the Second Circuit in *Johnson & Higgins* and the Court of Appeals for the Tenth Circuit in *Trainor v. Apollo*, recognized that individuals may fulfill dual roles as employers and employees. Each court was willing to find that individuals could be employees entitled to the protection of the federal antidiscrimination laws, despite the fact that they enjoyed positions of ownership, management and control. The Supreme Court's decision in *Clackamas*, however, indicates that if elements of control are present, the role of employer will predominate in determining status under the federal discrimination statutes. The Supreme Court did not cite the language that introduces the six factors that assist in determining coverage; the section begins with a statement that "[i]n most circumstances, individuals who are partners, officers, members of boards of directors, or major shareholders will not qualify as employees."¹⁰¹ In adopting the EEOC's guidance, therefore, the Supreme Court significantly changed the emphasis on who qualifies for protection under

¹⁰⁰ EEOC COMPLIANCE MANUAL, *supra* note 6, pt. 2(III)(D). The fact that Mr. Pilgrim was paid a salary would not outweigh all the other indicia of his control. A federal district court has since applied theories from *Trainor* to another counting case involving an S corporation. *Arbaugh v. H Corp.*, No. 01-3376, 2003 U.S. Dist. LEXIS 5568 (E.D. La. Apr. 2, 2003) was decided just prior to *Clackamas*. Thus, the court in *Arbaugh* continued to analogize the shareholders to partners, rather than simply asking whether they were employers. The district court held that owner managers were partners or employers, not employees, leading the court to grant a motion for summary judgment for the defendant. The district court in *Arbaugh* questioned whether the existence of two of the three factors as in *Trainor* should be sufficient to find that a corporate officer or director is also an employee, noting in particular the absence of a person reporting to a higher authority as problematic because it "is an essential element of the employer/employee relationship." *Id.* at *25. Further, the district court noted that this element would be lacking in many professional corporations and closely held corporations. *Id.*

¹⁰¹ EEOC COMPLIANCE MANUAL, *supra* note 6, pt. 2(III)(D).

task has become increasingly difficult, as one court noted, because “[p]artnerships are mutable structures, and partners come in varying shapes and sizes.”¹⁰⁷ Large partnerships whose management resides in the hands of a small group of partners are particularly likely to face the question of whether those labeled partners may be considered employees under federal antidiscrimination laws.

The facts of the *Clackamas* case did not require the Court to address questions about whether partners in a partnership may be considered employees, but the professional corporation’s insistence that its physician shareholders functioned like partners led the Court to comment on the employment status of partners. The Court rejected the professional corporation’s comparison between partners and shareholders in a professional corporation, remarking that “asking whether shareholder-directors are partners—rather than asking whether they are employees—simply begs the question.”¹⁰⁸ Noting that many partnerships include hundreds of members, the Court stated that some of them “may well qualify as ‘employees’ because control is concentrated in a small number of managing partners.”¹⁰⁹ Adopting a common law approach, with assistance from the EEOC factors as the means to differentiate between employers and employees, the Supreme Court in *Clackamas* rejected the argument by the physician shareholders that their employment status rested on whether they were, “in reality,” partners, thereby confirming that the label “partner” is not sufficient to rule out the possibility that an individual may be an employee who is entitled to protection under the federal employment discrimination laws.¹¹⁰ The

¹⁰⁷ *Serapion v. Martinez*, 119 F.3d 982, 987 (1st Cir. 1997); see also Kristin Nicole Johnson, *Resolving the Title VII Partner-Employee Debate*, 101 MICH. L. REV. 1067 (2003) (arguing that Title VII should include partners as employees and maintaining that the modern partnership has changed significantly since Justice Powell’s opinion in *Hishon*).

¹⁰⁸ *Clackamas Gastroenterology Assocs. v. Wells*, 123 S. Ct. 1673, 1678 (2003).

¹⁰⁹ *Id.*

¹¹⁰ *Id.*

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¹⁰⁷ *Serapion v. Martinez*, 119 F.3d 982, 987 (1st Cir. 1997); see also Kristin Nicole Johnson, *Resolving the Title VII Partner-Employee Debate*, 101 MICH. L. REV. 1067 (2003) (arguing that Title VII should include partners as employees and maintaining that the modern partnership has changed significantly since Justice Powell’s opinion in *Hishon*).

¹⁰⁸ *Clackamas Gastroenterology Assocs. v. Wells*, 123 S. Ct. 1673, 1678 (2003).

¹⁰⁹ *Id.*

¹¹⁰ *Id.*

Court makes it clear that partners and partnerships should not be treated any differently than individuals bearing other titles in other types of business organizations. Because the statutes distinguish only between employers and employees, defining those terms should transcend attempts to analogize various employment relationships to the partnership relationship.¹¹¹

Lower courts that have followed various versions of the economic realities test have also resisted the conclusion that partners are employers per se.¹¹² The economic realities tests employed to determine who qualifies as a true partner have focused on certain indicia of partnership—generally including ownership, remuneration and management.¹¹³ Some overlap occurs between the partnership criteria that courts have generally considered and the EEOC factors. Most notably, the EEOC factors consider “whether the individual shares in the profits, losses, and liabilities of the organization.”¹¹⁴ The EEOC factors and the *Clackamas*

¹¹¹ Several courts fell into a trap of fallacious reasoning, arguing that certain individuals were or were not employees because they were like or unlike partners. *See, e.g., Schmidt v. Ottawa Med. Ctr.*, 322 F.3d 461, 466 (7th Cir. 2003) (concluding that a physician shareholder in a professional corporation played a role “akin to that of a bona fide partner-employer rather than that of an employee”); *Hyland v. New Haven Radiology Assocs.*, 794 F.2d 793, 794 (2d Cir. 1986) (finding that a professional corporation was not a partnership).

¹¹² *See, e.g., Serapion v. Martinez*, 119 F.3d 982 (1st Cir. 1997) (stating that “Title VII’s employment-related shelter might in certain circumstances extend to a person who is a partner in a law firm”); *Simpson v. Ernst & Young*, 100 F.3d 436 (6th Cir. 1996) (holding that individual who held title of partner was not a partner and could bring suit under the ADEA as an employee); *EEOC v. Peat, Marwick, Mitchell and Co.*, 775 F.2d 928 (8th Cir. 1985) (partner could be considered an employee in some situations). Courts that follow the corporate form approach take a similar method to partnerships as those employing the economic realities approach, but limit the economic realities test to cases involving “actual de jure partnerships.” *EEOC v. Johnson & Higgins*, 91 F.3d 1529, 1538 (2d Cir. 1996) (citing *Hyland v. New Haven Radiology Assocs.*, 794 F.2d 793, 797 (2d Cir. 1986)).

¹¹³ *See Serapion*, 119 F.3d at 990 (1st Cir. 1997).

¹¹⁴ EEOC COMPLIANCE MANUAL, *supra* note 6.

decision, however, focus more on the overall issue of control, thereby expanding the potential candidates for employee status beyond those who would have been considered employees under the economic realities tests proposed by the various circuit courts of appeal. In a sense, emphasizing the control factor reverts to the theory that those in control are not in need of protection, but those who have little or no control do need the protection of the employment discrimination statutes.¹¹⁵

The Court's comments in *Clackamas* indicate that some individuals who bear the title "partner" may be employees entitled to the protection of the federal discrimination statutes. The *Clackamas* decision offers timely guidance to the district court and the Court of Appeals for the Seventh Circuit in a case involving an EEOC investigation of age discrimination at a large law firm. In *EEOC v. Sidley Austin Brown & Wood*, the EEOC sought information to determine whether the law firm, Sidley, had violated the ADEA by demoting thirty-two partners to "counsel" or "senior counsel" status.¹¹⁶ Because antidiscrimination laws such as the ADEA do not protect employers, the EEOC must establish that the demoted individuals were employees before their demotion.¹¹⁷

The law firm claimed that it did not have to provide additional information to the EEOC, because it had provided sufficient information to indicate that the individuals in question were "real partners" and, consequently, not employees covered by the ADEA.¹¹⁸ Sidley argued that "a partner is an employer within the meaning of the federal antidiscrimination laws if (a) his income included a share of the firm's profits, (b) he made a contribution to the capital of the firm, (c) he was liable for the firm's debts, and (d) he had

¹¹⁵ The Court of Appeals for the Tenth Circuit discounted this "domination" theory in *Wheeler v. Main Hurdman*, 825 F. 2d 257, 269 (10th Cir. 1987).

¹¹⁶ 415 F.3d 696, 698 (7th Cir. 2002).

¹¹⁷ *Id.*

¹¹⁸ *Id.* at 698-99.

some administrative or managerial responsibilities.”¹¹⁹ The firm maintained that all of these criteria had been proven concerning the thirty-two individuals in question.¹²⁰

Judge Posner, writing for the majority, questioned Sidley’s assumptions that partners are not entitled to protection under the antidiscrimination laws because partners are always employers. Judge Posner identified the issue by querying, “Employers are not protected . . . but are partners employers? Always?”¹²¹ Noting that the antidiscrimination laws do not contain an exemption for discrimination against partners, Judge Posner maintained that even if the individuals were partners before their demotion, it does not necessarily follow that they were employers.¹²² At the heart of Judge Posner’s concern is the fact that state laws allow a partnership to be “reconfigured” so as to function as a “de facto corporation” and that a federal agency should not be hamstrung by such reconfigurations to treat all individuals labeled partners as employers.¹²³

Because the status of the demoted individuals was critical to the EEOC’s inquiry, the Seventh Circuit instructed the lower court to order defendant Sidley to comply with the EEOC’s request for documents relating to whether the thirty-two demoted partners were covered employees under the ADEA.¹²⁴ The appellate court ruled that the defendant law firm was not required to comply with requests for information regarding the reasons for demotions until the trial court determined whether the partners in question were protected employees for purposes of the ADEA, but stated that “there is enough doubt about whether the 32 demoted partners are covered by the age discrimination law to entitle

¹¹⁹ *Id.* at 699.

¹²⁰ *Id.*

¹²¹ *Id.* at 702.

¹²² *Id.* at 701-02.

¹²³ *Id.* at 705.

¹²⁴ *Id.* at 707.

the EEOC to full compliance with that part, at least, of its subpoena."¹²⁵

The *Clackamas* decision makes it clear that titles and labels are not the key to deciding employer or employee status. Whether the thirty-two individuals who were demoted at Sidley will be considered employees or employers will turn on the extent of control each had as measured by the EEOC factors, not on whether or not they were partners. The Supreme Court's decision and reflection on the EEOC factors will undoubtedly impact the manner in which partnerships, especially large firms, structure the employment relationship with partners.¹²⁶

C. The Same Definition of Employee Applies to Both Counting and Claimant Cases

The *Clackamas* decision supports the conclusion that the approach to determining who is an employee is the same, whether the case involves counting employees for jurisdictional purposes or evaluating the status of a claimant. In a footnote, the Court stated that "the meaning of the term 'employee' comes into play when determining whether an individual is an 'employee' who may invoke the ADA's protections . . . as well as when determining whether an individual is an 'employee' for purposes of the 15-employee threshold."¹²⁷ Courts have generally treated counting cases and claimant cases in the same manner. This approach is logical because the statutes distinguish only between employers and employees. Nevertheless, some plaintiffs have argued that courts should be more inclusive, interpreting employee status more broadly when the

¹²⁵ *Id.*

¹²⁶ See David A. Rappaport, Note, *A Coming of Age? Why Revised EEOC Guidelines May Force Firms to Protect Against Partner Age Discrimination Suits*, 59 WASH. & LEE L. REV. 1013 (2002) (cautioning law firms, professional organizations, and individuals who work for them to assess how the EEOC guidelines impact them).

¹²⁷ *Clackamas Gastroenterology Assocs. v. Wells*, 123 S. Ct. 1673, 1679 n.6. (2003).

claimant is clearly an employee, but needs to qualify other individuals, such as partners or shareholders, to meet the statutory minimum. In fact, Ms. Wells initially argued that a different test should be used to determine who is an employee under the ADA “depending upon whether the inquiry is coverage or the right to sue.”¹²⁸ The district court rejected any distinction between the two types of suits in defining the term “employee,” stating that the ADA contains only one definition of the term and no suggestion that different tests should be used in different types of cases.¹²⁹

Other courts have also rejected making a distinction in approach between cases involving coverage or the right to sue. In *Schmidt v. Ottawa Medical Center*, a case decided shortly before the *Clackamas* decision, the Court of Appeals for the Seventh Circuit considered whether a physician shareholder in a professional corporation could bring a claim under the ADEA.¹³⁰ Dr. Schmidt was one of eight shareholder physicians in a professional corporation.¹³¹ Alleging age discrimination, Dr. Schmidt had to prove first that he was an employee entitled to the statute’s protection.¹³² In *Clackamas*, the status of the physician shareholders at Clackamas Gastroenterology was raised only to determine whether the statutory minimum of fifteen employees was satisfied; the plaintiff Wells was clearly an employee prior to her termination.¹³³ Thus, in *Clackamas*,

¹²⁸ *Wells v. Clackamas Gastroenterology Assocs.*, No. CV 99-406-AS, 2000 U.S. Dist. LEXIS 8590, at *5 (D. Or. Mar. 22, 2000).

¹²⁹ *Id.* In fact, the district court decision in *Wells* noted that if “different definitions were used, inconsistent results would be possible.” *Id.* See also, Stephanie Greene & Christine Neylon O’Brien, *Partners and Shareholders as Covered Employees under Federal Antidiscrimination Acts*, 40 AM. BUS. L.J. 781, 819-20 (2003) (maintaining that there is a theoretical basis to distinguish the two types of cases but that courts are bound by the single definition in the statutes and such a distinction could only be made by legislative amendment).

¹³⁰ 322 F.3d 461, 462 (7th Cir. 2003).

¹³¹ *Id.*

¹³² *Id.*

¹³³ *Clackamas Gastroenterology Assocs. v. Wells*, 123 S. Ct. 1673, 1676 (2003).

counting the physician shareholders as employees would have allowed a bona fide employee to bring her claim, whereas in *Schmidt* the question was whether the shareholder himself could seek protection under the federal employment discrimination laws. In deciding *Schmidt*, the Court of Appeals for the Seventh Circuit looked to a case it had previously decided involving employment status in a professional corporation. In *EEOC v. Dowd & Dowd*, the court adopted an economic realities approach to determine the employment status of shareholders in a professional corporation.¹³⁴ *Dowd*, however, like *Clackamas*, was a counting case, not a case that involved a shareholder claimant, as *Schmidt* did. In *Schmidt*, the court considered whether the same economic realities analysis of determining who is an employer or employee applied where the shareholder herself is a claimant, and, if so, which factors should determine the shareholder's status as employer or employee.¹³⁵

In *Schmidt*, the Court of Appeals for the Seventh Circuit also referred to its recent decision in *EEOC v. Sidley Austin Brown & Wood*,¹³⁶ in which it allowed an EEOC investigation of partner status to continue.¹³⁷ Although the issue of the status of the individuals in question in *Sidley* was remanded for further inquiry, the court stated that its holding in *Sidley* "must be read to apply *Dowd's* functional test of employee status to determinations of whether an individual claimant qualifies as an employee under the ADEA."¹³⁸

¹³⁴ 736 F.2d 1177, 1178 (7th Cir. 1984).

¹³⁵ *Schmidt v. Ottawa Med. Ctr.*, 322 F.3d 461, 463-64 (7th Cir. 2003).

¹³⁶ 315 F.3d 696 (7th Cir. 2002).

¹³⁷ See *supra* text accompanying notes 116-25.

¹³⁸ *Schmidt*, 322 F.3d at 464 (emphasis added). While clarifying that the economic realities test or functional approach applies to partners and shareholders alike, the Seventh Circuit sidestepped the question of which factors are critical to the status determination. In *Schmidt*, the court stated that it anticipated a multi-factored analysis that would go beyond labels in determining the status of shareholders and partners, identifying statutory purpose and common law agency principles as two potential forces that could influence what those factors should be. *Id.* at 464-65.

Had the court of appeals in *Schmidt* had the benefit of the *Clackamas* decision and the Supreme Court's endorsement of the EEOC factors, its conclusion would undoubtedly have been the same. The Court of Appeals for the Seventh Circuit accurately anticipated that the Supreme Court would not distinguish between counting cases and claimant cases in determining who is an employee.

Although several lower courts have considered the option of treating counting cases and claimant cases differently, none have adopted different approaches. The dissenting justices in the *Clackamas* case raise the issue as one connected to the corporate form approach. Justice Ginsburg favored treating the shareholder physicians as employees because they performed services on behalf of the corporation, had employment contracts, and were admittedly employees

The court cited control as a relevant factor to both agency law and statutory purposes; agency law focusing on the right to control the work of another, and statutory purpose focusing on controlling access to the job market. *Id.* at 466. Stating that it need not articulate specific factors to decide Dr. Schmidt's case, the court noted that Dr. Schmidt had significant control over the professional corporation throughout his career, as a corporate officer and director with voting rights equal to those of the other seven physician shareholders. *Id.* at 467. Dr. Schmidt's employment agreement characterized him as an employee, the court noted, but this did not diminish his control over the organization. The court concluded that Dr. Schmidt was a bona fide employer, holding "that when an individual claimant-shareholder enjoys the opportunity for shared control of the closely held professional corporation, including the opportunity to share in its profits," he is not entitled to sue under the ADEA. *Id.* at 467-68. The language of the Court of Appeals for the Seventh Circuit in *Schmidt* seems to imply that its holding is limited to individual claimant shareholders. The district court in *Schmidt* made clear that it would treat the definition of employee the same in both counting and shareholder claimant cases. *Schmidt v. Ottawa Med. Ctr., P.C.*, 155 F. Supp. 2d 919, 921 (N.D. Ill. 2001). "The issue in *Dowd & Dowd* was the number of employees for jurisdictional purposes, but the same test should be used to determine who is an employee regardless of whether the inquiry is coverage or the right to sue because the ADEA only contains one definition of 'employee,' and Dr. Schmidt gives no reason why a different test should be used." *Id.* (citing *Wells v. Clackamas Gastroenterology Assocs.*, 2000 WL 776416, at *2 (D.Or. May 5, 2000)).

for various purposes under federal and state law.¹³⁹ According to Justice Ginsburg, “the character of the relationship between Clackamas and the doctors supplies no justification for withholding from clerical worker Wells federal protection against discrimination in the workplace. . . .”¹⁴⁰ At the heart of Justice Ginsburg’s concern is the numbers issue. She criticizes the Court’s approach because it fails to account for the “magnitude of the company’s business or its capacity for complying with federal prescriptions.”¹⁴¹ Courts agree that Congress intended “to spare very small firms from the potentially crushing expense of mastering the intricacies of the antidiscrimination laws, establishing procedures to assure compliance, and defending against suits when efforts at compliance fail.”¹⁴² An argument can be made that firms that have the magnitude to comply with federal discrimination laws should not be exempted from coverage because individuals more closely fit the definition of employer than employee, especially when such designation prevents an employee from seeking the statutes’ protections.

Justice Ginsburg’s perception that the Court’s approach unfairly excludes those intended to be protected by federal discrimination laws can be rectified only by legislative amendment.¹⁴³ The plain language of the federal

¹³⁹ *Clackamas Gastroenterology Assocs. v. Wells*, 123 S. Ct. 1673, 1681-82 (2003) (Ginsburg, J., dissenting).

¹⁴⁰ *Id.* at 1683.

¹⁴¹ *Id.* at 1682. *See also* *Drescher v. Shatkin*, 280 F.3d 201, 205-06 (2d Cir. 2002) (plaintiff maintained unsuccessfully that “while there are different policy reasons for withholding the remedies of the Act from an ‘employee’ . . . who has the power to change whatever he might complain of, these policy reasons have little bearing on the counting of employees to determine whether the employer is small enough to be exempt from the act”).

¹⁴² *Papa v. Katy Industries, Inc.*, 166 F.3d 937, 940 (7th Cir. 1999).

¹⁴³ Judge Daughtrey of the United States Court of Appeals for the Sixth Circuit wrote a concurring opinion to encourage legislative amendment because business organizations such as partnerships have changed so greatly. Referring to nominal partners in large partnerships, Judge Daughtrey stated that “the nominal co-owners of the company are,

discrimination statutes gives no indication that the context should dictate how the term "employee" is interpreted. The discrimination laws should more clearly define "employee" in terms of whom the statutes intend to protect. At the same time, the statutes should better define which employers should be spared the burdens of compliance. While the definition of covered employers might still make reference to the number of employees required to meet a jurisdictional threshold, it should specify how the number of employees is determined. A compromise in defining employees might be reached by using the Supreme Court's *Clackamas* test and the EEOC factors it endorses for claimants, but broadening the test for jurisdictional purposes to include those who might be characterized as employers under the *Clackamas* test. The individuals included for counting purposes would not include those traditionally exempted from the count such as consultants and independent contractors, but would include partners, shareholders, officers, directors and other members who meet the hours per week and weeks per year requirements of the statutes. Such a compromise would best accommodate the goals of the federal discrimination statutes by extending protection to all who are not in positions of management or control while exempting only those firms whose size qualifies them for exemption.

V. CONCLUSION

In *Clackamas v. Wells*, the Supreme Court held that shareholders in a professional corporation do not qualify as employees for purposes of federal discrimination laws merely because they work for an entity that has a corporate form. The Court adopted neither the corporate form approach followed by two circuit courts of appeal nor the economic realities approach followed by the majority of the circuit courts of appeal. Instead, the Court developed a new test for

by necessity, so far removed from the seat of actual power as to be subject to the reach of the invidious acts that employment discrimination statutes seek to remedy." *Simpson v. Ernst & Young*, 100 F.3d 436, 445 (6th Cir. 1996) (Daughtrey, J., concurring).

interpreting the term "employee" in federal discrimination statutes. Using the common law of agency as a gap-filling mechanism for the sparse language of the statutes, the Court held that an individual's employment status depends on whether or not he or she has control within the organization. The Court endorsed factors outlined in the EEOC's Compliance Manual that assist in determining whether such control exists.

The Court's test for defining employers and employees, while similar to that used by courts employing the economic realities test, has several advantages. First, the test applies to all forms of business organization, eliminating the different approaches courts have taken to cases involving partners, shareholders, officers, and directors. Second, the Court emphasizes control as the deciding factor, so that courts weighing the various EEOC factors may achieve greater uniformity and firms and individuals assessing their employment relationship may more readily assess whether they are exposed or shielded by the discrimination statutes in question.

In addition to providing better guidance on how to determine "who counts" as employers and employees under the federal discrimination laws, the Court resolved several other questions regarding the definition of "employee." The Court allowed that partners are not always employers. Recognizing that partnerships have evolved from small, traditional, intimate organizations to large firms, where control may reside in a small fraction of the partners, the Court stated that partners may, in some circumstances, be employees entitled to the protection of the federal discrimination laws. The employment status of partners is subject to the same scrutiny as that of other principals in business organizations. The Court also concluded that the test for determining who is an employee applies to both counting and claimant cases.

The test announced in *Clackamas* for determining "who counts" under federal discrimination laws favors neither employers nor employees. The effect of the *Clackamas* case may be to deny coverage to an employee who claims

discrimination in a small firm, because the principals will be considered employers rather than employees for purposes of satisfying the jurisdictional minimum prescribed by the statutes. This outcome may seem unfair in cases where the number of employers is large. Nevertheless, the language of the statutes does not indicate a different definition of the term employee in cases involving claimants or size issues. The Court's decision, therefore, is true to the statutes' language and, in most cases, consistent with congressional intent to protect small firms from the burdens of compliance and litigation. Statutory amendments are necessary to remedy inconsistencies and unfairness in determining the size of a firm and whether it is subject to the discrimination laws.

Despite the hardship that the Court's decision might work on some employees, the decision does not necessarily have the effect of contracting the number of individuals protected by the discrimination laws. In fact, the approach adopted by the Court may have the effect of increasing the range of individuals that fall within the statutes' protections because some partners, officers, members of boards of directors, and major shareholders, who would have been defined as employers according to tests developed by the lower courts, may now be defined as employees entitled to the statutes' protections.