

Restrictive covenants and moving on as a partner

By Kristi Edwards

Despite the lingering malaise and threat of the dreaded “double dip” recession, we are seeing one of the most fluid legal recruitment markets at partner level in a number of years. Unprecedented levels of consolidation, no end of news of de-equitisations and the like and firms shifting focus as they scramble to remain relevant and attract talent in fashionable disciplines in the struggle to increase revenue: all factors that cause substantial activity (both as a result of choice and otherwise) at the top end.

When law firms really were making hay, in the halcyon days of 2005-2008, the majority of them were not harshly enforcing covenants, preferring to side-step disputes, attempting to retain clients, assisted by the implementation of garden leave provisions and the quality of their existing practices. We now exist in a new landscape. A challenging economic climate, the downward pressure on fees and the emphasis on retaining and increasing profits are ingredients for a swelling appetite for stricter enforcement of covenants; especially when a partner is seeking to move not only client relationships but a team of assistants and other partners.

If you are in a position where a move as a partner is something that you are considering, then in order to assess your ability to move with a client following (and potentially a team) and the timeline and ease with which you are able facilitate this, you will need to consider restrictive covenants and their enforceability. Partners are sometimes taken aback to find that their covenants actually have a fighting chance of being enforced, despite on first appearance seeming overly harsh. Whilst they should be of concern and you should bear them in mind, do consider that in practice, in most cases an agreement can be reached. There are few things you will need to do/contemplate in order to place yourself in the best position from which to negotiate.

1. Read the Deed

The first thing you will need to do is to re-familiarise yourself with your partnership deed or LLP agreement. The following “checklist” will always be applicable to equity partners and whether or not it is to salaried or to fixed share partners, will depend on whether their contractual terms would have them construed as *more* than mere employees with the badge of partner; for example, those who take part in partnership decisions, make capital contributions and take a share of profits.

The law treats partners and employees in this respect completely differently; the latter are deemed to have inherently weaker bargaining power and not to benefit from a stake in the goodwill of the firm. Whilst covenants are of course applicable to employees, they are certainly far more likely to be binding (and more onerous) on partners, so check where you stand.

What do clauses dealing with garden leave state? What are the provisions relating to the solicitation and canvassing of firm clients or conducting business with firm clients? What are the provisions relating to the solicitation of other partners or assistants?

Considering the way the deed addresses all of these points will at least place in you a position to understand, at least in theory, how your firm deal with partner exits. Forewarned is forearmed.

2. Look at precedents

Have regard to previous departures. Of course, how you are treated will very much be dependent on what (and indeed who) you are seeking to take with you but there will be a clue in how your current firm has handled exiting partners in the past: has this behaviour caused the restrictive covenant and notice obligations in the deed to be altered by conduct? Or, has there previously been a particularly vicious application of the

terms of your firm's deed or agreement? Past conduct will give you a very good idea as to what lengths your current firm is prepared to go to limit competitive damage and what course your negotiations will take.

3. Check the drafting

You would be surprised how many firms (even some larger and very successful ones) have poorly drafted provisions in relation to non-solicitation, non-acting, non-poaching, non-compete and garden leave, or remain silent on some or all of these, instead choosing to rely upon a notice period and a "duty of good faith" to the partnership. So, as well as reading the deed, you should also have regard to the way in which the document is drafted; are there vulnerabilities and holes or is it tightly drafted? A carefully drafted deed is generally a reflection of the way a firm will approach exit negotiations (including client portability, garden leave and team moves) and in some senses, will make the outcome more predictable and easier to plan for.

4. Plan. Plan. Plan.

Plan your communication carefully. It is generally the case that if you have received an offer to move as a lateral, you will have presented a detailed business plan, much of which related to your client base and the likelihood of that client base instructing you in your new "home". It will be very likely that you will have already had some oblique (and in some cases not so oblique) conversations with key clients who may have represented to you that they wish to continue instructing you. You will need to think very carefully about how and to what extent this message is communicated because you may have in theory already breached your agreement. Think also about how and when you will give notice and how you would like this communicated internally. You should be planning these conversations because there will be a number of things that need to be made clear in the early stages of your exit negotiations. You will also need to consider who it is that is likely to be making the decisions on your exit. It may be that you need to alter your approach to suit their style. Well planned communication will make your discussions more productive and ultimately lead to a faster resolution.

5. Record your meetings. Keep track of email correspondence

In some cases, exits will become contentious. Don't underestimate how time consuming and stressful this can be; sometimes in the mire of negotiations, discussions, emails and meetings record keeping can slip (yes, this is a point that even needs to be made to lawyers, especially when it is their personal situation and not client work we are discussing). Take care in the wording of emails and keep contemporaneous notes of all meetings, no matter how informal. Also do remember that once you have left the building you will likely not have access to your emails so any retrospective information gathering will not be possible!

Perhaps a note here on joining your new firm; do consider very carefully any new restrictions you are about to take on and sign up to. A bit like a pre-nup, you don't want to go into a marriage thinking it is going to fail but sometimes, it helps to put in place a framework in case things don't work out and you realise it is not the marriage made in heaven you thought it would be. Consider negotiating a clause within your agreement that effectively ring fences clients to exempt them from covenants, keeping them from being regarded as "firm clients" should you elect to move again.

We should also make an observation at this point on panel relationships; we are seeing fewer incidences of partners having a solely self-standing book of business and have for some time observed the effect of the increasingly panelised and institutional nature of significant client relationships. The more institutionalised the client base, the more law firms move toward the model of partners taking something akin to an "account manager" role. This shift in shape of the market and in the business of law firms can have an impact on your ease of movement.

In some disciplines such as banking, insurance and construction, law firm panels tend to be pretty tightly run but do have regard to the sheer size of some of these; if the firm you are joining has the benefit of being on your client's panel, even if it is not necessarily instructed to the same level or even for the same type of work, you will find a mutual panel spot helpful in arguing for non-enforcement of your covenants *and* your faster release. It is also significant to have an appreciation of any relevant client's ability to instruct "off panel" – an important factor and something you will need to explore. Keep in mind - it is rarely the case that there is not some kind of agreement that can be reached on such matters.

Indeed, we have heard of recent deals being struck that perfectly illustrate the point that in in these strained times, revenue (and the maintaining of it) is a priority that is jockeying for position with client wishes, shaping some interesting negotiation outcomes! We can cite a recent example of a departing partner who was able to negotiate a substantially reduced garden leave; he has continued to deal with the client (and accept instructions from them) at his new firm and yet have his previous firm's associates actually undertaking the work for a period of time. The client then bills the partner at his new firm who remits a fee to his old firm on a formula which means that although his new shop will benefit from the kudos of the client relationship, for a period of time, his alumni will enjoy the benefit of the bulk of the profit.

A final point in relation to team moves. No firm is going to be overjoyed with a partner potentially excising its entire ability to service a particular type of work or client or the cross-selling opportunities and profile that depart with him/her. It can be difficult to judge when to raise a potential move with your team and indeed how you should do that. A good recruiter can assist you at this point and there are a number of tools that can be used to help ease a sticky situation in this regard.

It remains the case that in the vast majority of exits, most situations are resolved amicably with a good dollop of pragmatism and commercial realism. Even with increasing efforts to wrench back or maintain the client relationships of departing partners, most firms will be able to come to a sensible compromise with regard to both clients and garden leave, after all who wants disaffected clients as the price of strict and unbending enforcement of covenants?

If the current economic woes prevail, it will be interesting to observe whether firms start to take a harder line in dealing with departing partners and teams. We suspect that client wishes will, on balance continue to trump those of law firms.