

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

ANNE ELIZABETH ZIEGLER : CIVIL ACTION
and DEBRA ANN DeANGELO :
 :
v. :
 :
ANESTHESIA ASSOCIATES OF :
LANCASTER, LTD. : NO. 00-4803

M E M O R A N D U M

WALDMAN, J.

March 12, 2002

Plaintiffs have asserted claims for sex discrimination in employment in violation of Title VII and the Pennsylvania Human Relations Act ("PHRA"). Plaintiffs allege that defendant refused to offer them partnership because of their sex, terminated Ms. Ziegler because of her sex and forced Ms. DeAngelo to resign because of her sex. Defendant filed a motion to dismiss for lack of subject matter jurisdiction, asserting that it never employed fifteen or more employees.

An entity must have at least fifteen employees each workday for at least twenty weeks in the current or preceding year to be an "employer" for purposes of coverage under Title VII. See 42 U.S.C. § 2000e(b). This requirement has been viewed as a jurisdictional prerequisite. See Hukill v. Auto Care, Inc., 192 F.3d 437, 441 (4th Cir. 1999)(federal court "lacks subject matter jurisdiction over an FMLA claim if the defendant is not an employer as that term is defined in the FMLA"), cert. denied, 529 U.S. 1116 (2000); Scarfo v. Ginsberg, 175 F.3d 957, 961 (11th

Cir. 1999)("[u]nless the appellees constitute an employer who has 15 or more employees ... Title VII is inapplicable, and the district court lacks subject matter jurisdiction"), cert. denied, 529 U.S. 1003 (2000); Simpson v. Ernst & Young, 100 F.3d 436, 439 (6th Cir. 1996)("the distinction between a partner and an employee under ADEA and ERISA is a preliminary jurisdictional issue"), cert. denied, 520 U.S. 1248 (1997); Greenlees v. Eidenmuller Enterprises, Inc., 32 F.3d 197, 199 (5th Cir. 1994)(as defendant "employs fewer than fifteen employees, it does not fall within the statutory definition of employer under Title VII" and "[t]hus the district court was correct in holding that it lacked subject matter jurisdiction"); Rogers v. Sugar Tree Products, Inc., 7 F.3d 577, 579 (7th Cir. 1993)("[f]or federal subject matter jurisdiction to exist [over an ADEA claim] the defendant must meet the definition of an employer as Congress set forth"); Podsobinski v. Roizman, 1998 WL 67548, *1 (E.D. Pa. Feb. 13, 1998)(whether defendant employs fifteen persons necessary to be "employer" subject to Title VII is "jurisdictional issue"); Daliessio v. DePuy, Inc., 1998 WL 24330, *1 (E.D. Pa. Jan. 23, 1998); Zarnoski v. Hearst Business Communications, Inc., 1996 WL 11301, *10 (E.D. Pa. Jan. 11, 1996); Shepherdson v. Local Union No. 401, 823 F. Supp. 1245, 1249 (E.D. Pa. 1993).

It is undisputed that, excluding its shareholders, defendant employed less than fifteen employees during the

pertinent period. The issue presented is whether defendant's shareholders are employees for Title VII purposes.

When the factual basis of its jurisdiction is challenged, a court may look beyond the assertions in a plaintiff's complaint to extrinsic evidence without converting the proceeding to one for summary judgment. See Carpet Group Int'l v. Oriental Rug Importers Ass'n, 227 F.3d 62, 69 (3d Cir. 2000); Berardi v. Swanson Mem'l Lodge No. 48, 920 F.2d 198, 200 (3d Cir. 1990). See also Dynamic Image Techs., Inc. v. United States, 221 F.3d 34, 37 (1st Cir. 2001); Zappia Middle East Constr. Co. v. Emirate of Abu Dhabi, 215 F.3d 247, 253 (2d Cir. 2000). The burden is on a plaintiff to prove that jurisdiction exists with appropriate affidavits or other relevant evidence. See Devine v. Stone, Leyton & Gershman, P.C., 100 F.3d 78, 82 (8th Cir. 1996); Berardi, 920 F.2d at 200; Lattanzio v. Security Nat'l Bank, 825 F. Supp. 86, 88 (E.D. Pa. 1993).¹

The court denied defendant's motion without prejudice to renew following a period of jurisdictional discovery. After the close of the allotted discovery period, defendant filed a

¹ On the record presented after discovery on the issue, the result in this case would be the same if the fifteen employee requirement were viewed as an essential element of plaintiffs' claim and defendant's motion were treated as one for summary judgment.

renewed motion to dismiss for lack of subject matter jurisdiction.²

In deciding whether the shareholders of a professional corporation should be considered employees under Title VII, courts in the best reasoned cases have looked beyond the formal organization of the entity and considered all factors relevant to the pertinent relationship and the "economic reality" of the firm's existence and operation. The key consideration is the extent to which a shareholder manages, controls and owns the business. See Devine, 100 F.3d at 81 ("[t]he better reasoned cases hold that the substance of the employment relationship determines whether an individual is an employee under Title VII"); Fountain v. Metcalf, Zima & Co., P.A., 925 F.2d 1398, 1400-01 (11th Cir. 1990)(based on actual role in management and control shareholder in professional corporation was in reality partner and not "employee" for purposes of ADEA); EEOC v. Dowd & Dowd, Ltd., 736 F.2d 1177, 1178 (7th Cir. 1984)("economic reality" of professional corporation indicates it functions like partnership and thus its shareholders are akin to employers rather than employees); Saxon v. Thompson Orthodontics, 71 F.

² Plaintiffs suggest that some requested documents were not produced. It appears, however, that defendant formally objected to these requests and plaintiffs never thereafter filed a motion to compel. Defendant did produce more than 1,300 pages in response to scores of different document requests.

Supp. 2d 1085, 1089 (D. Kan. 1999)("if a shareholder of a professional corporation possessed essential attributes of a 'partner,' then the shareholder, regardless of the chosen corporate form, would not be considered an employee").

The court recognizes that this approach has not been universally accepted. The Second Circuit has declined to look beyond the corporate form to assess whether the owners are de facto partners and thus not employees for purposes of the ADEA. See Hyland v. New Haven Radiology Assocs., P.C., 794 F.2d 793, 798 (2d Cir. 1986). See also Wells v. Clackamas Gastroenterology Assocs., P.C., 271 F.3d 903, 905 (9th Cir. 2001)(following Hyland in ADA case).

The Court in Hyland recognized that partners generally are considered employers and not employees for purposes of the ADEA. See Hyland, 794 F.2d at 797. The same is true for purposes of Title VII. See Hishon v. King & Spaulding, 467 U.S. 69, 79-80 (1984)(Powell, J., concurring); Serapion v. Martinez, 119 F.3d 982, 986 (1st Cir. 1997); Wheeler v. Hurdman, 825 F.2d 257, 263 (10th Cir.), cert. denied, 484 U.S. 986 (1987). The Court in Hyland also recognized that "certain modern partnerships and corporations are practically indistinguishable in structure

and operation," but elected to confine its focus to the de jure form of the organization in question. Hyland, 794 F.2d at 998.³

The court is reluctant to rely on form over substance to treat inconsistently those who are otherwise similarly situated for material purposes. A partner who actually functions as an employee should be counted as one. A shareholder in a professional corporation who contributes capital, participates in all significant management decisions, receives compensation based on profits and essentially functions as a partner is in reality, and should be deemed, an employer and not an employee. See Serapion, 119 F.3d at 988 (stating "form should not be permitted to triumph over substance" and citing with approval Devine for proposition that "a court should not treat either the individual's title or the entity form as determinative" of whether he is employee under Title VII).

Plaintiffs contend that defendant's shareholders should be regarded as employees and not employers under Title VII because they signed employment agreements, had taxes withheld and

³ Interestingly, in a recent opinion the Second Circuit looked beyond the corporate form to actual control in holding that the sole shareholder of a professional corporation was not an "employee" for purposes of the Title VII fifteen employee threshold despite "his performance of traditional employee duties" because of his dominant position in managing the firm. See Drescher v. Shatkin, 280 F.3d 201, 2002 WL 193320 (2d Cir. Feb. 8, 2001). In many professional partnerships, of course, no one partner can unilaterally set firm policy and yet all bona fide partners are deemed to be employees for purposes of Title VII.

participated in an ERISA profit sharing and retirement plan.⁴

Plaintiffs also contend that under the doctrine of spoliation,

⁴ Plaintiffs suggest the same common law agency principles are used to determine whether an individual is an "employee" for IRS, ERISA and Title VII purposes and thus if he is an employee for any purpose, he must be an employee for all purposes. Plaintiffs cite to Nationwide Mutual Ins. Co. v. Darden, 503 U.S. 318 (1992) and this court's opinion in Cox v. Master Lock Co., 815 F. Supp. 844 (E.D. Pa.), aff'd, 14 F.3d 46 (3d Cir. 1993). Darden and Cox involved determinations of whether individuals were employees or independent contractors. See, e.g., In re Watson, 161 F.3d 593, 597 (9th Cir. 1998)(Darden inapplicable to question of whether corporate shareholder was employee as "in Darden the issue involved the distinction between 'employees' and 'independent contractors'"); E.E.O.C. v. Johnson & Higgins, Inc., 91 F.3d 1529, 1538 (2d Cir. 1996)(Darden addressed issue of "whether an individual is an 'employee' or an 'independent contractor'"); Stouch v. Brothers of Order, 836 F. Supp. 1134, 1139 (E.D. Pa. 1993)("[t]he common law test for distinguishing between an employee and an independent contractor was summarized by Darden"). "Cases that distinguish employees from independent contractors are not directly applicable" in determining whether a shareholder in a professional corporation is an employer where the question is not "whether an individual is part of the enterprise" but "whether they manage and own the firm." Devine, 106 F.3d at 81 n.4. The common law principles implicated in such a determination are encompassed by the economic realities test, e.g., participation in management, exposure to liability, participation in profits and losses, voting rights, capital investment, compensation based on profits and similar indicia of ownership. See Simpson, 100 F.3d at 443-44. See also Serapion, 119 F.3d at 986 (declining to rely on "cases deciding whether a particular individual is an employee as opposed to an independent contractor" because "the factors central to that inquiry are inapposite" in deciding whether one is an employer or employee). Plaintiffs conclude that the shareholders are employees under Title VII by assuming they are employees for IRS and ERISA purposes. There has been no legal determination that they are bona fide employees for any purpose. Moreover, one may be considered an employee for tax purposes without necessarily being an employee under Title VII. See id. at 988 n.5. Also, courts have held even sole shareholders, who have the ability completely to control the management and policies of a corporation, may be treated as employees under ERISA plans and receive benefits when others employed by the corporation also participate in the plan. See Gilbert v. Alta Health & Life Ins. Co., 276 F.3d 1292, 1301-02 (11th Cir. 2001); Leckey v. Stefano, 263 F.3d 267, 271-72 (3d Cir. 2001).

they are entitled to an inference that some shareholders did not vote on plaintiff Ziegler's termination from which one may conclude, despite otherwise uncontroverted evidence to the contrary, that some shareholders do not participate in all firm decisions and thus should be considered employees.

While the parties not surprisingly seek to draw different ultimate conclusions from the evidence presented, the pertinent facts are essentially uncontroverted.

Defendant's shareholders share ownership and are accorded equal voting rights in virtually all matters including hiring, termination, offers of partnership and contracting with outside parties. This suggests they are employers. See Devine, 100 F.3d at 81 (shareholders of professional corporation deemed owners for Title VII purposes where they participated in all significant management decisions and set firm policy); Saxon, 71 F. Supp. 2d at 1090 (shareholders who participate in all management decisions and set firm policy are employers); Moebus v. Ob-Gyn Assocs., Inc., 937 F. Supp. 867, 870 (E.D. Mo. 1996)(shareholders who participated in all major decisions not employees for purposes of ADEA).

Each shareholder makes a capital contribution. The compensation of shareholders is not tied to their performance and indeed no shareholder is evaluated or supervised by anyone. Each shareholder but one receives compensation based on defendant's

profits.⁵ This suggests that at least all but one of the shareholders are employers. See Devine, 100 F.3d at 81 (contributions to firm capital and compensation based on profits indicate shareholder is employer); Schmidt v. Ottawa Medical Center, P.C., 155 F. Supp. 2d 919, 922 (N.D. Ill. 2001)(economic reality that shareholder is like partner in partnership supported by fact he shares in profits); Reddy v. Good Samaritan Hosp. and Health Ctr., 137 F. Supp. 2d 948, 979 (S.D. Ohio 2001)(position of shareholder in professional corporation which included "significant management control and a share of the profits" not employee for purposes of Title VII).

Defendant's shareholders are limited to licensed anesthesiologists. See Dowd, 736 F.2d at 1179 (restriction on professional corporations that all shareholders be licensed professionals make them akin to partnerships); Baker v. Berger, 2001 WL 1028394, *4 (N.D. Ill. Sept. 6, 2001)(like partnership, only professionals within relevant profession can be shareholders in professional corporation); Schmidt, 155 F. Supp. 2d at 922. Defendant's shareholders are liable for their acts of professional negligence and for those of persons acting under

⁵ The exception is Dr. Shantz who in 1994 elected to practice for limited hours and receive a fixed salary. The basis of compensation is a sufficiently significant factor that Dr. Shantz could reasonably be found to be an employee. It is undisputed, however, that defendant never had fifteen employees even if Dr. Shantz were counted unless other shareholders are also so counted.

their supervision. See Dowd, 736 F.2d at 1178 (like a partnership, shareholders in professional corporation share malpractice liability).

The shareholders executed "employment agreements" but were referred to as "partners" amongst themselves, within the healthcare community and by office personnel including plaintiffs.⁶

The "employment agreements" do not obviate the manner in which the shareholders actually functioned. See Schmidt, 155 F. Supp. 2d at 922 (rejecting argument that shareholder was employee because he had employment contract when economic reality was that he functioned like partner in partnership). See also Fountain, 925 F.2d at 1401 (stating "the evidentiary value of a label is extremely limited" and concluding use of label "employee" in firm documents did not raise genuine issue of material fact or constitute reasonable basis for drawing inference individual was an employee); Saxon, 71 F. Supp. 2d at 1090 (that defendant characterized shareholders as "employees" in

⁶ Indeed, in her PHRC filing of May 25, 1998 plaintiff DeAngelo stated that the defendant firm had "nineteen partners" and "three employees."

firm documents "simply does not speak to the relevant issue" of "how the business was actually run").⁷

The shareholders also executed a shareholder agreement. There also are different forms of "employment" agreements. Those executed by the shareholders contemplate "substantially full time" engagement in the practice of anesthesiology and provide for compensation as determined by a board comprised of all shareholders. Those executed by others, including plaintiffs, specify a 45-hour work week and provide for a fixed specified annual salary.

That taxes are withheld for shareholders also does not show they were employees. See Baker, 2001 WL 1028394 at *4 (deductions withheld from professional corporation's shareholder's pay and his inclusion on tax wage statements did not make him employee for purposes of Title VII); Saxon, 71 F. Supp. 2d at 1090 (withholding of FICA taxes does not render shareholders employees particularly where their compensation was

⁷ Plaintiffs reference language from a firm employment agreement which describes the responsibilities of the "Employer" to determine the duties assigned to employees as well as employee work hours and to review services performed by employees. It is the shareholders, however, whom plaintiffs seek to label as employees, who carry out these responsibilities of the "Employer."

based on firm profits).⁸ That a shareholder in a professional corporation may receive pension and health benefits under a firm benefit plan also does not make him an employee for purposes of Title VII. See Devine, 100 F.3d at 81; Baker, 2001 WL 1028394 at *4.

Plaintiffs' invocation of the spoliation doctrine is based on the testimony of Robert Falk, then defendant's president, that he did not retain the written list of shareholders contacted in reference to plaintiff Ziegler's termination and how they voted. As noted, plaintiffs contend that this entitles them to an inference that some shareholders did not vote from which one may conclude that some shareholders do not participate in all firm decisions and thus should be considered employees. The spoliation doctrine applies only to the intentional spoliation or destruction of evidence with fraudulent intent and not where destruction was a matter of routine or is otherwise innocently accounted for. See Brewer v. Quaker State Oil Refining Corp., 72 F.3d 326, 334 (3d Cir. 1995).

Dr. Falk testified that it was his practice only to retain vote tallies through the conclusion of the shareholder meeting at which the subject of the vote was discussed. There is

⁸ Plaintiffs argue that "there is no distinction between the shareholder employees and the non-shareholder employees made to the IRS by" defendant. In fact, the individual shareholders and their ownership interests are identified on Schedule E attached to defendant's 1996, 1997 and 1998 federal tax returns.

no competent evidence of record to show he did otherwise. Defendant's minutes confirm that the firm as a routine matter did not maintain a record of how each partner voted on an issue. In any event, Dr. Falk acknowledged that not every shareholder voted but testified that he contacted every shareholder who was available, reached a substantial majority and received no negative votes. Moreover, even accepting plaintiffs' unsubstantiated premise, the fact that one or more of the shareholders have more influence or authority than others would not make the latter employees. See Devine, 100 F.3d at 81 ("[p]articipation rights need not be equal"); Fountain, 925 F.2d at 1401 ("[d]omination by an 'autocratic' partner over others is not uncommon and does not support a finding that the others are employees"); Schmidt, 155 F. Supp. 2d at 922 (that one or more of the shareholders have more influence than others does not support a finding that the others are employees).

It is clear from the record presented that defendant's shareholders manage, control and own the firm. They have a right to participate in firm governance and policy-making. They have made capital contributions and all but one are compensated based on profits. See Serapion, 119 F.3d at 990 ("the critical attributes of proprietary status include three broad overlapping categories: ownership, remuneration and management"). All but Dr. Shantz clearly possess the essential attributes of a partner

and are not employees for purposes of Title VII. See Saxon, 71 F. Supp. 2d at 1089.

When a court lacks jurisdiction over any federal claim, there is no basis for an exercise of supplemental jurisdiction over a related state law claim. See Pryzbowski v. U.S. Healthcare, Inc., 245 F.3d 266, 275 (3d Cir. 2001) (to exercise supplemental jurisdiction over related state claims "the federal claims must have substance sufficient to confer subject matter jurisdiction"); Scarfo, 175 F.3d at 962 ("federal courts of appeals, however, have uniformly held that once the district court determines that subject matter jurisdiction over a plaintiff's federal claims does not exist [it] must dismiss a plaintiff's state law claims" and thus upon determination that defendant was not an "employer" under Title VII and dismissal of Title VII claim, court must dismiss related state law claims); Gill v. Upson Regional Medical Center, 1 F. Supp. 2d 1480, 1481 (M.D. Ga. 1998) (as court lacked jurisdiction over plaintiff's ADA claim, there was no basis for exercise of supplemental jurisdiction over related state law claims); Jordahl v. Democratic Party of Virginia, 947 F. Supp. 236, 242 (W.D. Va. 1996) (when federal claims are dismissed for lack of

jurisdiction, there is no basis for exercise of supplemental jurisdiction).⁹

Accordingly, defendant's motion will be granted. Plaintiffs, however, may pursue relief under their parallel state law claims. The time this action was pending is tolled for purposes of the limitations period pursuant to 42 Pa. C.S.A. § 5103(b)(1) and plaintiffs' PHRA claims may be pursued upon prompt compliance with § 5103(b)(2). See Ferrari v. Antonacci, 689 A.2d 320, 322-23 (Pa. Super.), app. denied, 698 A.2d 594 (Pa. 1997); Davis v. Commonwealth, 660 A.2d 157, 161-62 (Pa. Commw. 1995).¹⁰

An appropriate order will be entered.

⁹ In any event, when all federal claims are eliminated before trial federal courts routinely decline to exercise supplemental jurisdiction over any state law claims absent considerations not present in the instant case. See Sullivan v. Conway, 157 F.3d 1092, 1095 (7th Cir. 1998); McClelland v. Gronwaldt, 155 F.3d 507, 520 (5th Cir. 1998); Borough of W. Mifflin v. Lancaster, 45 F.3d 780, 788 (3d Cir. 1995); Lovell Mfg. v. Export-Import Bank of the U.S., 843 F.2d 725, 734 (3d Cir. 1988); Burke v. Mahanoy City, 40 F. Supp. 2d 274, 287 (E.D. Pa. 1999); Johnson v. Cullen, 925 F. Supp. 244, 242 (D. Del. 1996); Litz v. City of Allentown, 896 F. Supp. 1401, 1414 (E.D. Pa. 1995); Renz v. Shreiber, 832 F. Supp. 766, 782 (D.N.J. 1993); 13B Charles Alan Wright et al., Federal Practice and Procedure § 3567.2 (1984).

¹⁰ See also 28 U.S.C. § 1367(d)(tolling limitations period for supplemental claims). But see Raygor v. Regents of the University of Minnesota, __ U.S. __, 2002 U.S. LEXIS 1375, *27 (Feb. 27, 2002)(holding provision does not toll limitations period for claims against states on which sovereign immunity has not been waived while explicitly declining to express any view "on the application or constitutionality of § 1367(d) ... when a defendant is not a State).

