UPDATE ON COVENANTS NOT TO COMPETE: WILL THEY SURVIVE IN THE HEALTHCARE INDUSTRY?

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I. Introduction

Covenants not to compete undergo considerable scrutiny in all industries. In healthcare, however, proponents of covenants not to compete must argue for enforcement of the covenant against the countervailing weight of the rights of patients to be treated by their own physicians at the hospitals of their choice, as well as the community need for the type of medical service the physician provides. It has been argued that the public interest in supporting those hospitals willing to make a financial commitment to establish a medical specialty practice is given little consideration in many recent cases, where courts have voided the covenant not to compete. Courts around the country are starting to internalize this point of view, and increasingly are balancing the equities of the particular facts and circumstances to determine whether the restrictive covenant should be upheld.

II. Restrictive Covenants In General

A. Historically, plagues like the Black Death decimated much of the skilled labor force in Europe. With virtually no labor force in place, it is understandable that the earliest cases in 14th Century England found covenants not to compete void as against public policy due to the restraint of trade.[1] Similarly, in 17th Century England, the custom of the Crown granting exclusive trading privileges fostered a public dislike of all restraints upon free trade. In the 18th Century, however, England found itself in a new commercial era. In this setting, the courts began to enforce common law contracts in partial restraint of trade, provided they were ancillary to the principal transaction and reasonable with regard to geographic scope and duration.[2]

B. Restrictive covenants found in clauses of partnership or employment agreements generally limit a contracting party after termination of the contract from performing similar work for a specified and reasonable period of time and within a certain reasonable geographic region.[3]

C. A restrictive covenant is enforceable if the restraint is reasonable under the facts and circumstances of the particular case. Generally, the reasonableness of a restrictive covenant in a contract for employment is determined by considering the effects of the restriction upon the parties, the presence and extent of geographical and time limitations as well as the scope of activities with respect to which the employee may not compete.[4]

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[1] Morgan's Home Equipment Corp. v. Martucci, 390 Pa. 618, 136 A.2d 838 (1957); *See also,* Derek W. Loeser, *The Legal, Ethical, and Practical Implications of Noncompetition Clauses: What Physicians Should Know Before They Sign*, 31 J.L. Med. & Ethics 283 (2003).

[2] *Id.*

[3] Black's Law Dictionary (6th Edition).

[4] Ferdinand S. Tinio, *Validity And Construction Of Contractual Restrictions On Right Of Medical Practitioner To Practice, Incident To Employment Agreement*, 62 A.L.R.3d 1014 (Updated July 2005.)

D. However, when reviewing the reasonableness of a restrictive covenant in the contract of employment of a medical practitioner, the courts have also inquired whether the covenant would have an injurious effect on the public.[5] Of particular concern to the courts is the public's right to freedom of choice among physicians, the right to continue an ongoing relationship with a physician and the benefits derived from having an increased number of physicians in any given community.[6] These public policy considerations are playing an increasingly larger role in courts' determinations of the enforceability of medical practitioners' agreements not to compete.

E. Restrictive covenants are generally of two types and are used to safeguard the business interests of the employer from disclosure and competition.

1. **Non-disclosure restrictive covenants** limit the dissemination of an employer's confidential business information by the former employee. The information may consist of trade secrets, inventions, confidential business practices, financial terms, price lists (patient lists), formulas, marketing strategies, etc. that are unique to the employer's business.[7]

a. The Pennsylvania Supreme Court has made clear that even in the absence of a non-disclosure restrictive covenant in an agreement, the disclosure of trade secrets, including confidential customer lists, is to be protected. The customer lists and customer information that have been compiled by such firms represent a material investment of an employer's time and money. This information is highly confidential and constitutes a valuable asset. Such data has been held to be in the nature of a "trade secret" for which an employer is entitled to protection, independent of a nondisclosure contract, either under the law of agency or under the law of unfair trade practices. The presence of a nondisclosure covenant does not create the right to protection, but rather serves as evidence of the confidential nature of the data.[8]

b. Non-disclosure covenants are not subject to the "reasonableness" requirement that often curtails the enforcement of non-compete restrictive covenants.

2. **Non-competition restrictive covenants** typically prohibit competition by a former employee for a specified period of time within a designated geographical area. This covenant may be used to prevent the employee from exploiting customer contacts (patients) established during employment or to prevent the employee from working for a competitor or setting up the employee's own business.[9]

a. Generally, covenants not to compete made ancillary to a sale of a business serve a more useful economic purpose as compared to a restriction on competition that is ancillary to an employment agreement. The covenant in an agreement of sale will protect the

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[5] *Id*.
[6] *See e.g.,* Murfreesboro Med. Clinic, PA. v. Udom, 166 S.W.3d 674 (Tenn. 2005)
[7] Kurt H. Decker, *Refining Pennsylvania's Standard for Invalidating a Non-Competition Restrictive Covenant When an Employee's Termination is Unrelated to the Employer's Protectible Business Interest,* 104 Dick L. Rev.619 (Summer, 2000).
[8] *Id*., *See* Morgan's Home Equipment Corp., *supra*, note 1.
[9] *Id*.

goodwill asset that the purchaser has bought. Many times it is this particular asset that is the inducement for the sale, particularly when there are no definable trade secrets. If the seller were free to initiate competition directly upon the conclusion of the sale, the buyer would be holding the "proverbial empty poke."[10]

b. The value in a non-compete covenant that is ancillary to an employment agreement is the ability to prevent competition from a former employee who was provided special training and skills or learned a carefully guarded method of doing business which are the trade secrets of a particular enterprise and the former employer. Non- compete covenants are enforced by the courts as reasonably necessary for the protection of the employer.[11]

c. Because a non-compete covenant serves as a partial restraint on trade, the courts will construe them strictly. Courts will balance what is reasonably necessary for the protection of the employer against the undue hardship on the employee to determine whether the covenant is more of a penalty for termination of employment than it is an employer-protection device.[12]

III. Constitutional/Statutory Covenants Not To Compete

A. Based upon the historical rejection of restraints on trade, some states have opted to regulate covenants not to compete through legislation. Generally, these state statutes are based on five approaches:

1. The District of Columbia has chosen to ban covenants not to compete altogether. State statutes that declare covenants not to compete void usually contain broad language. For instance, the District of Columbia's legislature passed a statute that "every combination in the form of a trust or otherwise, or conspiracy in restraint of trade or commerce all or any part of which is within the District of Columbia is declared illegal."[13]

2. Other states have declared covenants not to compete void as a matter of public policy but have provided exceptions to the rule for the sale of the good will of a business, disassociation of a partner from a partnership, or upon dissolution of a partnership or limited liability company so long as the purchaser of the business or remaining partners carry on a like business.[14] However, many of these agreements limit the covenant not to compete to a specified geographic area such as the county, city where the principal office of the business is located or a contiguous county.[15]

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[10] *Id.*
[11] *Id.*
[12] *See* Albee Homes, Inc. v. Caddie Homes, Inc., 417 Pa. 177, 207 A.2d 768 (1965).
[13] D.C. Code §28-4502.
[14] Alabama, California, Hawaii, North Dakota, Montana and Oklahoma have adopted this rule. *See* attached chart for statutory citations. Note, Oklahoma also provides that an employee may be contractually prohibited from soliciting established customers of a former employer. 15 Okla. Stat. §219A.
[15] *See, e.g.* Mont. Code Ann. §§28-2-703 and 704.

3. Certain states permit covenants not to compete but legislate the terms of the agreements.[16] For instance, in South Dakota covenants not to compete cannot exceed two years and are limited to a specified county, first or second class municipality or any part thereof.[17]

4. Other states expressly permit covenants not to compete if they are reasonable.[18] The standard for reasonableness is generally determined by a court after review of all the facts and circumstances.[19] Oregon also requires that "the services performed by the employee pursuant to the agreement include substantial involvement in management of the employer's business, personal contact with customers, knowledge of customer requirements related to the employer's business or knowledge of trade secrets or other proprietary information of the employer." [20]

5. A handful of states expressly regulate physician non-compete agreements either declaring them void or requiring them to comply with certain restrictions.[21]

a. Delaware and Colorado ban covenants not to compete in physician contracts but permit a former employer to sue for monetary damages related to competition.[22] These limitations apply only to a physician's ability to practice medicine and therefore may not apply to employment which does not include the practice of medicine, such as a medical directorship without attendant duties or a medical consultant.

b. Massachusetts expressly declares void any covenant not to compete in a physician contract and does not provide for damages.[23]

c. Texas permits the enforcement of non-compete clauses against physicians as long as the covenant:

i. Does not deny the physician access to a list of his patients who he had seen or treated within one year of termination of the contract or employment;

ii. Provides access to medical records of the physician's patients upon authorization of the patient and any copies of

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[16] This approach is adopted by Florida, Louisiana and South Dakota. *See* attached chart for statutory citations.
[17] S.D. Codified Laws § 53-9-11.
[18] Missouri, Nevada, Oregon and Wisconsin laws expressly permit reasonable covenants not to compete. *See* attached chart for statutory citations.
[19] *See, e.g.* Silvers, Asher, Sher & McLaren, M.D.s Neurology, .P.C. v. Batchu, 16 S.W.3d 340 (Mo. Ct. App. 2000) (holding that it was reasonable to limit a neurologist from practicing within 75 miles of his previous practice for a period of two years.)
[20] Or. Rev. Stat. §653.295.
[21] Delaware, Colorado, Massachusetts and Texas have all adopted laws governing non-compete agreements entered into by physicians. *See* attached chart for statutory citations.
[22] *See* 6 Del. Code. Ann. § 2707 and Colo. Rev. Stat. § 8-2-113.
[23] Mass. Gen. Law. Ch. 112, §12X. *See, also,* Falmouth Ob-Gyn Assocs v. Abisla, 417 Mass. 176, 629 N.E.2d 291 (1994).

medical records for a reasonable fee as established by the Texas State Board of Medical Examiners;

iii. Provide that any access to a list of patients or to patients' medical records after termination of the contract or employment be in the format in which such records are maintained, unless otherwise agreed by the parties;

iv. Provide for a buyout of the covenant by the physician at a reasonable price or as determined by an arbitrator; and

v. Provide that the physician will not be prohibited from providing continuing care and treatment to a specific patient or patients during the course of an acute illness, even after employment has been terminated.[24]

B. In Georgia, covenants not to compete are constitutionally void based on the Georgia state constitution.[25]

IV. Covenants Not To Compete Under Common Law

A. Because the law values free mobility of employees and free competition, non-competition agreements are looked on by the courts with disfavor in most jurisdictions.[26] The reasons for this include: 1) a desire not to interfere with an individual's ability to earn a livelihood; 2) the conflict between these types of covenants and notions of free economy; and 3) a desire not to give undue protection to an employer who happened to establish a business first.[27]

B. Generally, a valid agreement not to compete must be ancillary to another agreement and cannot be entered into for the sole purpose of restricting competition. As with any other contract, it must be supported by adequate consideration.[28]

1. An offer of continued employment, with the condition that the employee sign a restrictive covenant, may constitute adequate consideration where there is a preexisting contract of employment terminable at will by either party.[29]

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[24] Tex. Bus. & Com. Code §§15.50-.52. *See also* Mahmood v. Fanasch, 2005 Tex. App. LEXIS 9632 (holding that a covenant not to compete was unenforceable for failure to comply with Tex. Bus. & Com. Code. Ann. § 15.50).
[25] *See* Ga. Const. Art. III, § VI, Par. V(c)1.
[26] *See, e.g.*, Freiburger v. J-U-B Engineers, Inc., 111 P.3d 100, 104 (Idaho 2005); Sentilles Optical Servs. v. Phillips, 651 So.2d 395 (La. App. 2d Cir. 1995); Faces Boutique, Ltd. v. Gibbs, 318 S.C. 39 (S.C. App. 1995); Briskin v. All Seasons Service, Inc., 206 A.D.2d 906 (Dep't 1994); Creative Entertainment Inc. v. Lorenz, 638 N.E.2d 217 (Ill. App. 1st dist. 1994).
[27] *See, e.g.*, Chrysalis Health Care, Inc. v. Brooks, 640 N.E. 2d 915 (Ohio Mun. 1994); Laidlaw Inc. v. Student Transp. Of America, Inc., 20 F. Supp.2d 727 (D.N.J. 1998); Nigra v. Young Broadcasting, 177 Misc. 2d 664 (Supreme Court New York City 1998).
[28] Special Prods. Mfg. Inc. v. Douglass, 159 A.D.2d 847 (N.Y. App. Div. 1991).
[29] *See* Davis & Warde, Inc. v. Tripoli, Pa. Super. 450, 616 A.2d 1384 (1992).

2. An annual raise, if given routinely at a certain percentage level, will not be sufficient consideration for a covenant not to compete, but rather could be considered a bonus.[30] However, one court has ruled that a $1,000.00 bonus alone is not sufficient consideration.[31]

3. Changing an employee from part-time to full time, providing a fixed term contract over at-will employment, promotions, and raises unrelated to yearly increases, increases in benefits all appear to be acceptable consideration. Most acceptable as "adequate consideration" seems to be the offer of multiple benefits.[32]

C. Courts will enforce a restrictive covenant only if it is reasonable and protects an employer's legitimate business interest. Factors considered include:

1. Does the employer have a legitimate business interest in being protected from the competition of the employee?

2. Is the agreement reasonable in light of all of the circumstances?

3. Is the agreement reasonably limited in time and geography?

4. Will enforcement of the agreement prove harmful or unduly burdensome to the public?[33]

5. Courts may consider additional factors such as:

   a. The employee's ability and intent to compete;

   b. The employee's relationships and contacts with those who have expertise in the business; and

   c. The employee's relationships and contacts with customers.

D. Absent the consent of the employee or an express assignability clause in the employment contract, a restrictive covenant is not assignable.[34]

E. Reasonableness of time, geographic scope, and activity - A restrictive covenant will not always be enforced even though it is designed to prevent the loss of an employer's protectible business interest and is supported by adequate consideration. The courts will examine a restrictive covenant to see if the restrictions are not overly broad in protecting a

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[30] *See* Gregory Jordan and Mary Hackett, *Non-Compete Agreements and Considerations - What's an Employer to Do?* The Pennsylvania Bar Quarterly, April 1996, pp. 76-79.

[31] *See* Kramer v. Robec, Inc., 824 F. Supp. 508 (E.D. PA. 1992).

[32] *Id*., *See* Jordan and Hackett, *supra* note 30.

[33] *See e.g.*, Hayes v. MSP Communications, 1998 WL 188567 (Minn App. 1998); In-Flight Newspapers, Inc. v. Magazines In-Flight LLC, 990 F. Supp. 119 (E.D.N.Y 1997); HPD, Inc. v. Ryan, 227 A.D.2d 448 (App. Div. Dep't 1996); Platinum Management, Inc. v. Dahms, 666 A.2d 1028 (N.J. Super. Ct. Law. Div. 1995); Seymour v. Buckley, 628 So.2d 554 (Ala. 1993).

[34] *See* All-Pak Inc. v. Johnston, 694 A.2d 347 (Pa. Super. 1997).

legitimate business interest, not overly burdensome to the employee and not injurious to the public.

1. Courts will sometimes reform an overbroad covenant in order to protect the legitimate business interests of the employer, the courts will refuse to do so when the restrictive covenant indicates intent to oppress the employee or establish a monopoly. For example, when a covenant did not contain any restrictions on geographic limitation or on the type of employment or activity prohibited, and prohibited the employee from being employed by anyone other than the employer during a three year period from the date of the contract, the court found that the covenant in effect enslaved the employee for three years and would not be enforced by the court.[35]

2. Reasonable time and geographic limits are highly fact-specific inquiries for the court, not amenable to uniform guidelines. The challenger has the burden to demonstrate unreasonableness.

a. The geographic extent of a restraint should be designed to protect the employer's interest in the customer relationships developed by an employee whose contact with customers occurred at the customer's premises extends no further than the sales territory to which the employee was assigned. Where a covenant imposes restrictions broader than necessary to protect the employer, the court may grant enforcement limited to those portions of the restrictions that are necessary for the protection of the employer.[36]

3. The court has found the geographic extent of a restrictive covenant that is the United States is reasonable, when the company distributes computers throughout the nation and overseas, acknowledging that competition in the computer market is worldwide.[37] However, the court found that the three years' ban on competition was longer than necessary to protect a computer company's interest, reasoning that the shelf life of computers and computer products is 12 to 18 months. Therefore, the court limited the covenant's duration to two years.[38]

V. Restrictive Covenants in the Medical Profession

A. Several jurisdictions have held that medical providers have a legitimate business interest in protecting their patient base.

1. Medical practices, particularly those providing specialized care, generally have an interest to be protected in their sources of referral.[39] Moreover, a medical practice's

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[35] *See* In re: Daniel G. Monaghan, 141 B.R. 80 (E. D. Pa., 1992).
[36] *Id*., *See also* Wellspan Health, *supra* note 40.
[37] *Id*., *See* Kramer, *supra* note 31.
[38] *Id*.
[39] Valley Med. Specialists, Inc. v. Farber, 982 P.2d 1277, 1284 (Ariz. 1999); Medical Specialists, Inc. v. Sleweon, 652 N.E.2d 517, 523 (Ind. Ct. App. 1995); Weber v. Tillman, 913 P.2d 84, 91 (Kan. 1996); Ballesteros v. Johnson, 812 S.W.2d 217, 223 (Mo. Ct. App. 1991).

patient referral base is a protected interest and the investment required to develop such a base is protectible.[40]

2. In addition, a medical practice itself is a legitimate business interest an employer may protect.[41]

B. All jurisdictions may not uphold restrictive covenants in physician agreements. Generally non-competition provisions in physician agreements are challenged on the basis of reasonableness. Of course, what is reasonable may differ from the perspective of the employer versus that of the employee. Many cases discuss the factors that go into a determination of whether or not the proposed restrictions are reasonable. *See, e.g., Community Hospital Group, Inc. v. More* at Note 58 for an interesting discussion of these factors.

C. Whether the non-competition provisions of a physician's contract are reasonable or not is tested under various standards, depending upon the jurisdiction.

1. One line of authority applies a heightened scrutiny to already disfavored non-compete provisions in the medical setting because these provisions are not considered to be in the public interest.[42]

2. Other jurisdictions continue to apply the same standards applicable in the ordinary commercial context to non-competition agreements between physicians, and do not consider the difference between the doctor-patient relationship and ordinary commercial producer-customer relationships.[43]

D. A non-competition clause in a physician's contract must also be considered reasonable in its geographic and time limitations.

1. An Indiana court held that a covenant not to compete that sought to restrict an ophthalmologist's ability to practice all aspects of medicine or surgery was overly broad because the former employer's business was limited to ophthalmology services. Thus, the former employer had no legitimate business interest in the medical services provided by its former employee, as the employer did not offer anything but ophthalmology.[44]

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[40] Wellspan Health v. Bayliss, 869 A.2d 990 (Pa Super 2005).

[41] *See* Weber, *supra* note 39 at 92; *See also* Retina Services, LTD. v. Garoon, 538 N.E. 2d 651 (Ill. App. Ct. 1989). But note that other courts have held that experience and skill gained by the employee during his employment cannot, by itself, justify a non-compete provision in a physician's contract – there must be something about the employment that gives the employee an unfair advantage. Fields Found, Ltd. v. Christensen, 309 N.W. 2d 125 (Wis Ct. App. 1981).

[42] *See* Ohio Urology, Inc. v. Poll, 594 N.E.2d 1027, 1031 (Ohio Ct. App. 1991) (Ordinary disfavor with which non-compete agreements are viewed is "especially acute" when considering reasonableness of non-compete agreements between physicians.)

[43] *See, e.g.,* Raymundo v. Hammond Clinic Ass'n, 449 N.E.2d 276 (Ind. 1983); Rash v. Toccoa Clinic Med. Assocs., 320 S.E.2d 170 (Ga. 1984); Duneland Emergency Physician Med. Grp. v. Brunk, 723 N.E. 2d 963 (Ind. Ct. App. 2000); Gant v. Hygeia Facilities Found. Inc., 384 S.E. 2d 842 (W.Va. 1989).

[44] Intermountain Eye and Laser Centers, P.L.L.C. v. Miller, 2005 Ida. LEXIS 187 (2005).

2. An Illinois court reached a different conclusion and upheld a restrictive covenant limiting a physician's ability to practice medicine.[45] The court reasoned that the employee doctors were licensed to practice in other areas of medicine outside of their specialties, so, in addition to the practice of their specialties, their general practice of medicine could injure the employer. Given this factual determination, the prohibition of the practice of medicine in general was not a greater restraint than necessary to protect the employer.

VI. Public Policy Considerations Related To Physician Non-Competition Agreements

A. The United States Supreme Court has been increasingly harsh toward anticompetitive practices in the learned professions.[46] One of the factors to be considered in reviewing the issuance of an injunction enforcing an anticompetitive employment covenant is the effect of the action upon the interests of society as a whole.

B. Where a restrictive covenant seeks to limit the professional practice of a health care provider, the court will scrutinize the effect of the resulting loss of similar professional health care services on the public interest. Courts have stated that the effect upon the consumer in need of medical care may trump the rights of the parties to the contract. If the result of the equitable relief sought would deprive the community of a desperately needed medical service, the relief will not be granted.[47] This represents the traditional view.

C. The traditional view was that restrictions in a covenant must not extend beyond what is reasonably necessary to protect the interests of the employer, must not be unnecessarily injurious to the interests of the employee, and must not unduly interfere with the interests of the public.[48] Thus, an Idaho court stated that restrictive covenants in physician agreements are not against public policy, and any detriment to the public interest in the possible loss of the services of the physician is more than offset by the public benefit arising out of the preservation of the freedom to contract.[49]

D. More and more courts have begun to view the public interest impact of a restrictive covenant in a physician's agreement as a critical factor. This approach seems to stem from the acknowledgement that non-compete provisions between physicians and their employers implicate public policy concerns not present in the ordinary commercial context.[50] In fact some jurisdictions recognize that the doctor-patient relationship cannot be easily or accurately compared to relationships in the commercial context.[51]

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[45] Mohanty v. St. John's Heart Clinic, S.C., 832 N.E. 2d 940 (Ill. App.2d 2005).

[46] *See, e.g.*, National Society of Professional Engineers v. United States, 435 U.S. 679, 98 S.Ct. 1355, 55 L.Ed.2d 637 (1978); Bates v. State Bar of Arizona, 433 U.S. 350, 97 S.CT.2691, 53 L.Ed.2d 810 (1977); Virginia State Board of Pharmacy v. Virginia Consumers Council, 425 U.S. 748, 96 S.Ct. 1817,48 L.Ed. 346 (1976); Goldfarb v. Virginia State Bar, 421 U.S. 773, 95 S.Ct. 2004, 44 L.Ed.2d 572 (1975).

[47] *Id*., *See* New Castle Orthopedics, *supra* note 52.

[48] *See* Tinio, *supra* note 4.

[49] Marshall v. Covington, 339 P.2d 504 (Idaho 1959).

[50] *See*, Intermountain Eye and Laser Centers, P.L.L.C., *supra* note 44.

[51] *See* Valley Med. Specialists, *supra* note 39.

E. Traditionally, courts have denied the enforcement of restrictive covenants if they were deemed harmful or injurious to the public. This may occur where a community's supply of doctors would be adversely impacted if the covenant were enforced.[52] In 2005, several courts were asked to decide whether non-competition provisions in physician agreements were per se void against public policy.

1. Recently, a Tennessee court ruled that non-competition provisions in a physician contract violated public policy and were void.[53] The court found that the public's right to freedom to choose its own physicians, the right to continue an on-going relationship with a physician, and the benefits derived from having an increased number of physicians practicing in any given community all outweigh the business interests of an employer.[54] The court found persuasive the fact that the Tennessee Legislature expressly permitted restrictive covenants among physicians employed by a hospital or a medical faculty plan but did not choose to extend such rights to private medical practices.[55] This was based on the court's view that the right of an individual to choose his/her own physician is so fundamental that the court cannot allow it to be denied because of an employer's restrictive covenant.[56]

a. On the other hand, courts have refuted physicians' assertions that any evaluation of public interest must include," a patient's right to choose a health care provider, to maintain a continuous relationship with that healthcare provider, and to receive the best medical services available without forfeiting that relationship," and must override the interests of the hospital employer. In a Pennsylvania case, the appellate court enforced a non-competition agreement against the physician and found that no jurisdiction has recognized a public interest in assuring the unrestricted ability of a particular patient to maintain continuity of care with a particular physician. The court rested its decision on the fact that there was no documented shortage of oncologists in the geographic area, and the record demonstrated that the departure of the oncologist in this matter did signal a loss of business opportunity and market advantage for the employer.[57]

2. The New Jersey Supreme Court has declined to declare restrictive covenants among physicians unenforceable per se. Instead, it has chosen to continue the case-by-case approach of evaluating the reasonableness of each specific agreement. This past year, the Court opted to retain the twenty-five year old *Solari* test to determine the validity of physician non-competition agreements. The *Solari* test emphasizes public interest concerns over parochial or private interests, and has been applied expansively in the case of *Karlin v. Weinberg*.[58] The

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[52] *See* New Castle Orthopedic Assn. v. Burns, 481 Pa. 460, 392 A.2d 1383 (1978).

[53] *See* Murfreesboro Med. Clinic, PA. *supra* note 6 (holding that such agreements are against the public interest and are therefore unenforceable as a matter of law).

[54] *Id*.

[55] *Id.*

[56] *Id.*

[57] *See* West Penn Specialty MSO, Inc. and Medical Center Clinic, P.C. v. Teresa Nolan, M.D., 1999 Pa. Super. 218, 737 A.2d 295 (1999).

[58] Community. Hosp. Group, Inc. v. More, 181 N.J. 36; 869 A.2d 884; 2005 N.J. LEXIS 299 (2005); Karlin v. Weinberg, 390 A.2d 1161 (N.J. 1978).

Court held that there was no need to declare physician non-competition agreements void per se. Using the *Solari* test, the Court analyzed:

a. Whether the covenant in question protects legitimate interests of the employer (in this case, a hospital), which may include:

(1) protecting confidential business information, including patient lists; (2) protecting patients and patient referral bases; and (3) protecting investment in the training of a physician.

b. Whether the covenant imposes undue hardship on the employee:

This inquiry requires the court to determine the likelihood of the employee finding other work in his or her field, and the burden the restriction places on the employee. In applying this part of the test, the reason for the termination of the parties' relationship is also relevant. If the employee terminates the relationship, the court is less likely to find undue hardship as the employee put himself or herself in the position of bringing the restriction into play. Where the employer causes the parties to separate, enforcement of the covenant may cause hardship on the employee, which may fairly be characterized as undue in that the employee has not, by his conduct, contributed to it.

c. Whether the restrictive covenant is injurious to the public.

Significant to this issue is the demand for services rendered by the employee, and the likelihood that those services could be provided by other physicians already practicing in the area. If enforcement of the covenant would result in a shortage of physicians within the area in question, then the court must determine whether this shortage would be alleviated by new physicians establishing practices in the area. The court also should examine the degree to which enforcement of the covenant would foreclose resort to the services of the "departing" physician by those of his patients who might otherwise desire to seek him out at his new location. If the geographical dimensions of the covenant make it impossible, as a practical matter, for existing patients to continue treatment, then the trial court should consider the advisability of restricting the covenant's geographical scope, in light of the number of patients who would be affected.

3. Also in 2005, a Pennsylvania court held that restrictive covenants in physician agreements are not per se unreasonable or unenforceable.[59] Under Pennsylvania law,

[59] *See* Wellspan, *supra* note 40.

the court applies a balancing test, first looking at the employer's legitimate business interest, and then at the employee's interest in earning a living. Subsequently, the court will balance the employer/employee interests with the interests of the public.

4. The public interest analysis of non-competition covenants involving physicians requires a determination of the number of physicians practicing in the restricted area. When patient demand in the geographic region in question exceeds the ability of appropriately trained physicians to provide expeditious treatment, then the public interest predominates over the right to enforce a covenant not to compete.

F. One of the interesting questions raised by these cases is whether the public interest analysis is limited to the impact of the restrictive covenant on the patients of the particular physician defendant, or whether the interest of all patients in the restricted geographic area is of importance. As noted by some commentators, the interest of the general patient population in a particular geographic area may be better served by enforcement of the covenant, as this may provide incentives and benefits to hospitals, and these incentives may provide broader benefit to the patient public as a whole.[60]

VII. Physician Non-Competes in Telemedicine

A. As medical practices increase their geographic range by the use of telemedicine services,[61] courts may find it increasingly difficult to justify enforcement of physician non-competes. This is because the geographic reach of telemedicine services is expansive. Many of these services are provided by satellite, and could be available worldwide. Thus, one must query whether a court would enforce a worldwide covenant not to compete, and if so, for what length of time?

B. Courts increasingly are struggling with public policy considerations such as the right to continue an on-going relationship with a physician, and the benefits derived from having an increased number of physicians and/or particular specialists practicing in any given community. Telemedicine directly impacts these public policy considerations by providing medical services and expertise to underserved areas. At the same time, patients often do not have a direct relationship with a particular physician (in fact, they may never meet the physician or know his or her name). Thus, this interest, which is of paramount importance in analysis of the normal medical restrictive covenant, is not present with the provision of services via telemedicine. Conversely, the employer's legitimate business interest in having a certain number of physicians available to render medical services via telemetry does seem to be strong in this situation.

C. While this author has found no cases directly on point in the medical field, non-competition provisions which limit a physician's ability to provide telemedicine services may be

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[60] Michael M. Mustokoff and Amanda M. Leadbetter, *Hospitals, their Physicians and Their Non-Competes: Breaking Up-Should be Hard to Do,* 8 Health Lawyers News 26 (2004).

[61] Telemedicine is a broad term the incorporates a variety of services but it generally involves telephonic, video, or computer aided methods of providing medical support or education to locations throughout the United States. *See* Bradley v. Mayo Foundation, 1999 U.S. Dist. LEXIS 17505 (E.D. Ky. 1999).

challenged as overly broad in geographic scope and time limitations, and against public policy. New York courts provide some guidance in the situation where a covenant not to compete affects an employee in an internet-based position.[62]

VIII. Enforcement Requirements for Restrictive Covenants

A. A court sitting in equity may enjoin a breach of contract (including a breach of a restrictive covenant contained in an employment agreement) where money damages are an inadequate remedy.[63] Plaintiff must show immediate and irreparable harm that damages cannot compensate in order to establish the requisite elements for injunctive relief. Since a preliminary injunction is similar to a judgment and execution before trial, it will only issue where there is an urgent necessity to avoid injury, which cannot be compensated by money damages. An injunction usually is not granted unless greater harm will be done by its denial than by its grant,[64] and it is possible to restore the parties to the status quo, as it existed immediately prior to the alleged wrongful conduct.[65]

B. At least one court has said that it is not the initial breach of a covenant that establishes the existence of irreparable harm, but rather threat of unbridled continuation of the violation and the resultant incalculable damage to the former employer's business that constitutes justification for equitable intervention.[66]

IX. Challenges To Covenants Not To Compete

A. **Waiver** is a defense often raised to the enforcement of a non-compete agreement. The argument is that the former employer has not enforced the non-compete agreement in the past against other employees, and has waived its enforceability. The success of this defense is fact specific. It will depend largely on the number and timing of the past instances of failing to enforce the non-compete and whether the other employees had the same type of job as the employee at issue.

B. **The Unclean Hands Doctrine** stands for the proposition that a court in equity will not aid a party who resorts to unjust and unfair conduct. A Connecticut court refused to enforce non-competition provisions against a physician, at least in part due to the fact that the plaintiff medical practice had unclean hands.[67] The court found that for a period of four years, the practice manager failed to inform the defendant doctor of her right to participate in the medical practice retirement plan. Consequently the plan discriminated in favor of the physician practice manager, a highly compensated employee. Thus, the court held that the plaintiff came to court with unclean hands and could not prevail in its action to enforce the non-compete clause against defendant physician.

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[62] Earthweb, Inc. v. Schlack, 71 F. Supp.2d 299 (S.D. NY 1999), *aff'd* 2000 U.S. App. LEXIS 11446 (2d Cir. 2000).
[63] *Id*., *See* Concord Orthopedics Prof. Ass'n v. Forbes, 702 A.2d 1273 (NH 1997).
[64] See Herman v. Dixon, 393 Pa. 33,141 A.2d 576 (1958).
[65] *Id*., *See* New Castle Orthopedic Assn., *supra* note 52.
[66] *Id*., *See* Concord Orthopedics Prof. Ass'n, *supra* note 63.
[67] Paradis v. Pinou, 1997 Conn. Super. LEXIS 1111 (1997).

C. Prior Material Breach may also be raised as a defense to the enforcement of a non-compete clause. The key factor with respect to this defense is whether a prior breach of the agreement is material. The materiality of the breach is usually a question of fact.[68]

1. Among the significant circumstances that guide the finder of fact in determining materiality are:

a. The extent to which the injured party will be deprived of a reasonably expected benefit;
b. The extent to which the injured party can be compensated for the part of that deprived benefit;
c. The extent to which the party failing to perform will suffer forfeiture;
d. The likelihood that the party failing to perform will cure the failure; and
e. The extent to which the behavior of the party failing to perform comports with the standards of good faith and fair dealing.[69]

2. A Missouri appellate court refused to enforce a non-compete clause against a defendant physician because it found that the plaintiff employer had violated its duty of good faith and fair dealing. After the employer and physician could not agree on new contract terms before the expiration of an existing contract, the employer cancelled all of the physician's scheduled duties and notified all of his patients that he would no longer be practicing in the area. The court found that this conduct violated the duty of good faith and fair dealing because both parties had a duty to cooperate to obtain the benefits they both reasonably expected.

3. An Illinois court refused to uphold a covenant not to compete against two defendant physicians due to a material breach of the medical group's partnership agreement.[70] The court found that, along with other breaches of the partnership agreement, the plaintiff medical group conducted secret meetings and fired the chief executive officer without a meeting of the executive committee. The court held that these breaches were material, and defendant physicians' obligations under the covenant not to compete were discharged.

D. Lack of Consideration is an important defense to the enforcement of a covenant not to compete. Courts will not enforce a non-compete clause for which there is no consideration. What constitutes adequate consideration varies, and states have adopted differing views on whether the continuation of at-will employment of a physician is sufficient consideration for a non-compete agreement.

1. Some jurisdictions have held that at least some additional consideration, not the mere continuation of employment, must be given to support a restrictive covenant once employment has begun:

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[68] Shelbina Veterinary Clinic v. Holthaus, 892 S.W.2d 803, 805 (Mo. App. E.D. 1995).
[69] McKnight v. Midwest Institute of Kansas City, Inc., 799 S.W.2d 909 (Mo. App. 1990).
[70] The Galesburg Clinic Association v. West et al., 706 N.E. 2d 1035 (Ill. App.3d. 1999).

a. A Texas court recently held a physician's covenant not to compete was unenforceable because: consideration for a promise not to compete cannot be dependent on a period of at-will employment. "Such promise would be illusory because it fails to bind the promisor who always retains the option of discontinuing employment in lieu of performance."[71]

b. In Minnesota, a court held that a covenant not to compete which prohibited doctors from practicing medicine or establishing a practice in competition with the employer clinic within a specified area after termination of the agreement or termination of employment, was unenforceable for lack of consideration, where the covenant was not bargained for, and no distinction was made between signers and non-signers of the contract embodying covenant. [72]

2. Other jurisdictions have recognized continued employment as consideration to support a covenant not to compete, where discharge from the job was the alternative or where the employee remained with the employer for a substantial time after the covenant was signed.[73]

a. A New York court held that a restrictive covenant against an ophthalmologist, which limited his ability to practice medicine in the state, was valid because his promise not to compete was supported by adequate consideration, as his employment was at-will and his former employer exercised forbearance by not discharging him.[74]

X. Judicial Treatment/Relief of Restrictive Covenants

A. Courts may utilize a variety of methods in determining the enforceability of the restrictive covenant.[75]

1. Courts may reform a covenant not to compete by removing the unreasonable terms. The theory behind "blue lining" allows the court to mark out the unreasonable terms of the covenant so that they are severed from the rest of the covenant or contract. If the remainder of the covenant is reasonable, it is enforced. (This can be equated to an implied severability clause.)[76]

a. For example, a Pennsylvania court chose to enforce a covenant not to compete against a physician, but limited its scope to two counties rather than the five-county areas contained in the clause.[77] The court found that the physician and her former employer only competed in two counties. Thus, the court reasoned that if an employer does not compete in a particular geographical area, enforcement of a non-competition covenant in that area is not

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[71] *See* Mahmood, *supra* note 24 at *5.

[72] Freeman v. Duluth Clinic, Ltd., 334 N.W.2d 626 (Minn. 1983).

[73] *See, e.g.,* Affiliated Paper Cos. v. Hughes, 667 F. Supp. 1436 (N.D. Ala. 1987).

[74] Zellner v. Conrad, 183 A.D.2d 250 (N.Y. App. Div. 1992).

[75] *See* Decker, *supra* note 7.

[76] *See* Wellspan, *supra* note 40. Some state statutes also expressly permit "blue lining" of an agreement. *See* Mich. Comp. Laws. Ann. §455.774(a).

[77] *Id*.

reasonably necessary for the employer's protection. Accordingly, the court limited the non-competition covenant to the two counties necessary to protect the employer's interest.

2. Judicial interpretation of a restrictive covenant allows the court to take out the unreasonable terms and rewrite the rest of the covenant.

3. A court may also read the covenant as it is written. If it is unreasonable in any way, it will not be enforceable.

B. Generally there are two types of relief a court may provide a plaintiff to enforce a non-competition agreement.

1. Most non-competition agreements, including physician agreements, contain a consent to injunctive relief provision. Injunctive relief immediately bars the defendant from continuing the offending conduct, usually solicitation of customers (patients) or competing employment activity.[78] Injunctive relief is considered an extraordinary remedy and courts are reluctant to grant it.[79]

2. Another form of relief is liquidated damages. These provisions allow parties to negotiate and resolve the cost of the breach before any breach occurs. These clauses are enforceable only if it would be difficult to ascertain damages in the event of a breach; they must be reasonably related to damage expectations and cannot operate as a penalty.[80]

a. Practitioners also should note the impact that a decision by a court, which holds that a physician non-competition agreement violates public policy, has on liquidated damages clauses. At least one court has held that because the non-competition covenant in a physician's contract violated public policy, the liquidated damages provision also could not be enforced.[81] The court reasoned that the liquidated damages provision is required of the physician only to obtain his release from specific enforcement of the restrictive covenant. However, if the covenant cannot be enforced, the physician should not have to pay liquidated damages.

XI. Practical Considerations

A. Buying Your Way Out Of The Contract

Even without a liquidated damages clause in the contract, the parties may agree that the employer/hospital will relieve the physician from his/her obligations under the covenant not to compete for a specified amount of money to be determined in negotiation. The employer will attempt to have the physician pay an amount that approximates the amount of damages the employer anticipates, should the physician start practice right away in the restricted area.

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[78] *See* Loeser, *supra* note 1.

[79] *Id.*

[80] *Id. See also,* Ryan v. Mooney, 1981 U.S. Dist. LEXIS 14026 (N.D. Ill. 1981) (holding that physician was required to pay liquidated damages of $ 60,000 for violation of a non-competition agreement because it was a reasonable amount in light of the difficulty in determining damages caused by the physician's breach.)

[81] *See* Junkin v. Northeast Arkansas Internal Medicine Clinic, P.A., 42 S.W.3d 432 (Ark. 2001).

Naturally, the physician will attempt to pay as little as possible to relieve herself from the covenant restrictions.

B. Where Is the Practice Radius Measured From?

As a restriction against practicing within a certain geographic area is always in terms of distance from a certain point, the question becomes: exactly where is this distance measured from? The starting point for the measurement is usually the location where the physician has been practicing. What happens, however, when the physician has offices or sees patients in several different locations? Can the distance be measured from all of them? Employers usually attempt to make the radius of the restricted area as broad as possible. The physician, of course, will seek to have the restricted area narrowed. Where a physician sees patients in many different locations, one possibility is to measure the restricted area only from those locations where the doctor spends more than a certain percentage of his/her time. Another option is to limit the sites from which the radius will be drawn to 2 or 3 practice sites used by the doctor.

C. Re-Hiring Former Employees

Restrictions in physicians' employment agreements often state that a physician cannot hire any of the prior employer's employees (or induce them to leave their job) for a certain period of time after he/she leaves the prior employer. This becomes particularly difficult where the employees at the prior place of employment came with the physician to the new job. At times, an employer will relax this restriction. Other times, the employee herself will make the decision to go with the physician to his new office, without any inducement from the physician. (An employer cannot prevent an employee from voluntarily leaving one job and going to another.) where the restriction is on hiring (as opposed to inducing to leave), the physician may not be able to hire back a former employee for the amount of time contained in the restriction.

D. Contacting Former Patients

Patients always have the choice of their own physician, and they can always determine to leave one practice and go with their physician to his/her new place of work. The physician, however, may not be able, under the terms of the restrictive covenant, to contact his/her patients to notify them of the new location of the practice. Often, the parties agree in advance of the wording of a letter that will be sent to the patients, notifying them that their physician has left. In addition, the departing physician may be able to place a notice of his/her new practice location in a newspaper of general circulation, even if he is not able to contact patients directly. As patient lists and medical records are a main source of contention when a practice breaks up, this particular issue must be handled very carefully. Query: Could it be a violation of HIPAA if a physician leaves a practice and takes patient names and addresses with him, without the patient's consent or request?

E. Change Of Practice Notice

The issue here is who sends out the notice that a physician has left the practice, and is there any requirement that patients be told by the former employer where the departing physician is practicing? As noted above, often these notices are worked out by the parties prior to the time a physician leaves a practice or hospital.

F. Medical Records

Often the employment agreement will specify who the medical records of the patients belong to. Nonetheless, a patient always has the right to receive a copy of his/her medical record, upon payment of a reasonable copying fee. Alternatively, the patient can write to the medical practice and request that his/her record be copied and sent to another treating physician of choice. If there is a dispute between physicians, patient medical records, properly requested and paid for, cannot be held hostage.

XII. Conclusion

Public policy considerations increasingly have become the most important factor in determining whether a physician non-competition agreement will be enforceable. Regardless of the valid business interests sought to be protected, courts will not enforce a physician non-compete agreement if it unduly affects patient access to medical care, the public's freedom to choose the provider of choice and the number of physicians practicing in a particular area. Thus, attorneys should advise their clients to tailor narrowly the geographic and time limitations within a physician non-competition agreement, in light of the demographics of the practice area, the legitimate business interests of the employer and the number and specialty of physicians working in the same community.

COVENANTS NOT TO COMPETE AND HEALTHCARE:
A FIFTY STATE SURVEY

State	Statute or Constitutional Provision	Common Law
Alabama	Ala. Code § 8-1-1	Yes
Alaska		Yes
Arizona		Yes
Arkansas		Yes
California	Cal. Bus. & Prof. Code. §§ 16600 - 16602.5	Yes
Colorado	Colo. Rev. Stat. §8-2-113	Yes
Connecticut		Yes
Delaware	6 Del. Code Ann. § 2707	Yes
District Of Columbia	D.C. Code §28-4502	Yes
Florida	Fla. Stat. Ann. § 542.335	Yes
Georgia	Ga. Const. art. III, § VI, Par. V(c)1	Yes
Hawaii	Haw. Rev. Stat. §480-4(c)	Yes
Idaho		Yes
Illinois		Yes
Indiana		Yes
Iowa		Yes
Kansas		Yes
Kentucky		Yes

COVENANTS NOT TO COMPETE AND HEALTHCARE:
A FIFTY STATE SURVEY

State	Statute or Constitutional Provision	Common Law
Louisiana	La. Rev. Stat. Ann. §23:921	Yes
Maine		Yes
Maryland		Yes
Massachusetts	Mass. Gen. Law Ch. 112, §12X	Yes
Michigan	Mich. Comp. Laws § 445.774a	Yes
Minnesota		Yes
Mississippi		Yes
Missouri	28 Mo. Stat. Ann. §431.202	Yes
Montana	Mont. Code Ann. §§28-2-703 and 704	Yes
Nebraska		Yes
Nevada	Nev. Rev. Stat. §613.200	Yes
New Hampshire		Yes
New Jersey		Yes
New Mexico		Yes
New York		Yes
North Carolina	N.C. Gen. Stat. §75-4	Yes
North Dakota	N.D. Cent. Code §9-08-06	Yes
Ohio	Ohio Rev. Code Ann. §1331.02	Yes

COVENANTS NOT TO COMPETE AND HEALTHCARE:
A FIFTY STATE SURVEY

State	Statute or Constitutional Provision	Common Law
Oklahoma	15 Okla. Stat. §§217-219	Yes
Oregon	Or. Rev. Stat. §653.295	Yes
Pennsylvania		Yes
Rhode Island		Yes
South Carolina		Yes
South Dakota	S.D. Codified Laws §53-9-8 through §53-9-11	Yes
Tennessee		Yes
Texas	Tex. Bus. & Com. Code §§15.50-15.52	Yes
Utah		Yes
Vermont		Yes
Virginia		Yes
Washington		Yes
West Virginia		Yes
Wisconsin	Wis. Stat. Ann. §103.465	Yes
Wyoming		Yes

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