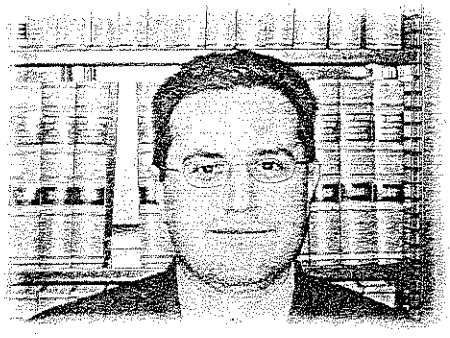

Renewed Vitality to the Enforcement of Physician Restrictive Covenants

by Leonardo M. Tamburello, Esq.

In its most common form in a employer-employee context, a "restrictive covenant" is a provision of an employment contract which prevents an employee from engaging in competition after their tenure has ended. Sometimes called "non-competition agreements," these restrictions are usually defined in terms of a fixed period of time and/or geographic area. When a post-employment dispute arises, it usually takes the form of the employer asking a court to enforce these limitations against their former employee.

New Jersey courts, like the majority of states, have not found restrictive covenants among physicians per se unenforceable. Moreover, our Legislature has not enacted any laws specifically prohibiting their use. Some states such as Colorado, Delaware, Massachusetts, Alabama and North Dakota have. Against this backdrop, New Jersey courts have enforced restrictive covenants in almost all fields of work, including among physicians. Because of the broad public policy ramifications in this area, however, courts have mapped this unique landscape gradually. In 1978, the New Jersey Supreme Court unequivocally stated that the use of restrictive covenants by physicians was not per se unreasonable and that physicians, no less than other employers, have a "legitimate interest" in protecting their patient relationships through the use of restrictive covenant agreements with employees.[1]

When evaluating a restrictive covenant among physicians, courts focus on three things:

1. Whether the covenant protects "legitimate interests" of the employer, and to the extent which geographical and other limitations are beyond an employer's "legitimate interests," they may not be enforced. Similarly, where the departing employee is not "in competition" with a former employer, such pursuits cannot be prohibited by a restrictive covenant and will not be enforced by a court.
2. Whether an "undue hardship" is imposed on the departing employee, noting that mere "personal hardship" does not, by itself, meet this standard. Instead, it is important to consider whether the employee can find work in the physician's field outside of the restricted area and the reasons for the termination of the relationship;
3. Whether the public interest will be adversely impacted by enforcement of the restriction. In evaluating any detrimental effect on the public, courts look to the demand for the departing physician's services and the opportunity for other physicians in the area to provide the same services. If the geographic restrictions would have the effect of preventing patients from receiving treatment, then courts will likely limit the geographic scope of the restriction.

In late 2003, the Appellate Division decided Community Hospital Group v. More[2], in which a hospital was seeking a enforcement of a restrictive covenant against a neurosurgeon who had resigned from its staff. In 1994, the plaintiff-hospital and defendant-physician entered into a one-year contract immediately following his residency. The doctor's employment was later renewed in 1995 for four years and again in July 1999 for an additional five years. Each of these contracts contained a restrictive covenant which prohibited him from practicing within a thirty-mile radius of Edison, New Jersey for two years after ending his employment. While he was on staff, the hospital promoted the defendant as one of its premier "sub-specialists" and featured him as an expert speaker at seminars and other programs designed to generate referral sources.

In July 2001, two years into the five-year term of the current contract, defendant tendered his resignation, effective one year later. Shortly before leaving, defendant referred to himself as the plaintiff-hospital's "top producer" and "rainmaker." After resigning in July 2002, he joined a neurosurgery practice approximately five miles from his former

employer.

This dispute grew into a litigation when the hospital learned that defendant joined this nearby practice group as a neurosurgeon. Believing defendant had acted in violation the restrictive covenant, the hospital applied to the Chancery Division for a preliminary injunction to enforce the prohibition against defendant working as a neurosurgeon for two-years within thirty miles of the hospital. A preliminary injunction is a specialized form of relief where a court is asked to consider an incomplete factual record and issue a temporary order. Under Crowe v. DiGioia,[3] courts may issue preliminary injunctions when the party seeking one can establish: (1) "irreparable harm," such as where money damages are inadequate of making an injured party whole; (2) that the legal right being asserted has already been "firmly established" or recognized by the courts; (3) it is reasonably probable that the party seeking preliminary injunction will prevail at a final hearing; and (4) on balance, it would be a greater hardship not granting the temporary relief to the party seeking it than the temporary relief, if granted, would impose on the defendant.

Key to the Appellate Division's consideration of Community Hospital v. More was the hospital's ability to portray itself as a non-profit, clinical-care, research and teaching hospital in the field of neurology. From this premise, the hospital successfully argued that it requires a broad patient base in terms of quantity and diversity to fulfill its mission and that it hires entry-level physicians such as the defendant and depends upon them to cultivate the requisite patient base. Moreover, it convinced the court that losing this patient base to former employees could threaten both the hospital's "institutional framework" and diminish its reputation in the field. In the court's view, this type of harm was not readily balanced with monetary damages and it therefore recognized the possibility of irreparable harm to the institution.

This "irreparable injury" obstacle is often the most formidable when seeking a preliminary injunction, particularly since equating some injury with an amount of economic compensation has become an industry unto itself in recent years. That the hospital derived some economic benefit from the volume of cases was recognized by the court, but the important evidence in clearing this hurdle was the broader-based institutional goals of research in neuroscience, training physicians and providing those benefits to the community. The defendant's arguments, while forceful, never provided a counterweight to the hospital's professed risk that it would be unable to continue in its mission as a research, training and teaching facility without the benefit of restrictive covenants such as the one contained in the contract with defendant.

In evaluating the likelihood that the hospital would ultimately prevail on the merits, the Appellate Division rejected the idea that a hospital does not have a legitimate interest in protecting its patient base. Indeed, it found that hospitals, no less than individual physicians, are capable of forming "doctor-patient" relationships which should be recognized and protected.

As to whether the restriction would cause an "undue hardship" on defendant, the court's primary focus was on whether the employee could find work in his field elsewhere, outside the restricted area, and the reasons for his termination. Additional factors it considered included: (1) the agreement's geographic and temporal scope; (2) whether the kinds of activities restrained would place the employee in actual competition with the former employer; and (3) whether enforcement would unduly burden an employee finding work in their field.[4]

Important to the Appellate Division's view that the two-year, thirty-mile restriction would not create an "undue hardship" on the defendant was evidence that he was offered but declined employment outside the restricted area and that he, not the institution, initiated the termination of employment. In light of this, the court viewed any hardship resulting from enforcement of the covenant as "personal and self-induced."[5] This, of course, begs the question of whether the court would have reached a different outcome had the hospital terminated the physician and then sought to enforce the restrictive covenant.

Compared to other professions, somewhat larger temporal and geographic restrictions are permitted with respect to physicians because of the relatively infrequent contacts between a doctor and patient. Nonetheless, the restrictions remain limited to the period needed for the employer to demonstrate their effectiveness to patients. In this situation, the court found the two-year period "reasonable," given the area of specialty involved. Similarly, the thirty-mile geographic-limitation was found reasonable in light of evidence that patients travel greater distances for specialized care such as neurosurgery and also in recognition that plaintiff draws its neurosurgical patient base from a wider geographical area than a general practitioner would.

In terms of the "undue burden" which the restrictive covenant may place on a defendant in finding employment in their field, none existed in this case where the defendant conceded that he did not consider employment at several hospitals beyond the restricted zone, and specifically declined employment at others located outside the thirty-mile radius. Interestingly, the court gave little, if any, weight to the defendant's contention that employment outside of the thirty-mile limit would lave required him to move his family which had substantial ties to their current community.

The Appellate Division identified three primary public policy concerns: first,

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whether enforcement of the restrictive covenant would create a shortage of physicians in the area; second, whether defendant's patients within the restricted area would be burdened in continuing their relationship with him; and third, the impact on institutions such as the plaintiff of not enforcing restrictive covenants like this one.

Based on evidence that there were at least five other hospitals with qualified neurosurgeons on staff, there was no evidence that enforcement of the covenant would deprive the public of any needed medical services. As for defendant's own patients, the court recognized the possible "burden of traveling an increased distance," but ultimately acknowledged that traveling to see specialists such as defendant was not unusual and would not present a major obstacle to defendant's patients. Thirdly, the court found that institutions such as plaintiff who make investments in cultivating young, unestablished practitioners must be allowed to protect such assets. It therefore recognized the possibility that nullifying restrictive covenants such as this could, over time, diminish the availability of specialists in an area because of the institution's reluctance to expend the time and money required for their training.

The court also found that granting the injunctive relief would not cause more harm than denying it. Again, the court was strongly influenced by the hospital's function as a training ground for the community's physicians. This factor weighed in favor the plaintiff based upon its investment in fostering defendant's professional development and the risk that without protection in the form of enforcement of restrictive covenants like this, "erosion of either plaintiff's patient or referral bases" would render it unable to operate in the capacity in this capacity in the future. Appellate Division then remanded this matter to the trial court which had initially denied enforcement of the restrictive covenant.

When contemplating any change in employment relationship where a restrictive covenant is involved, it is incumbent upon both the employer and employee to appreciate the scope of any possible future restrictions. As this recent Appellate Division case demonstrates, courts will not hesitate to enforce reasonable time and location limitations under proper circumstances, even going so far as to "blue-line" either the geographic or temporal conditions of a restrictive covenant to a specific situation.

It is also important to heed the fact-sensitive nature of these types of cases. Central to the Appellate Division's analysis in Community Hospital v. More was its belief that not enforcing the restrictive covenant exposed the plaintiff-hospital to much more than an immediate economic loss and jeopardized the hospital's fundamental core mission of education, research and training of physicians to serve the community. Had the plaintiff not been a hospital which developed specialists such as defendant; or had the defendant been terminated by the plaintiff; or had the defendant practiced in a less specialized area, the outcome of this case could have been drastically different. In other cases where less altruistic institutional goals were at stake, the courts have struck down of restrictive covenants. The restrictive covenant nevertheless remains an important tool both in planning and managing employment relationships.

1 Karlin v. Weinberg, 77 N.J. 408 (1978).
2 — N.J. Super. — (Docket No. A-3861-02T3) (App. Div. 2003).
3 90 N.J. 126 (1982).
4 Community Hospital v. More, supra slip op. at 26 (discussing Maw v. Advanced Clinical Communications, Inc., 359 N.J. Super. 420 (App. Div. 2003), appeal docketed, No. A-99-02 (N.J. 2003)).
5 Community Medical Hospital., supra, slip op. at 27.

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