Protecting the Practice: Restrictions on Partners and Associates

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* Financial Interest

Overview

• Scenarios
  • Associate physician resigns or is terminated
  • Shareholder physician resigns or is terminated

Bad Things that Can Happen

• Loss of patients and referring sources
• Loss of revenue to cover overhead
• Unsupportable buyout obligations
• Decrease in provider availability
• Loss of good support staff
• Litigation
Objectives

- Deter competitive departures
- Protect volume from competitive doctor
- Protect incomes of remaining doctors
- Minimize disruption/transition pain
- Avoid decrease in doctor availability, quality of service
- Avoid litigation

Countervailing Considerations

- Will a tough non-compete clause effect associate recruiting?
- Will your shareholders sign non-compete clauses?
- Costs of enforcing non-compete or non-solicit provisions
- Legality of non compete restrictions
- Buyout “fairness”

Tools

- Non-compete restrictions
- Non-solicitation provisions
- Confidentiality clauses
- Patient charts as property of corporation
- Operational data security – patient names
- Provisions that limit buyout costs
Good Documents are Critical

- Employment Agreements for associates and partners
- Shareholders Agreements or LLC Operating Agreements, for partners

Associate Physicians

- A non-compete is expected by new hires, and often accepted without change
- Employing practice has the leverage
  - It has the job
  - Most associates are more concerned with the salary

Non Compete Clauses

- Key question: what state are you in?
  - Some states do not allow non-compete clauses, or limit their scope
    - E.g. MA, CA: no covenants for associate doctors
    - TX: must provide reasonable buyout clause
  - Most states: a “reasonable” covenant is enforceable
Non-Compete Agreements – Nuts and Bolts

- What is "reasonable"?
  - Duration: 1-3 years
  - Radius or Geography: your service area, conservatively estimated
  - Your attorney will tell you what the courts in your state have said on these issues

Non-Compete Remedy

- Injunction
  - "You may not practice, period", by order of court
- Liquidated Damages
  - "You can practice, but you must pay $______ for the privilege"

Non-Compete Vulnerabilities

- Not permitted in all states
- May not be enforceable in rural or other underserved area
- Disliked by many judges as an undue constraint on right to earn a living
There must be legal “consideration”
- For new hires: the job itself
- For a current partner: other partners signing the same restriction
- For an associate who is already working:
  - An increase in pay or bonus
  - Conversion to shareholder status

Legal “Consideration”
- But “sign or you’re fired” is likely unenforceable – talk with your attorney

Common Associate Concerns
- “If you fire me without cause, I’m not to blame. In this situation, the non compete should not apply.”
Common Associate Concerns

• “The practice is in my home town. If things don’t work out with this practice, I will have to leave the place where all my family and connections are.”

Non-Solicitation Clauses

• Consider the departing doctor with a 10 mile non-compete
• He goes 10.1 miles away, and then writes a letter to all of your patients: “I am pleased to announce the opening of my new practice”
• Non-solicit clause bars such solicitation

Bar Solicitation of:

• Any Practice patient, including patients treated by the departing doctor
• All referring sources and contractual arrangements
• Practice employees
Non-Solicit Remedies

- Court injunction is often not enough
- Once the solicitation letter has been sent, the injunction is useless because the damage is done

Liquidated Damages

- Can be a fixed number: e.g. $100,000
- Or a formula: e.g. 50% of departing doctor’s annual salary
- Avoid: “damages as determined by court”
  - Difficult to prove and quantify solicitation damages
- Add: Recovery of attorneys fees, if Practice must sue to enforce

Solicitation of Employees

- Prohibited acts:
  - Solicitation of staff, or inducing them to terminate relationship with Practice
  - BUT ALSO prohibit HIRING of employee, even if there was no solicitation
  - “Employees” include anyone who worked in Practice within 6 months of departing doctor’s termination date
Pushback on Non-Solicit Clause

- Doctor claims you are forcing him to “abandon” his patients in violation of ethical obligations
- But patient is not abandoned. Remaining doctors in group are ready to take care of patient.

Other Good Provisions

- “Employee acknowledges and agrees that all medical charts and records and patient lists are confidential information, trade secrets, and property of the Practice, and not of the Employee. Employee will not remove or copy patient lists.”

Other Good Provisions

- “Employee may not in any advertising or marketing materials make reference to her present or past affiliation with Practice”
Other Good Provisions

• “Employee may not engage in direct mail solicitation of patients residing in the following zip codes: ____________”

Non-Disparagement Clause

• “Employee agrees that, both during the Term and thereafter, he will not directly or indirectly, disparage the Employer, its business, services, personnel, or management.”

No Long Goodbyes

• Contract normally says that either employer or employee can terminate relationship, without cause, upon 30 – 120 days advance written notice.
No Long Goodbyes

• Problem: during the notice period, if the doctor remains on-premises, he may:
  • Say bad things about the Practice, to your employees
  • Solicit patients verbally
  • Download or copy patient addresses

• So add a clause that gives the Practice the right to relieve the Employee doctor of further duties during the notice period, so long as he continues to receive his salary
• Gets the employee doctor out of a position to harm you

Operational Protections

• Keep data secure
• “Trade secrets” enjoy special protection under laws of many states.
• But patient data won’t have status as “trade secret” unless you take reasonable steps to maintain its secrecy
Other Operational Issues

• Patients call asking for departed doctor
• What should the front desk say?
  • "I'm sorry we have no information on Dr. X" [not true]
  • Forces insistent patient to find the doctor on his own
  • Creates an angry patient

Better Response

• "Dr. X is no longer here but Dr. Y can see you."
• If patient insists, give departed doctor’s location
  • You aren’t going to retain this patient
  • You can only make things worse by resisting

Departing Shareholder Issues

• Are they any different from associates?
  • Likely enjoys greater protection from involuntary termination
  • Maybe not so willing to sign a non compete
  • Have more financial resources to litigate
  • Can do far more damage; they have larger patient followings and reputation
  • Rights to buyout $$
How to Handle Shareholders

- Strongly consider non-compete and non-solicit provisions for all shareholders
- Do not insulate any shareholder from involuntary termination, even without cause
- Careful with shareholder veto rights or supermajority provisions

Shareholder Buyout Protections

- Provide that a shareholder who competes or solicits loses all or part of buyout
- This may be legal even if a “regular” non compete is not enforceable
  - Check state law

Shareholder Buyout Protections

- To get full buyout, shareholder must give substantial advance notice, e.g. 12 months
- Total buyout payments in any one year can never be more than 2%-6% of annual receipts
  - Like a modest overhead item
Tying up Loose Ends: Termination Agreements

- Employer Gets:
  - Unconditional release from any potential lawsuit
  - Control over post-termination actions by employee
  - Resolution of all outstanding issues

Tying up Loose Ends: Termination Agreements

- Employee Gets:
  - Severance; and / or
  - Good recommendation; and / or
  - Adjustment of non-compete area; and
  - Certainty as to payment

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