

PHYSICIAN OWNERS AND COVENANTS NOT TO COMPETE

IF YOU HAVE QUESTIONS REGARDING THIS MATTER, PLEASE CONTACT:



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Texas courts are reluctant to enforce covenants not to compete ("non-competes") in employment arrangements. Courts examine non-competes with close scrutiny and do not hesitate to strike them if they fail to meet statutory requirements. Non-competes in the employment context are disfavored because they inhibit an employee's ability to make a living after leaving his or her former employer. To date, the courts have not addressed the enforceability of non-compete clauses as against physician owners. Unlike non-competes as against employees, non-competes in the physician investor context restrict only ownership in a competing facility. Texas courts will eventually confront non-competes in the ownership context, and when they do, medical project developers need to make sure that the non-competes in the contracts they have with physician investors are strong enough to withstand judicial scrutiny and are enforceable.

Thus far, the requirements for non-compete enforceability, found in Section 15.50 of the Texas Business & Commerce Code have been applied only in employment arrangements; however, nothing in the plain language of Section 15.50 restricts its requirements to the employment context. Section 15.50 is the standard in Texas used by courts to evaluate the enforceability of non-competes. It lists the requirements with which non-competes must comply before they can be enforced. Section 15.50(a) provides two general requirements for non-competes. Section 15.50(b) imposes five additional requirements for non-competes with licensed physicians including the requirement that the non-compete provide for a buy-out of the covenant by the departing physician at a reasonable price or, at the option of either party, as determined by a mutually agreed upon arbitrator or, in the case of an inability to agree, an arbitrator of the court whose decision shall be binding on the parties. The buy-out provision is a Section 15.50(b) requirement. The theory is that the practice supported the physician during the time that the physician saw patients with the practice. If the departing physician leaves with patients he or she has met at the practice, the practice will incur substantial new costs to replace both the departing physician and the patients the departing physician is taking. The other side of the coin is that a physician cannot be haled as an indentured servant to a group simply because he or she began practice there. The compromise is that the physician may be released from this promise not to compete in exchange for a reasonable buy-out.

To date, all of the court decisions involving non-competes and the requirements of Section 15.50 have pertained to the employer-employee context.¹ The few court cases involving non-competes with physicians have arisen out of employment arrangements with the subject physicians and have involved the employers' attempts to restrict the employees' ability to practice medicine. In these physician-employment arrangements, the courts have made it clear that unless non-competes comply with the provisions of Section 15.50, they will not be enforced. Texas courts have not yet applied Section 15.50's requirements outside the employment context; however, this does not mean that 15.50's requirements will be restricted to employment

arrangements.

The drastic changes that medical practice has undergone in recent years will require Texas courts to examine physician non-competes in an entirely new context- the ownership context. Physicians are investing in entities such as general acute care hospitals, specialty hospitals, ambulatory surgical centers, cardiac catheter labs, long-term acute care centers and imaging centers for a variety of reasons. One reason is the reduced reimbursement rates physicians are facing, but that is definitely not the only reason. Physician ownership in health care facilities aligns the interests of the physicians and the administrators of the facility. The result is increased physician oversight in the day-to-day operations of the provider and improvements in all aspects of patient care.. The vast majority of partnership agreements and company agreements contain non-compete clauses that restrict the physician owner's ability to invest in competing entities.

Unlike non-competes in the physician- employment context, non-competes in the physician- ownership context do not prevent the physician from seeing patients and continuing his practice. A physician investor is free to continue to make a living by providing medical care to patients. He or she is only restricted in his or her ability to invest in or provide other services for competing facilities.

Until the Texas courts address the issue of physician investors and non-competes and whether the requirements of Section 15.50 will be applied beyond the employment context, drafters of these provisions in an investment context are faced with the question of whether to include the limitations of Section 15.50 or not. Will the courts use the distinction between non-competes in the employment context and non-competes in the ownership context to deem Section 15.50's requirements inapplicable to physician investor non-competes? Or will the courts view physician owner non-competes with as much disdain as they view employer-employee non-competes and subject physician investor non-competes to close scrutiny and the requirements of Section 15.50?

Absent further clarification from the courts, the prudent course of action for medical project developers is to strengthen the non-competes in the contracts they have with physician investors by including the requirements of Section 15.50 for non-compete enforceability. Texas courts will be more likely to enforce the physician investor non-competes if they meet Section 15.50's requirements.

¹ See e.g. *Light v. Centel Cellular Co. of Texas*, 883 S.W.2d 642 (Tex. 1994); *Weatherford Oil Tool Co. v. Campbell*, 340 S.W.2d 950 (Tex. 1960); *C.S.C.S., Inc. v. Carter*, 129 S.W.3d 584 (Tex. App.—Dallas 2003, no pet.); *Laredo Med. Group v. Lightner*, 153 S.W.3d 70 (Tex. App.—San Antonio 2004, pet. filed Jan. 5, 2005); *TMC Worldwide, L.P. v. Gray*, 178 S.W.3d 29 (Tex. App.—Houston 2005, no pet.).