Legal Briefs

GENE A. BLUMENREICH, JD
AANA General Counsel
Nutter, McClennen & Fish, LLP
Boston, Massachusetts

Covenants not to compete

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We have recently learned of cases where anesthesiology groups are offering employment to CRNAs only if they enter into employment agreements which prohibit the CRNA from competing with the employer. Because covenants not to compete have not been common in the healthcare field, it may be useful to discuss them and some of the legal issues which surround them.

Covenants not to compete typically prohibit an employee from competing with the employer during the employment period and for some period of time after the employment relationship is terminated. In a well-accepted application, an employer has developed a new technology which is only partially protected by patent or copyright laws, the employer may seek to protect its investment by prohibiting its employees from competing with it. Covenants not to compete are "legal" in the sense that courts will, in appropriate circumstances, enforce them, often by granting injunctions. However, the effect of enforcing covenants not to compete is often to force someone to give up employment, risking the livelihood of the individual and his or her family, something courts are reluctant to do. Therefore, although covenants not to compete are legal, they are often difficult to enforce.

What does it mean to enforce a covenant not to compete? In general, breaches of contractual provisions result in the awarding of monetary damages. In the area of employment by a competitor, however, monetary damages may be difficult to determine. Moreover, a former employee may be willing to pay some nominal profit to the former employer just to compete. A more desirable remedy is an injunction, an order of the court prohibiting someone from engaging in certain activities. The main benefit of the injunction is that the entire power of the legal system can be used to enforce it. If it is violated, not only will the competitor become subject to damages but also he or she can be held "in contempt" and jailed to punish or stop the prohibited activity.

Law and equity courts

An injunction is an "equitable" remedy. At the time of the American Revolution when our court system was established, courts in England were divided into "law" and "equity." Law courts awarded damages in contract and tort actions while equity courts were permitted "to do justice." Equity courts reformed contracts, granted injunctions, and awarded other kinds of relief which the law courts were prohibited from doing. Because it was "to do justice," an equity court would not grant exceptional relief unless the court believed justice would be served by doing so.

Modern day courts combine the law and equity functions but still follow the historic traditions. This has two effects. First, as we shall shortly discuss, the request for an injunction must be fair. Courts will not award injunctions under circumstances where justice will not be served. Second, the determination of whether justice will be served is largely one of discretion, the discretion of the local trial court. Whether the trial court denies or grants an injunction, the appellate court will rarely overturn it, in the absence of evidence that the trial court abused its discretion. Merely being wrong is insufficient, to be reversed the court must

have been so wrong that no reasonable court would have acted that way. This suggests a major caution for this article. Not only can the laws of individual states differ, but also within the states, results can be effected in a major way by the attitudes, personalities, sympathies, and even the prejudices of the trial court hearing the matter.

Time, geographic scope, and basic fairness

To be enforceable, a covenant not to compete must be reasonable as to time and geographic scope. In my experience, covenants prohibiting competition for periods of longer than 2 or 3 years, in the absence of special circumstances, will be difficult to enforce. Even for shorter periods, the court will consider whether the legitimate needs of the employer justify the period in which competition is prohibited. Courts will inquire as to the useful life of an invention and consider the period of noncompetition when viewed against the useful life. For example, in the computer field, new technologies may have a useful life of 6 months before they are replaced by even newer technology. Courts will be reluctant to prohibit a former employee from remaining unemployed for several years when other competitors will have the same information and be able to effectively compete in 6 months. The second area of limitation on covenants not to compete is geographic. An employer who employed someone as a salesman servicing and calling on accounts in New York City will find it difficult to enforce a covenant not to compete that prohibits the salesman from competing along the entire East Coast.

But the courts' concern with fairness is not limited to length and geography. Courts will also consider basic fairness. Does the restriction merely punish the employee by keeping him or her from working at all, or is the employer trying to protect business secrets or other legitimate interests in a limited fashion? Covenants which are merely designed to keep an employee from working are not viewed as reasonable by the courts. There must be some way in which the employee's present employment harms the interest of the former employer. A covenant not to compete given by someone selling his or her business to a new owner will be enforced by the courts because the old owner's unavailability is an appropriate way to transfer customer loyalty from the old owner to the new.

In many states, if a covenant not to compete is too broad, the courts may have the discretion of reducing the time or geographic coverage to one that is enforceable rather than dismissing the covenant entirely. Because enforcement depends on the discretion of the court, it is nonetheless desirable for the employer to have a suitably limited covenant not to compete to avoid appearing unreasonable. Courts are, after all, human and often maintain a sense of fairness and a dislike for overreaching. An overly broad covenant may lead the court to believe it would be inappropriate to enforce the covenant at all. Even when courts are willing to cut down a covenant not to compete to a reasonable time or geographic area, they will not enforce a provision that is unreasonably broad in other regards. In one case, a prohibition against using "any information gained" during the employment period was too broad to be enforced.[1]

Consideration

Covenants not to compete also require "consideration." Contracts are not one-way streets. They are supposed to be a benefit to both parties. In the normal employment setting, the employer pays wages in return for the employee's services. The wages are the consideration. If the employment relationship is just beginning, the employer's promise to pay wages is the consideration for the employee's agreement not to compete. Note that courts will seldom determine the *adequacy* of the consideration. The court will merely look to see if there was any consideration at all. If there is none, the covenant not to compete will again be unenforceable. In some instances, an employer may ask an existing employee to sign an agreement not to compete. If no new employment terms are offered, the employer may claim that continued employment serves as consideration for the covenant not to compete. Some courts have held that this is not adequate to serve as consideration for a covenant not to compete, while others have said it does. In one county in Ohio, the same court ruled both ways within 6 months.[2]

Trade secrets

Perhaps the most common use of covenants not to compete are in the area of trade secrets. There are good economic reasons to protect an employer's trade secrets. Employers need to impart trade secrets to employees in order to utilize trade secrets in their businesses. Unless the employer can prohibit the employee from using its trade secrets, businesses will be unable to grow, consumers will be deprived of desirable goods and services, and the economy will suffer.

How do these principles apply to covenants not to compete in healthcare or in anesthesia in particular? There are no trade secrets in anesthesia. Techniques are widely disseminated, and knowledge is encouraged to be disbursed, not maintained as trade secrets. Unless the CRNA is

working in an advanced research or developmental area, it is hard to justify a covenant not to compete on the need to protect trade secrets.

Some states recognize "customer contacts" as a legitimate interest to be protected. In some instances, an employer may have some unusual contractual to be protected. A less onerous way of protecting the employer's interest would seem to be longer term contracts with the institutions, not tying up employees to keep them from competing for the contract. Nonetheless, there are cases where courts have indicated that they would uphold covenants not to compete to protect customer contacts. In *Leopoldstadt, Inc. v Fitzgerald,*[3] a court refused to grant summary judgment in favor of a nurse who argued that her covenant not to compete was unreasonable. The covenant may have been needed to protect customer contacts. Additionally, the nurse had accepted $497,000 as consideration for her execution of the stock redemption and noncompetition agreements. However, for a covenant not to compete to protect customer contacts to be enforceable, the nurse anesthetist would have to accept employment where he or she had "customer contacts." A nurse anesthetist leaving one employment situation to accept another where he or she had no customer contacts is merely being punished for leaving employment.

On the other hand, sometimes an employer will ask that a CRNA sign a covenant not to compete during the term of employment only. This may be enforceable depending on the employer's motivation in asking for it. If the employer wants to make sure the CRNA will be available to take call, will be rested, and will not be overworked, then these may be legitimate reasons for the covenant not to compete. If the employer is merely trying to eliminate the CRNA as a potential competitor from other part-time contracts, then the situation may be entirely different.

In some states, the courts or legislatures have held that the relationship between healthcare workers and their patients is of such a nature that contracts which detract from or limit that relationship are unenforceable. The more remote the region, the greater the argument that enforcement of a restrictive covenant would be contrary to public policy, especially if there is evidence that patients might suffer in the absence of qualified anesthesia providers.[4] In at least Colorado, Delaware, and Massachusetts, there are statutes barring covenants not to compete in physician employment contracts or partnership agreements.[5] As a matter of public policy, these provisions *should* also bar covenants not to compete in employment contracts with CRNAs.

Try to avoid signing a covenant not to compete

What do you do when your employer asks you to sign a covenant not to compete? First try to avoid signing one. Even if the covenant is unenforceable, you will have entered into an agreement that on its face restricts your freedom to seek employment elsewhere. Should you later compete with the employer, you could find yourself being sued and spending time in court and money on attorneys. Worse, the outcome of litigation is always uncertain, and even if you have the best case, there is some risk that you could lose and be restrained from competing.

If you cannot avoid signing a covenant not to compete, consider your alternatives. Is there another position with comparable terms you could seek which does not require a covenant not to compete? Are you committed to the location? If you really have no viable alternatives, consider how likely it would be that you would *want* to challenge the covenant not to compete. Hypothetically, is the anesthesiologist who is offering you a position the brother of the surgeon who owns the hospital and performs all the surgery so that even if you wanted compete, there would be no practicable way to do so? Can you make the terms of the covenant not to compete less onerous? Consider a shorter term covenant not to compete or a covenant not to compete that covers a small section of the community that would still leave you employment alternatives. Try to limit the covenant not to compete to situations where you voluntarily terminate employment so that if you are fired or driven out of the employment, there would be no covenant not to compete.

Finally, if you have no choice because, for example, this is the only hospital in a community where you grew up and where your spouse and high school aged children live, do what you have to do, but keep in mind that courts do not favor covenants not to compete. If you find yourself in a situation where you might want to violate your covenant, seek legal advice because there may be a variety of legal theories on which to avoid it. These agreements should not be entered into lightly, but they may not be the handcuffs they appear to be.

REFERENCES

(1) *Abramson v Blackman,* 340 Mass. 713-715 (1960).
(2) See the discussion in *Chrysalis Health Care Inc. v Brooks,* 65 Ohio Misc.2d 32, 640 N.E.2d 915 (1994).
(3) 992 WL 396330 (D. Kan.).
(4) See, for example, *Middlesex Neurological Associates, Inc.* (3 Mass. App.Ct. 126, 324 N.E.2d 911, 1975 [before Massachusetts adopted a statute prohibiting convenants not to compete in physician contracts]).
(5) Colo.Rev.Stat. § 8-2-113(3) (1986); Del.Code Ann. tit. 6, § 2707 (1993), Mass.Gen.Law Ch. 112 § 12X.