

“These cases demonstrate that post-employment restrictive covenants between physicians remain enforceable, and will be enforced by New Jersey’s courts . . .”



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The *More* and *Pierson* Decisions: Restrictive Covenants Between Physicians are Enforceable, and May Restrict Physicians from Practicing in Local Hospitals

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The Superior Court of New Jersey, Appellate Division, recently decided *The Community Hospital Group, Inc. t/a JFK Medical Center v. More, M.D.* and *Pierson v. Medical Health Centers, P.A.*, both of which upheld restrictive covenants between physicians, and both of which resulted in prohibiting the departing physician not only from practicing within the area covered by the covenant, but also from practicing in hospitals located within the affected area. These decisions are of extreme significance for the medical community in New Jersey because they dem-

onstrate the continued enforceability of restrictive covenants between physicians, reaffirm the seminal decision in New Jersey enforcing such restrictive covenants, *Karlin v. Weinberg*, and, for the first time in this state, specifically approve covenants that require the departing physician to cease practicing at hospitals located within the area affected by the covenant. In fact, recognizing the widespread importance of the matters at issue, the Supreme Court of New Jersey has recently entered a “stay” on the *More* decision, pending its review of that decision.

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THE *COMMUNITY HOSPITAL* DECISION

In *Community Hospital*, the New Jersey Neuroscience Institute (a part of the JFK Medical Hospital, entered into successive one-year contracts with the defendant physician. The contracts contained post-employment restrictive covenants that prohibited the defendant physician from, among other things, engaging in medical practice in competition with the Institute within a 30-mile radius of the hospital for two years following the termination of his employment with the Institute.

The Institute hired the defendant physician upon the completion of his residency at Mount Sinai Hospital in New York. The defendant physician did not bring to his position any practice or patient base. However, the Institute promoted him to the public and to other specialists, having him featured as an expert speaker at seminars and other programs tailored to referral sources. The defendant physician's practice grew from no patients when he was first hired, to 35 to 40 surgeries within his first six months at the Institute, and his practice increased annually each year. The defendant physician attributed the growth of his practice to his increased visibility and continued employment by the Institute, and before leaving employment with the Institute, he proclaimed himself as the "top producer" and "rainmaker" among the Institute's physicians.

On July 17, 2001, the defendant physician submitted his resignation to the Institute effective July 17, 2002. On July 22, 2002, the defendant physician joined Neurosurgical Associates at Park Avenue (NAPA), which was located approximately five miles from JFK Hospital, contrary to the two-year, 30-mile restriction contained in his post-employment restrictive covenant with the Institute. The defendant physician also obtained privileges at Somerset Medical Center ("SMC"), which was located in the restricted area. The Institute thereafter filed an application for injunctive relief to enjoin the defendant physician from practicing with NAPA in violation of his restrictive covenant.

THE *PIERSON* DECISION

In *Pierson*, Medical Health Centers, P.A. ("MHC") entered into an employment agreement with the plaintiff physician, an interventional cardiologist, which commenced on July 1, 1997. During his employment, plaintiff physician had active staff privileges at several local hospitals including Riverview Medical Center ("RMC")

and Jersey Shore Medical Center ("JSMC"). Interventional cardiac procedures were mostly performed at JSMC during his employment because RMC was not equipped to handle such procedures. Plaintiff physician claimed that MHC had hired him, in part, so that he could develop a patient base and referral sources at JSMC for such procedures. The plaintiff physician's employment agreement with MHC contained a restrictive covenant that prohibited him from entering into the practice of medicine "in any manner or capacity" within 12 miles of MHC's Middletown, New Jersey office, or within six miles of any of MHC's other offices if he, in fact, had worked there.

By letter dated March 22, 2002, MHC provided the plaintiff physician with 90 days written notice of its intention not to renew his employment (as it was permitted to do under the employment agreement). The letter also advised the plaintiff physician of his post-employment obligations under the employment agreement, including compliance with the requirements of his restrictive covenant. Subsequently, the plaintiff physician filed an application challenging his restrictive covenant, arguing, among other things, that it did not protect a legitimate interest of MHC and was injurious to the public.

Analysis: The Community Hospital and Pierson courts both uphold the enforceability of the restrictive covenants between the physicians.

The Appellate Division, in both *Community Hospital* and *Pierson*, found the restrictive covenants to be fully enforceable. Consequently, in *Community Hospital*, the defendant physician was enjoined from performing neuro surgery within 30 miles of his former employer, which included a prohibition of such practice at hospitals (including SMC) located in the restricted area. Likewise, in *Pierson*, the Court found that the covenant prohibited the plaintiff physician from practicing medicine "in any manner or capacity" within 12 miles of his former employer's office, which specifically included a prohibition on practicing in hospitals within the affected area. These decisions are significant, and should be of interest to all practicing physicians in this state.

First, in the wake of recent commentary suggesting that the *Karlin v. Weinberg* decision – and its approval of restrictive covenants between physicians – may be subject to reconsideration, these cases demonstrate that post-employment restrictive covenants between physicians

remain enforceable, and will be enforced by New Jersey's courts where the covenants protect a legitimate interest of the employer, are not unduly burdensome to the former employee, and are not injurious to the public.

Second, both decisions are important because they both explicitly hold that medical employers have a legitimate interest in protecting their patient bases and "referral sources" from erosion by a former physician-employee. Thus, while prior cases have indicated that a naked restraint on competition may not be permissible, *Community Hospital* and *Pierson* demonstrate that medical employers have legitimate interests in protecting their patient bases and "referral sources" and that they may legitimately protect such interests by restricting former employees from practicing within an area designed to protect such patients and sources.

Third, the *More* decision is significant because it enforced a restrictive covenant that extended a full 30 miles from the employer's office. In this regard, the Court reasoned that *Community Hospital* performed a specialty, neurosurgery, and that it was reasonable to conclude that it would need to draw its patient base from a larger geographical area than a general practitioner would. Moreover, the Court also reasoned that the public interest would not be harmed by the 30-mile restriction because patients will typically travel to see a specialist. Significantly, the Court's holding suggests that specialized medical providers can legitimately restrict their employees from practicing in a much larger geographic area than would be permissible for general practitioners.

Lastly, both *More* and *Pierson* also demonstrate that where, as in those cases, the restricted area under a covenant includes hospitals, the former employee may also be enjoined from continuing to practice at such hospitals. Indeed, while this is implicit in the *More* decision, *Pierson* specifically addresses this aspect of a restrictive covenant's scope (for the first time by a New Jersey Court) and concludes that just as a medical employer is entitled to protect its patient base and referral sources from practice by the former employee in private practice in the restricted area, the employer is also entitled to protect its

patient base and referral sources at hospitals by restricting the former employee from practicing at local hospitals. This is significant not only because it represents the first decision in New Jersey to explicitly address this issue, but also because it recognizes medical employers' legitimate interest in patients and referral sources at hospitals, and finds that medical employers may legitimately protect those patients and referral sources from interference from a former employee.

Conclusion

In sum, the recent *Community Hospital* and *Pierson* decisions are significant. While reaffirming the traditional *Karlin v. Weinberg* test for assessing the enforceability of post-employment restrictive covenants between physicians, the cases also demonstrate that courts in this state are aware not only of the unique relationship between physicians and their patients, but are also cognizant of the business realities of a medical practice, the importance of a patient base and referral sources, and the legitimate need of such practices to protect patients and referral sources from erosion by a former employee. And, the cases also demonstrate that, in accordance with *Karlin v. Weinberg*, restrictive covenants may be enforceable for geographical areas spanning some 30 miles, and may also restrict a former employee from practicing at local hospitals.

As noted earlier, recognizing the importance of *More*, the Supreme Court of New Jersey has stayed that decision. Consequently, the full impact of that decision, and of the *Pierson* decision, which was decided after *More*, may not be known until the Supreme Court announces its final pronouncement on these issues. Nonetheless, in the wake of these decisions, it is important for all physicians in this state – whether negotiating an employment agreement, seeking to enforce an employment agreement, or even seeking to avoid restrictions contained in an employment agreement – to be aware of these decisions and the ramifications they may have on the enforceability of restrictive covenants that may be contained in such agreements.

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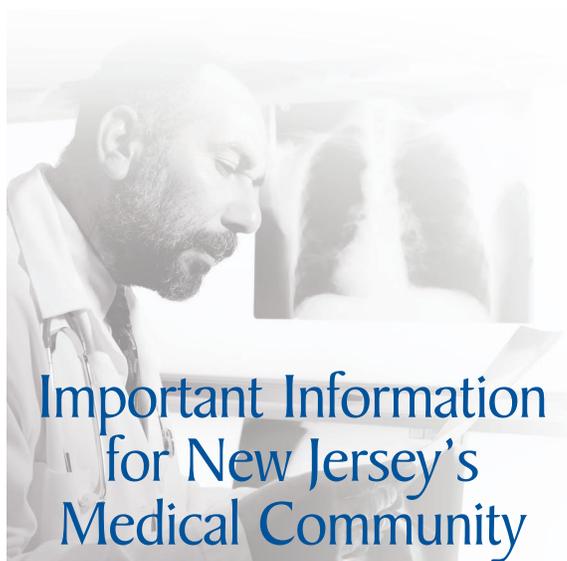
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