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Understanding employment contracts

What docs need to know about restrictive clauses

Twenty years ago, hospitals rarely employed physicians directly. However, today's physicians are increasingly seeking the steady income and predictable schedules associated with being a hospital employee. But before physicians sign any contracts, they should familiarize themselves with the fine print.

Noncompete clauses, restrictive covenants, and nonsolicitation clauses could come back to bite physicians in their wallets if they are unaware of all the implications.

MSB spoke to **Richard Sheff, MD, CMSL,** chair and executive director at The Greeley Company, a division of HCPro, Inc., in Marblehead, MA; **Mike Mainwaring,** vice president of business development at Cleveland Clinic Regional Hospitals; and **Michael Callahan,** an attorney at Katten Muchen Rosenman, LLP, in Chicago to answer some important questions physicians may be too afraid to ask about restrictive clauses.

Q What is the purpose of restrictive clauses?

A The purpose of restrictive clauses in physician-hospital contracts is to protect an organization's monetary investment in recruiting a physician or a group of physicians to the community and helping the individual or group build a practice.

Organizations often offer loan forgiveness, signing bonuses, and financial assistance for the first year or two of practice, which translates into tens of thousands of dollars, says Sheff. If a physician chooses to leave the organization before it has recouped the losses, it would have no way of regaining that investment if it didn't protect itself with appropriate contract language.

Q What's the difference between noncompete, restrictive covenant, and nonsolicitation clauses?

A Noncompete clauses protect an organization's interests by prohibiting physicians from doing business with one of the organization's direct competitors. These restrictions are enforceable for as long as the contract specifies—sometimes even for a period after the contract has been terminated.

Restrictive covenants prevent physicians who leave an organization from doing business within a defined geographic area, says Sheff. This area can be a radius around the organization's primary service site, specified counties, or specified zip codes. The purpose and terms of noncompete clauses and restrictive covenants often overlap, says Mainwaring.

Nonsolicitation clauses prevent a physician from leaving the organization to work for a competitor and subsequently soliciting patients and staff members to follow him or her to the new practice, says Mainwaring.

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HCPro

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Q To whom do such restrictions apply?

A Restrictive clauses apply to physicians or physician groups who are employed by or have exclusive contracts with a hospital or other healthcare organization. They do not apply to licensed independent practitioners because their relationships with hospitals are generally not governed by contracts.

Organizations may choose to apply restrictive clauses only to big-ticket specialties, such as neurosurgery or orthopedic care, which provide the most financial benefits to a hospital. They are not usually used for specialties such as radiology, in which the practitioners don't technically have a patient following and referrals are not likely to be negatively affected, says Callahan.

However, many organizations include restrictive clauses in all their contracts as a safety measure, but that doesn't mean the organization is obligated to enforce the terms of those clauses.

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"Hospitals always have a right to decide whether they want to enforce any term in a contract," says Callahan.

Q Who defines the terms of restrictive clauses?

A There is no cut-and-dry formula for determining what terms are reasonable. Although there are loose market standards, it's up to each hospital's administrative team to define the terms of the noncompete and restrictive covenant clauses, says Callahan.

Administrators make this determination after considering the size of the market, patient population, ease or difficulty of recruiting a physician of that specialty to the market, and numerous other factors, says Sheff.

However, as it becomes more difficult for organizations to recruit physicians due to the nationwide physician shortage, physicians will be in a better position to negotiate more generous terms, says Sheff. Thus, organizations may accept more flexible arrangements in the future.

Q What is a reasonable restriction?

A Noncompete clauses and restrictive covenants often define the geographic area in which a physician is restricted from practicing and the length of time the physician is restricted from practicing in that area. These terms vary depending on the market and specialty.

For example, prohibiting primary care physicians from practicing within a five-mile radius of the organization's primary service site is an example of a reasonable restriction in an urban area, says Mainwaring.

Specialists may be restricted from practicing within a 10-mile radius, simply because they tend to bring in patients from a wider geographic area, he says.

However, in a rural market, the radius for family physicians and specialists might be greater. "In order to support a practice in a rural area, you need to pull patients from a lot further away," Mainwaring says.

As for the duration of the restriction, one year generally does the trick. "If you pull someone out of a market for one year, I think that is accomplishing the goal of a noncompete [clause]. Most physicians don't leave a market for a year and come back—they make a definitive decision to stay or go," Mainwaring says.

Mainwaring adds that the geographic restriction should only include a radius around the organization's primary service site. For example, if a newly recruited internist plans to practice at two offices and at XYZ Hospital, and the contract he or she is about to sign would restrict him or her from competing within 10 miles of the organization, the internist should find out how the contract defines "organization." If the contract defines organization as all sites comprising the healthcare system, a 10-mile restriction can easily turn into a 30-mile restriction should the internist choose to terminate employment.

"You can essentially be blocked from an entire city," says Mainwaring.

A more reasonable approach would be to create a seven-mile restriction around the primary outpatient facility where the internist would be providing care, but not the secondary site or hospital at which he or she provides care. "I think there is a lot of variability in whether organizations count secondary locations, but if I was a physician, I'd fight very hard that it is only for the primary office location," says Mainwaring.

Restricting where physicians can practice and including a one- to two-year buffer allows the organization to find another physician to take the place of the physician who is leaving.

Q Do restrictive clauses affect patients' access to care?

A Usually, courts give noncompete clauses and restrictive covenants a stamp of approval. However, if such clauses will unreasonably restrict patient access to care that would not otherwise be available within the defined geographic market, a court hearing the dispute may rule to not enforce the terms of the noncompete clause or restrictive covenant, says Callahan.

Q Does the hospital leave empty handed if the court sides with the physician?

A Even if a court gives a physician or physician group the green light to compete directly with the organization, that doesn't mean the organization isn't entitled to some monetary damages. That's why organizations include a liquidated damages clause in any employment or exclusive contract.

"The judge may say, 'I'm not going to enforce the restrictive covenant, but I will enforce the liquidated damages clause and this physician must pay you [the organization] $100,000,' " Callahan says.

Q When is it inappropriate to include restrictions in a contract?

A There are only two primary instances when an organization would not include or enforce a restrictive clause in an employment agreement.

If the organization recruits a well-established physician into an employment agreement and he or she brings the value of a full practice with him or her, a noncompete clause or restrictive covenant is not necessary. In this circumstance, the organization would not be financially invested in helping the physician build a practice.

However, if the physician chose to leave, he or she would have to pay the fair market value for the assets and records, "just like the hospital did when it employed him. The physician would have to buy it back," says Mainwaring.

A noncompete clause also wouldn't hold much water in the case of a short-term contract (e.g., less than one year), Mainwaring says.

"The organization is not committing to a long-term relationship with you, so why should you, as a physician, agree to a noncompete clause?" he says.

Q What are the consequences if a physician breaks the terms of a contract?

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A The organization can bring the issue to court and ask a judge to enforce the terms of the contract. The judge would then weigh the terms of the contract and the possible effect on patients' access to care and decide whether it is fair and enforceable.

Most contracts include language that allows courts to change the terms to make it enforceable. For example, if an organization's restrictive clauses bar a physician from practicing within 25 miles of the primary service site, the court might decide that a 10-mile restriction is more reasonable.

Or, the court might deem that a five-year restriction is unfair and choose to enforce the terms of the contract for only one year.

Many organizations also enforce a recruitment payback contract provision in which a physician who chooses to move his or her practice to another location must pay the organization X dollars within one year of being recruited, Y dollars within two years, and Z dollars within three years, says Sheff.

Although some physicians may roll their eyes at a recruitment payback agreement, hospitals generally consider them justifiable.

"For a primary care physician to build a practice, it can take up to three years—and that is just for the hospital to break even," says Mainwaring.

Q Should medical staff bylaws address employment contracts and exclusive contracts?

A Medical staffs should include a provision in the bylaws stating that if there is a contractual arrangement between the hospital and any member of the medical staff, the terms of the contract take precedence over the bylaws, says Callahan. "You don't want to see a provision giving the bylaws precedence over the contract—the governing board would never approve that because it would limit their right to contract [with physicians and physician groups]," Callahan says.

Q What happens to a physician's privileges when he or she is no longer employed by a hospital or part of an exclusive contract group?

A If a physician's employment with a hospital is terminated, the hospital must determine whether to enforce the restrictive clauses in its contract with the physician. If it chooses to enforce them, the physician will lose his or her privileges. However, if the physician and hospital have a good relationship and the physician hasn't presented any quality issues, the hospital may allow the physician to keep his or her privileges and remain a member of the medical staff. "That is usually not a big deal for the hospital because they figure if you're in the community, you're bringing patients to the hospital and helping meet community need," says Sheff.

However, if the physician is part of a group that has an exclusive contract with a hospital, his or her privileges are automatically relinquished as a result of the termination, says Callahan. By keeping the physician on as an independent staff member, the hospital would be breaching its contract with the exclusive group. ■

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