

# RESTRAINTS ON PHYSICIAN COMPETITION IN GEORGIA

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## **I. INTRODUCTION**

Many Georgia physicians are bound by contractual covenants that seek to restrict their ability to compete (non-compete covenants), to solicit patients or referral sources (non-solicitation covenants), to solicit co-workers (non-recruitment covenants), or to use or disclose confidential information (non-disclosure covenants). Restrictive covenants may appear in physicians' employment agreements,<sup>1</sup> partnership agreements,<sup>2</sup> medical director contracts,<sup>3</sup> agreements executed upon the sale of a medical practice,<sup>4</sup> and even real estate leases.<sup>5</sup> Their enforceability will depend in large part upon four factors: (1) the effective date of the agreement containing the covenants; (2) the type of agreement in which they appear; (3) the breadth of the restrictions imposed (time, territory and scope of activities); and (4) for newer covenants, the discretion of a judge.<sup>6</sup>

This article is designed to give physicians (and their advisors) a general appreciation of legal issues associated with physician restrictive covenants in Georgia; it is not intended as a substitute for competent legal advice that considers a physician's unique circumstances. Section II describes the various types of restrictive covenants. Section III provides a brief overview of Georgia's restrictive covenants law prior to the 2011 effective date of the Georgia Restrictive Covenants Act (the "Act" or the "new law"). Section IV describes the sweeping changes brought forth by the Act. Section V analyzes how Georgia courts are likely to treat covenants affecting physicians. Section VI addresses some issues that may arise in litigation involving physician restrictive covenants.

## **II. DESCRIPTION OF THE VARIOUS COVENANTS**

### **A. NON-COMPETE COVENANT**

A covenant not to compete prohibits the employee from performing competitive activities in a certain geographic area for a certain period of time, thereby protecting the employer's "investment of time and money in developing the employee's skills."<sup>7</sup> Thus, a non-compete may prevent an employee from working for a competitor or from accepting competing business (whether solicited or not) from any of the employer's clients (whether previously contacted by him or not) within a given territory.<sup>8</sup>

### **B. CUSTOMER NON-SOLICITATION COVENANT**

A covenant not to solicit prohibits an employee from soliciting some or all of the employer's clients, thereby protecting the employer's investment of time and money in developing customer relationships and goodwill.<sup>9</sup> A non-solicitation covenant that seeks to restrain the former employee from accepting unsolicited business from restricted customers is unreasonable.<sup>10</sup>

### **C. EMPLOYEE NON-SOLICITATION COVENANT**

Many employers require their employees to covenant that they will not solicit or hire away employees of the employer. Like a non-compete covenant, a “non-recruitment covenant” covenant protects the employer’s investment in the development of its employees.<sup>11</sup>

### **D. NON-DISCLOSURE COVENANT**

A non-disclosure covenant places a restraint on the use of confidential business information.<sup>12</sup> It enables employers to protect confidential information beyond that which is already protected by the Georgia Trade Secrets Act.<sup>13</sup> A trade secret is “information, without regard to form, including, but not limited to, technical or nontechnical data, a formula, a pattern, a compilation, a program, a device, a method, a technique, a drawing, a process, financial data, financial plans, product plans, or a list of actual or potential customers or suppliers which is not commonly known by or available to the public.”<sup>14</sup> In order to be a trade secret the information must derive economic value and be subject to reasonable efforts to maintain its secrecy.<sup>15</sup>

## **III. PRE-STATUTORY RESTRICTIVE COVENANTS LAW**

In 2011, the Georgia General Assembly adopted the Georgia Restrictive Covenants Act as a comprehensive statutory framework applicable to restrictive covenants.<sup>16</sup> The Act in many ways legislatively overrules the large body of law developed by the Georgia courts on this subject (the “old law”). The General Assembly adopted the Act in response to the perception that Georgia courts’ hostility towards restrictive covenants was placing Georgia at a competitive disadvantage with other states. Because the new law was a reaction to the old law, and because the old law still applies to contracts executed before the effective date of the new law (May 11, 2011), a discussion of the old law is warranted.

The Georgia Constitution declares void on public policy grounds any contract which “may have the effect of or which is intended to have the effect of defeating or lessening competition.”<sup>17</sup> Although restrictive covenants lessen competition to some degree by their very nature, they do not violate the Georgia Constitution in all cases.<sup>18</sup> Accordingly, Georgia courts will enforce restrictive covenants that are: (1) reasonable in scope; (2) supported by consideration; (3) reasonably necessary to protect the restraining party’s interests; and (4) not unduly prejudicial to the interests of the public.<sup>19</sup>

The reasonableness of a restrictive covenant has always been a question of law for the court, considering the nature and extent of the trade or business, the situation of the parties, and all other relevant circumstances.<sup>20</sup> “A three-element test of duration, territorial coverage, and scope of activity has evolved as a ‘helpful tool’ in examining the reasonableness of the particular factual setting to which it is applied.”<sup>21</sup> This is a flexible

and imprecise test. For example, if a non-solicit is narrowly drawn to prevent a former employee from soliciting only those customers with whom he had contact and only for the purpose of competing with the former employer, a court will be more indulgent of a longer durational limit or larger geographic restriction.<sup>22</sup>

The single most important factor in the analysis of restrictive covenants under the old law is the level of scrutiny applied by the court because that often dictates whether an overbroad covenant will be struck down or judicially modified.

## 1. THE THREE LEVELS OF SCRUTINY

Georgia courts have traditionally applied three levels of scrutiny to restrictive covenants. As a general rule, they apply strict scrutiny to covenants contained in employment agreements, mid-level scrutiny to covenants contained in partnership agreements, and slight scrutiny to covenants contained in agreements concerning the purchase or sale of an interest in a business.<sup>23</sup> Covenants in independent contractor agreements are treated like covenants in employment agreements,<sup>24</sup> and covenants in medical director agreements are subject to the same mid-level scrutiny as partnership agreements.<sup>25</sup>

The different levels of scrutiny are intended to correspond to the differences in the parties' bargaining power. A physician who is merely seeking employment with a medical practice is presumed to have less bargaining power than a physician who is negotiating for an interest in a partnership, and even less still than a physician who is selling his practice to a purchaser.<sup>26</sup> The inquiry into the parties' relative bargaining power is often fact intensive. In West Coast Cambridge, Inc. v. Rice, for example, the Court of Appeals applied slight scrutiny to covenants in a physician partnership agreement because it found that the affected physician did not actively practice medicine and, as such, was more like a passive investor in the partnership.<sup>27</sup>

The more complex the relationships between the parties, the more difficult it becomes to navigate the scrutiny levels. What happens, for example, if a physician sells his or her interest in a practice but agrees to become a practice employee? In that situation, the physician may execute an asset sale agreement and an employment agreement as a part of the same transaction. And what happens if there is a covenant in one agreement but not the other, or if the two agreements contain inconsistent covenants? As shown below, the case law was hopelessly inconsistent.

Example 1: A stock purchase agreement and employment agreement executed simultaneously as a part of the same transaction, but only the employment agreement contained restrictive covenants. The Court of Appeals applied *slight* scrutiny – even though the covenants were contained in an employment agreement – because the employee had considerable bargaining power and he delivered the covenants as a precondition to the stock purchase agreement.<sup>28</sup> In so ruling, the court mentioned, but did

not overrule, an earlier case in which it applied *strict* scrutiny on the very same facts.<sup>29</sup>

Example 2: Asset purchase agreement (containing non-compete) and employment agreement (expressly incorporating non-compete and adding additional non-solicit and non-disclosure covenants) are executed simultaneously as a part of the same transaction. Applying Georgia law, the Eleventh Circuit applied *slight* scrutiny to *all* of the covenants because the asset sale was conditioned upon the subsequent employment and because all of the covenants “were a part of a unitary contractual scheme.”<sup>30</sup>

Example 3: Asset purchase agreement and employment agreement are executed as a part of the same transaction, but they contain *conflicting* non-compete covenants (i.e., the scope of the competing covenants is different). The court applied *strict* scrutiny to the covenants in the employment agreement and *slight* scrutiny to the covenants in the asset purchase agreement.<sup>31</sup>

Example 4: Physician’s wife sells dialysis clinic and, at the same time, her husband executes a medical director agreement with the purchaser. The asset purchase agreement restricts the wife’s ability to operate a competing facility for 10 years within a 40 mile radius, and the medical director agreement precludes the physician from operating a dialysis center for 2 years within a 40 mile radius. Although a medical director agreement by itself would be subject to mid-level scrutiny, the court applied *slight* scrutiny to *all* of the covenants because they were a part of the same transaction and the physician was “integral to the continued success” of the facility.<sup>32</sup>

Perhaps the only lesson to be learned from these irreconcilable holdings is that it is difficult to predict the scrutiny level in these types of hybrid transactions. On the one hand, a mechanical application of the scrutiny level based upon type of agreement (employment agreement, partnership agreement or business sale agreement) may offer some predictability to the parties. But on the other hand, that methodology undercuts the very reason for having different scrutiny levels in the first place – to level the playing field in differences in the parties’ relative bargaining power. It is difficult to conceive that a physician who sells his or her interest in a medical practice and simultaneously executes an employment agreement with the buyer has more bargaining power in the first agreement than in the second. While this uncertainty may keep transactional lawyers awake at night, it is a boon for litigators.

## 2. BLUE PENCIL RULE

What do strict scrutiny, mid-level scrutiny and slight scrutiny mean in practical terms? The most readily identifiable distinction is that a court applying strict scrutiny will not “blue pencil” an overbroad covenant to make it enforceable, but will instead strike down the entire covenant.<sup>33</sup> Under strict scrutiny, an entire non-compete is doomed even if it is only a discrete subsection of the non-compete that is overbroad.<sup>34</sup>

On the other hand, courts exercising mid-level scrutiny (partnership agreements) or slight scrutiny (business sale agreements) may limit unreasonably broad restrictions.<sup>35</sup> There are limits to this so called “blue pencil rule,” because while courts may strike or modify offensive terms in a covenant, they may not supply missing terms to make the covenant less vague.<sup>36</sup>

It is important to note that under strict scrutiny, non-compete and non-solicitation covenants stand or fall together, while non-recruitment and nondisclosure covenants are evaluated separately from the rest of the covenants.<sup>37</sup> For example, an invalid non-solicitation covenant would invalidate an otherwise valid non-compete, but it would not invalidate an otherwise valid non-disclosure agreement.<sup>38</sup> A severability clause is not a panacea. While it would allow the court to excise the entire restrictive covenant in order to preserve the balance of the agreement,<sup>39</sup> it cannot save a reasonable non-solicit from an unreasonable non-compete and vice versa.<sup>40</sup>

### **3. OTHER DIFFERENCES IN SCRUTINY LEVELS**

Aside from the blue pencil rule, there are few concrete differences between the scrutiny levels. One difference is that a non-compete covenant may be unlimited in time under both mid-level and slight scrutiny, but not under strict scrutiny.<sup>41</sup> Another difference is that a covenant prohibiting a professional from providing similar services to any organization, whether or not that organization competes with the professional’s former employer, will fail strict scrutiny but survive mid-level scrutiny.<sup>42</sup>

A third difference is the degree to which a court will consider post-execution events when evaluating the reasonableness of the covenants. A court applying strict scrutiny will consider such evidence if it tends to show that the covenant is unreasonable.<sup>43</sup>

## **IV. THE RESTRICTIVE COVENANTS ACT**

In 2011, the Georgia General Assembly adopted a comprehensive statutory framework applicable to restrictive covenants.<sup>44</sup> The Act replaced the three levels of scrutiny with statutory guideposts that are rebuttably presumed to be reasonable. The Act also allows for blue penciling for any covenant deemed to be overly broad. As discussed in more detail below, covenants are more likely to survive under the new law than under the old law.

### **A. THE EFFECTIVE DATE**

Much has been written about the confusion surrounding the effective date of the Restrictive Covenants Act, so it will not be covered in detail here. The General Assembly originally passed a restrictive covenants bill (HB 173) in November 2009, before the bill was constitutionally authorized.<sup>45</sup> HB 173 stated that it would become

effective the day after the Georgia voters ratified a constitutional amendment authorizing the Act.<sup>46</sup> Georgia voters ratified the amendment on November 2, 2010, but the amendment itself did not contain an effective date.<sup>47</sup> In that situation, the Georgia Constitution provides that the amendment does not take effect until January 1 of the following year, in this case January 1, 2011.<sup>48</sup> Thus, HB 173 became effective before the amendment authorizing the bill became effective. To remedy that problem, the General Assembly adopted a new restrictive covenants bill (HB 30) which would become effective upon the date it was signed by the Governor.<sup>49</sup> HB 30 expressly provides that it does not apply in actions concerning covenants executed before HB 30 was signed into law.<sup>50</sup>

The Governor signed HB 30 into law on May 11, 2011. Thus, it is now clear that any agreement executed after that date is governed by Georgia's Restrictive Covenants Act (HB 30).<sup>51</sup> The Georgia Supreme Court has since held that the new law "does not apply to contracts entered into before May 11, 2011."<sup>52</sup> Thus, May 11, 2011, is a clear line drawn in the sand which separates the old and new law and, in many cases, determines the fate of the covenant. Accordingly, employers should immediately replace pre-May 11, 2011 covenants in order to take advantage of the pro-employer aspects of the new law. Some employers have asked departing employees to "reaffirm" their pre-May 11, 2011 covenants in post-May 11, 2011 severance agreements in an effort to take advantage of the new law. For this to succeed, the employer must write the covenants into the new agreement rather than merely reference the old agreement because an employee cannot "ratify" covenants that were invalid at the time of execution.<sup>53</sup>

## **B. APPLICABILITY**

The Restrictive Covenants Act only applies to covenants between or among: (1) employers and employees; (2) distributors and manufacturers; (3) lessors and lessees; (4) partnerships and partners; (5) franchisors and franchisees; (6) sellers and purchasers of a business; and (7) two or more employers.<sup>54</sup> Thus, the Act covers physicians who execute covenants within employment agreements, covenants within partnership agreements, and covenants within agreements to buy or sell a medical practice.

It is unclear whether the Act applies to medical director agreements. Because "employer" is defined to include any person or entity that conducts business, or any person or entity that owns or controls 25 percent of such entity,<sup>55</sup> a covenant in a medical director agreement could arguably be a covenant between "two employers." If the medical director agreement is not covered by O.C.G.A. § 13-8-2, it would be analyzed under Georgia common law.<sup>56</sup>

## **C. THE BLUE PENCIL RULE**

The Restrictive Covenants Act goes to great lengths to correct perceived injustices in the common law by stating that covenants shall be interpreted "to comport with the

reasonable intent and expectations of the parties.”<sup>57</sup> In a dramatic departure from the common law, however, the Act gives the courts the power to “modify” or “blue pencil” overly broad covenants in employment agreements that would have been struck down altogether under the old law.<sup>58</sup>

The Act’s definition of “modification” seems to import the time-honored prohibition against reforming ambiguous covenants:

“Modification” means the limitation of a restrictive covenant to render it reasonable in light of the circumstances in which it was made. Such term shall include:

- (A) Severing or removing the part of the restrictive covenant that would otherwise make the entire restrictive covenant unenforceable; and
- (B) Enforcing the provisions of a restrictive covenant to the extent that the provisions are reasonable.<sup>59</sup>

In Pointenorth Ins. Group v. Zander, the district court held – in an order granting an employer a preliminary injunction under the new law – that a covenant prohibiting a former employee from soliciting any of the employer’s customers was overly broad because it was not limited to those customers with whom the employee had contact.<sup>60</sup> The court wrote that it could “remedy that finding by blue penciling the provision to only apply to customers that the Defendant contacted and assisted with insurance.”<sup>61</sup>

## V. ENFORCEMENT OF PHYSICIAN RESTRICTIVE COVENANTS

The likelihood that a Georgia court will enforce each of the four covenants is discussed below, with special emphasis devoted to unique issues likely to confront physicians.

### A. NON-COMPETE COVENANTS

#### 1. TIME

Under the old law, two years are routinely found to be reasonable for non-compete covenants covering former employees.<sup>62</sup> Longer periods may also be enforceable, especially if the scope of the restrictions is narrow.<sup>63</sup> Provisions stating that covenants are tolled during the time the employee was in breach are unenforceable.<sup>64</sup>

The Restrictive Covenants Act establishes a rebuttable presumption of reasonableness for non-compete covenants lasting *two* years as to employees, *three* years as to lessees, distributors, franchisees and the like, and *five* years as to the sellers of partnership and business interests.<sup>65</sup> With respect to the business or partnership interest,



the length of time that the seller/partner continues to receive payments on the sale is also presumptively reasonable.<sup>66</sup> Thus, an agreement that spreads payments out over a 10 year period could restrain competition for at least ten years.

## 2. SCOPE

There are a number of decisions under the old law that invalidated non-compete covenants because the scope of restricted activities was either ambiguous or overreaching. With limited exceptions, the new law does not purport to allow for broader restrictions on activities. It does, however, forgive common drafting mistakes that would have doomed covenants under the old law. As just one example, O.C.G.A. § 13-8-53(c)(2) provides that, “[a]ctivities, products, or services shall be considered sufficiently described if a reference to the activities, products, or services is provided and qualified by the phrase ‘of the type conducted, authorized, offered, or provided within two years prior to termination’ or similar language.” Such a covenant could not have survived strict scrutiny under the old law.<sup>67</sup>

O.C.G.A. § 13-8-56(3) makes one important substantive challenge in the law. It provides that “[t]he scope of competition restricted is measured by the business of the employer or other person or entity in whose favor the restrictive covenant is given.” This provision seems to legislatively overrule the line of cases that refused to enforce non-compete covenants that barred the employee from working for a competitor in any capacity.<sup>68</sup> Perhaps the only safeguard against such overreaching is O.C.G.A. § 13-8-58(d), which allows (but does not require) the court to consider the “economic hardship imposed upon an employee by enforcement of the covenant.”

## 3. TERRITORY

A territorial restriction has always been required for enforcement of a non-compete covenant.<sup>69</sup> That has not changed under the new law.<sup>70</sup> Almost everything else has.

While the old law required the territory and scope of activities to be fixed at the time the agreement was executed,<sup>71</sup> the new law takes a much more lenient approach. Thus, the term “territory where the employee is working at the time of termination” is now sufficiently definite for enforcement.<sup>72</sup>

Under the old law, the reasonableness of a territorial restriction was measured by the territory the *employee* serviced during the term of his employment. For example, if a hospital has three locations that draw from patients from 10 counties, but the physician only works at a single location that draws from three counties, the hospital could only restrict the physician from competing within those three counties.<sup>73</sup> Now, the geographic area in which the *employer* does business is reasonable so long as the total distance encompassed is also reasonable and/or the agreement contains a list of particular

competitors that are off-limits.<sup>74</sup> This is a substantial change because it allows for the employer to be protected even in areas the employee never serviced.

What is a reasonable territorial restriction? Many physician non-compete covenants express the territory in terms of miles from a set location (typically the facilities in which the physician worked). In Pittman v. Harbin Clinic, P.A., the court upheld a covenant prohibiting the physician shareholders (midlevel scrutiny) from “practicing medicine” within 30 miles of Rome, Georgia because the clinic established that this was the region from which the clinic drew its patients.<sup>75</sup> Importantly, the court also stated that 50-mile restrictions on non-shareholder physicians (strict scrutiny) were not per se unreasonable, though they were unenforceable in that case because they exceeded the territory of the clinic’s practice.<sup>76</sup>

It is also permissible to restrict a physician from competing in specified counties.<sup>77</sup> In McAlpin v. Coweta Fayette Surgical Assoc., the Court of Appeals upheld a covenant in a physician employment agreement prohibiting him from practicing competing and/or practicing medicine or surgery for two years within Coweta, Fayette, Fulton, Heard, Meriwether, Carroll, Clayton, Spalding, Troup and Pike Counties.<sup>78</sup> The McAlpin court found the covenant reasonable because: (1) while the employer had locations in Coweta and Fayette Counties, it drew patients from all 10 restricted counties; (2) residents of the 10 restricted counties could still travel to another county for treatment by the physician; and (3) the last census revealed that the combined population of Cobb, DeKalb and Gwinnett Counties exceeded that of the 10 restricted counties.<sup>79</sup>

Thus, a physician can expect that a non-compete in an employment agreement will be upheld if it restricts the practice of medicine within 10 counties or within 50 miles of a set location.

## **B. CUSTOMER NON-SOLICITATION COVENANTS**

Under the old law, a customer non-solicitation covenant with no geographic restriction must be limited to the customers with whom the employee had material contact. In Trujillo v. Great Southern Equipment Sales, LLC, for example, the Court of Appeals struck down a covenant that prohibited a former employee’s solicitation of customers about whom he obtained confidential information because the employee might not have had material contact with those customers.<sup>80</sup>

At first glance, O.C.G.A. § 13-8-53(b) seems to preserve the material contact requirement from the Trujillo decision by providing that an employee may agree not to solicit customers/patients with whom he or she had “material contact”. But a closer examination reveals that the Act legislatively overrules Trujillo by defining “material contact” broadly to cover situations in which employee “obtained confidential information” about the customer/patient.<sup>81</sup> The practical effect is that a physician who merely reviews a patient’s medical records but has no direct contact with the patient can

now be barred from soliciting that patient.

A typical physician non-solicitation covenant reads as follows:

During Physician's employment and for two years thereafter, Physician shall not, directly or indirectly, solicit, divert, or take away any patients who were treated by Physician during his employment, for the purpose of providing or offering to provide medical services to those patients.

That non-solicitation covenant gives rise to several issues. First, how is the term "patient" defined? If it could be construed to include former patients, the covenant may be overly broad. In a case including restrictions on an insurance broker, the Court of Appeals held that the brokerage firm does not have a protectable interest in protecting former customers.<sup>82</sup> The Restrictive Covenants Act does not appear to have changed this rule.<sup>83</sup>

It is much easier to distinguish between customers and former customers in the insurance business than it is in the healthcare field. In the insurance business, a former customer is one who declined to renew its insurance policies before the employee's departure.<sup>84</sup> If an orthopedic surgeon treats a patient's broken leg, does the patient become a "former patient" once he is released from further treatment? Is a cancer patient who comes out of remission a former patient or a new patient? These are questions that the courts will likely have to answer.

Another question the sample non-solicitation covenant raises is what is "solicitation?" The Act does not define the term, but Georgia case law has held that solicitation requires an affirmative act beyond the mere acceptance of business.<sup>85</sup> If a departing physician sends a notice merely apprising his patients of his new address, is that solicitation? In Robert, LTD v. Parker, the court held that a jury should decide whether a former employee's letters to former clients *and* offers of assistance constituted solicitation.<sup>86</sup> While no Georgia court has decided whether a mere notice of change of address is a solicitation, one Atlanta area hospital has taken that position. Relatedly, it is unlikely that a physician could generate patient notices without first accessing a patient list, which could expose the physician to a theft of trade secrets claim.<sup>87</sup>

The American Medical Association has addressed the issue of patient notices squarely:

The patients of a physician who leaves a group practice should be notified that the physician is leaving the group. Patients of the physician should also be informed of the physician's new address and offered the opportunity to have their medical records forwarded to the departing physician at

his or her new practice location. *It is unethical to withhold such information upon request of a patient.* If the responsibility of notifying patients falls to the departing physician, rather than to the group, the group should not interfere with the discharge of these duties by withholding patient lists or other necessary information. (Emphasis added)<sup>88</sup>

While AMA opinions lack the force of law, they may shame a recalcitrant hospital or practice to put patient care and professionalism above economic gain.

### C. NON-RECRUITMENT COVENANTS

Because the Restrictive Covenants Act does not expressly mention non-recruitment covenants, it is unclear if they are even covered by the Act. They are arguably contemplated in O.C.G.A. § 13-8-51(15), which defines “restrictive covenant” as any agreement between two parties to protect the first party’s interest in, among other things, employees. On the other hand, non-compete covenants also protect the employer’s interest in employees,<sup>89</sup> so the Act’s applicability to non-recruitment covenants is by no means clear.

To the extent they are covered under the Restrictive Covenants Act, non-recruitment covenants should be treated no differently than non-compete covenants, which require geographic and time restrictions.<sup>90</sup> Alternatively, non-recruitment covenants could be evaluated under the old law, which requires a territorial restriction<sup>91</sup> and which prohibits application of a non-recruitment covenant to all employees, regardless of position or tenure.<sup>92</sup>

The courts will likely have to clarify whether the Restrictive Covenants Act applies to non-recruitment covenants.

### D. NON-DISCLOSURE COVENANTS AND INEVITABLE DISCLOSURE

Courts apply a two factor test to non-disclosure agreements: (1) whether the employer intends to protect confidential information regarding the business, including: trade secrets, operational methods, customer names and personnel data and (2) whether the covenant relates to protecting such information.<sup>93</sup> In a change from the prior law, a non-disclosure agreement can now be enforced into perpetuity so long as the information remains confidential.<sup>94</sup>

The wording of the confidentiality covenant is critical because an employer has no right to restrict the use of publicly available information. Thus, a court will uphold a covenant that prevents the employee from using *confidential* information, but it will invalidate a covenant that bars the employee from using *any* information relating to the

employer's business.<sup>95</sup> The Restrictive Covenants Act likely remedied this situation because it allows the court to blue pencil the covenant so that it only applies to non-public information.<sup>96</sup>

In the medical field, a non-disclosure covenant would typically protect a variety of sensitive information such as patient medical information, patient names and contact information, insurance reimbursement rates, referral sources and strategic plans. When a physician departs, the handling of patient health records can be a source of controversy. While the provider (employer) is the owner of patient health records, it is clear that the patient has the right to obtain a copy of his records.<sup>97</sup> The best approach is for the patient to execute a release authorizing the departing physician to take the records with him. Any interference with the patient's request for medical records is unlawful.<sup>98</sup>

While a court might decline to enforce a non-compete covenant with a nationwide scope, it could enforce a confidentiality covenant (without any geographic restriction) to prevent an employee from working for a competitor because he cannot do so without using or disclosing the former employer's confidential information.<sup>99</sup> In that sense, a non-disclosure covenant can serve as a de facto non-compete covenant.<sup>100</sup>

Relatedly, the inevitable disclosure doctrine provides that "a plaintiff may prove a claim of trade secret misappropriation by demonstrating that defendant's new employment will inevitably lead him to rely on the plaintiff's trade secrets."<sup>101</sup> In those jurisdictions that have adopted the doctrine, courts consider whether: (1) the employers are direct competitors providing similar products or services; (2) the employee's position with the new employer has responsibilities similar to the position held with the former employer; (3) the employee will be unable to complete those responsibilities without relying on the former employer's trade secrets; and (4) the trade secrets are valuable to both employers.<sup>102</sup> Many courts also consider the employee's bad faith conduct or intent to disclose trade secrets.<sup>103</sup>

It is doubtful that the inevitable disclosure doctrine is viable in Georgia. In Essex Group v. Southwire Co., Essex hired away from its direct competitor (Southwire) an employee who led a team that developed a trade secret-protected logistics system.<sup>104</sup> Though the Georgia Supreme Court did not find that the employee took tangible materials from Southwire, it acknowledged that he possessed trade secrets within his memory, and it upheld the injunction barring him from working for Essex on that basis, seemingly adopting – implicitly at least – the inevitable disclosure doctrine.<sup>105</sup> In 2013, however, the Supreme Court in Holton v. Physician Oncology Services, L.P. rejected the notion that Essex adopted the inevitable disclosure doctrine, holding that "a stand-alone claim for the inevitable disclosure of trade secrets – untethered from the provisions of our state trade secret statute – is not cognizable in Georgia."<sup>106</sup> The Holton court reserved ruling on whether the inevitable disclosure doctrine could apply to support a claim for the threatened misappropriation of trade secrets.<sup>107</sup> This statement raises more questions than it answers since the Georgia Trade Secrets Act already authorizes injunctive relief

for threatened misappropriation.<sup>108</sup>

## VI. POTENTIAL EMPLOYER VULNERABILITIES UNDER THE NEW LAW

There is little for employees to like in the Restrictive Covenants Act. It legislatively overrules much of the pro-employee case law and it now allows courts to blue pencil agreements instead of striking them down in their entirety. The justification for disallowing such modifications had always been to discourage employers from “fashioning overly broad covenants that will remain unchallenged in most instances.”<sup>109</sup> Now employers have every incentive to do just that. For example, under the old law, many savvy employers chose not to demand non-compete covenants because they were so difficult to enforce and because an invalid non-compete would doom an otherwise valid non-solicitation covenant.<sup>110</sup> That is no longer the case. Now a valid non-solicitation covenant will survive even if the non-compete covenant is struck down or, more likely, judicially modified.<sup>111</sup>

There are potentially two bright spots for employees. The first requires a person or entity seeking to enforce a covenant “to plead and prove the existence of one or more legitimate business interests justifying the restrictive covenant.”<sup>112</sup> This is hardly an onerous burden since the employer will likely describe the business interest in the agreement and require the employee to acknowledge its legitimacy.<sup>113</sup> Nevertheless, O.C.G.A. § 13-8-55 may give a court the statutory justification it seeks to strike down or curtail a covenant.

The second bright spot for employees is somewhat brighter. O.C.G.A. § 13-8-58(d) permits the court, when assessing the reasonableness of a covenant, to “consider the economic hardship imposed upon an employee.” The economic hardship argument is only available to employees; it does not benefit business sellers, partners, distributors, franchisees or the like.<sup>114</sup> This is perhaps the only provision in the Act that puts employers at risk for extracting unreasonable covenants from employees, but that risk is mitigated because covenants that do impose an economic hardship on the employee can always be blue penciled.<sup>115</sup>

While the Restrictive Covenants Act offers little assistance to employees, traditional equitable principles may continue to be a valuable resource since employers’ preferred relief is typically injunctive. One potent equitable principle is that one who seeks equity must do equity. In Morgan Stanley DW, Inc. v. Frisby, for example, the district court refused Morgan Stanley’s request for a preliminary injunction because it had unclean hands, holding “Morgan Stanley regularly hires brokers from competitors and, in so doing, engages in the very same practices that it challenges here.”<sup>116</sup>

A second equitable principle helpful to an employee is that party seeking injunctive relief must demonstrate irreparable harm and no adequate remedy at law. Thus, in Morgan Stanley, *supra*, the court declined to enter injunctive relief, ruling that

Morgan Stanley's injury is a loss of commissions, which are easily traceable in the highly regulated brokerage industry, and which can be remedied through money damages.<sup>117</sup> A physician could make the same argument since fees for services are typically governed by Medicare and private insurance reimbursement rates, thus making the employer's losses easy to quantify.

## VII. CONCLUSION

In the wake of the recently adopted Restrictive Covenants Act, Georgia courts are now more likely than ever to enforce restrictive covenants against physicians. Consequently, physicians are well advised to consult with competent legal counsel before executing covenants.

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<sup>1</sup> McMurray v. Bateman, 221 Ga. 240, 241, 144 S.E.2d 345 (1965).

<sup>2</sup> Rash v. Toccoa Clinic Medical Assocs., 253 Ga. 322, 323, 320 S.E.2d 170 (1984).

<sup>3</sup> Davita, Inc. v. Othman, 270 Ga. App. 93, 96, 606 S.E.2d 112 (2004).

<sup>4</sup> West Coast Cambridge, Inc. v. Rice, 262 Ga. App. 106, 109-110, 584 S.E.2d 696 (2003).

<sup>5</sup> Davita, Inc., 270 Ga. App. at 93.

<sup>6</sup> It is no small irony that restrictive covenants, while permitted against doctors, are prohibited against attorneys under the theory that there should be no interference with a client's choice for legal representation. See Georgia Rule of Professional Conduct 5.6, and cmt. 1. In a non-binding opinion, the American Medical Association discourages non-compete covenants for physicians because they "restrict competition, disrupt continuity of care, and potentially deprive the public of medical services." See American Medical Association Opinion No. 9.02 (<http://www.ama-assn.org/ama/pub/physician-resources/medical-ethics/code-medical-ethics/opinion902.page>) (last downloaded May 15, 2013). Nevertheless, Georgia courts have expressly ruled that physician covenants do not violate the state's public policy or conflict with medical ethical principles. Rash v. Toccoa Clinic Medical Assoc., 253 Ga. 322, 326, 320 S.E.2d 170 (1984) (rejecting public policy attack on physician covenant). See also Pittman v. Harbin Clinic, P.A., 210 Ga. App. 767, 770, 437 S.E.2d 619 (1993) (physician covenants do not injure the public in general or conflict with medical ethical principles). Cf. Shankman v. Coastal Psychiatric Assoc., 258 Ga. 294, 368 S.E.2d 753 (1988) (Smith, J., dissenting) ("I would hold restrictive covenants in a medical contract illegal per se as against the strong public policy [to protect the health of its citizens and to regulate those professionals that it licenses] irrespective of whether the covenant is reasonable").

<sup>7</sup> Habif, Arogeti & Wynne, P.C. v. Baggett, 231 Ga. App. 289, 294, 498 S.E.2d 346 (1998).

<sup>8</sup> Id.

<sup>9</sup> Id.

<sup>10</sup> H&R Block Eastern Enterprises, Inc. v. Morris, 606 F.3d 1285, 1291 (11th Cir. 2010).

<sup>11</sup> Palmer & Cay of Georgia, Inc. v. Lockton Companies, Inc., 280 Ga. 479, 481, 629 S.E.2d 800 (2006).

<sup>12</sup> Durham v. Stand-by Labor of Ga., Inc., 230 Ga. 558, 563, 198 S.E.2d 145 (1973).

<sup>13</sup> O.C.G.A. § 10-1-760, *et seq.*

<sup>14</sup> O.C.G.A. § 10-1-761(4).

<sup>15</sup> Id.

<sup>16</sup> O.C.G.A. § 13-8-50, *et seq.*

<sup>17</sup> Ga. Const. of 1983, Art. III, Sec. VI, Para. V(c). This provision was amended in 2010 to specifically allow for the enforcement of certain restrictive covenants as provided in the Georgia Restrictive Covenants Act, O.C.G.A. § 13-8-50, *et seq.*

<sup>18</sup> W.R. Grace & Co. v. Mouyal, 262 Ga. 464, 465, 422 S.E.2d 529 (1992).

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- <sup>19</sup> Id.
- <sup>20</sup> Id.
- <sup>21</sup> Id.
- <sup>22</sup> See, generally, Gale Indus. v. O’Hearn, 257 Ga. App. 220, 223, 570 S.E.2d 661 (2002).
- <sup>23</sup> New Atlanta Ear, Nose & Throat Associates v. Pratt, 253 Ga. App. 681, 683, 560 S.E.2d 268 (2002).
- <sup>24</sup> See Jenkins v. Jenkins Irrigation, Inc., 244 Ga. 95, 97–98, 259 S.E.2d 47 (1979).
- <sup>25</sup> Martinez v. DaVita, Inc., 266 Ga. App. 723, 598 S.E.2d 334 (2004).
- <sup>26</sup> Id. at 684.
- <sup>27</sup> 262 Ga. App. 106, 109-110, 582 S.E.2d 696 (2003).
- <sup>28</sup> American Control Systems, Inc. v. Boyce, 303 Ga. App. 664, 668, 694 S.E.2d 141 (2010).
- <sup>29</sup> Watkins v. Avnet, Inc., 122 Ga. App. 474, 476-77, 177 S.E.2d 582 (1970) (“Although the contract here involved is clearly related to the sale of a business, and in this sense involves only one aspect of a larger transaction, it is nonetheless a contract of employment, and must be construed under the rules applicable to the latter”).
- <sup>30</sup> Mohr v. Bank of New York Mellon Corp., 371 Fed. Appx. 10, 16, 2010 WL 1063856 (11th Cir. 2010). See also Clower v. Orthalliance, Inc., 337 F. Supp. 2d 1322 (2004) (identical covenants in business sale agreement and employment agreements were reviewed under *slight* scrutiny because the employment agreements “are manifestly part of the sale of the business”).
- <sup>31</sup> Hilb, Rogal & Hamilton Co. v. Holley, 284 Ga. App. 591, 595-96, 644 S.E.2d 862 (2007) (“[W]hen parties execute separate contracts for the seller’s sale of the business and the seller’s subsequent employment and each contract contains different restrictive covenants, the restrictive covenants in the employment contract are subject to *strict* scrutiny”). Accord Russell Daniel Irrigation Co. v. Coram, 237 Ga. App. 758, 759, 516 S.E.2d 804 (1999) (“Subjecting two covenants to different treatment, even though found in agreements executed as a part of the same transaction, is consistent with the rationale behind the various levels of scrutiny”). See also Hix v. Aon Risk Services South, Inc., 2011 WL 5870059 (N.D. Ga. 2011) (on same facts, court held “[t]he obvious answer is that each covenant stands on its own. Each covenant is separate and distinct.”)
- <sup>32</sup> Martinez v. DaVita, Inc., 266 Ga. App. 723, 727, 598 S.E.2d 334 (2004).
- <sup>33</sup> Baggett, 231 Ga. App. at 289-290.
- <sup>34</sup> See, e.g., T.E. McCutcheon Enter., Inc. v. Snelling & Snelling, Inc., 232 Ga. 609, 212 S.E.2d 319 (1974).
- <sup>35</sup> Hudgins v. Amerimax Fabricated Prods., 250 Ga. App. 283, 287-8, 551 S.E.2d 393 (2001).
- <sup>36</sup> Pratt, 253 Ga. App. at 687 (blue pencil rule could not supply a *missing* geographic restriction but it could reduce a territory that, while described clearly in the agreement, was simply too large to be enforced).
- <sup>37</sup> Sunstates Refrigerated Svcs. v. Griffin, 215 Ga. App. 61, 62-63, 449 S.E.2d 858 (1994).
- <sup>38</sup> Id.
- <sup>39</sup> Circle Appliance Leasing v. Appliance Warehouse, 206 Ga. App. 405, 425 S.E.2d 339 (1992).
- <sup>40</sup> Johnstone v. Tom’s Amusement Co., 228 Ga. App. 296, 297-8, 491 S.E.2d 394 (1997).
- <sup>41</sup> Jenkins, 244 Ga. at 98.
- <sup>42</sup> Baggett, 231 Ga. App. at 294 (public accounting firm’s non-compete, which prevented CPA from accepting an “in house” accounting position with a company such as Coca-Cola or the Varsity, survived mid-level scrutiny but would have failed strict scrutiny).
- <sup>43</sup> Peachtree Fayette Women’s Specialists, LLC v. Turner, 305 Ga. App. 60, 64, 699 S.E.2d 69 (2010) (applying strict scrutiny, court struck down a covenant that identified three hospitals the physician would be working in because, as it turned out, she only worked in two of the three hospitals). Cf. Habif, 231 Ga. App. at 294 (under mid-level scrutiny, fact that employee only worked in 9 of the 11 restricted counties at the time of his termination did not render the covenant overbroad because “the law does not require exact precision”).



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<sup>44</sup> O.C.G.A. § 13-8-50, *et seq.*

<sup>45</sup> 2009 Ga. Laws, Act 64 (HB 173).

<sup>46</sup> Id.

<sup>47</sup> Id.

<sup>48</sup> Ga. Const. of 1983, Art. 10, Sec. 1, Para. 6.

<sup>49</sup> 2011 Ga. Laws, Act 99 (H.B. 30), § 4.

<sup>50</sup> 2011 Ga. Laws, Act 99 (H.B. 30), § 5.

<sup>51</sup> Becham v. Synthes USA, 482 Fed. Appx. 387 (11th Cir. 2012) (applying Georgia law). In Becham, the Northern District of Georgia declared HB 173 unconstitutional because it was not constitutionally authorized at the time it was passed, thus providing persuasive authority for the proposition that any agreement executed before the November 3, 2010 constitutional authorization is governed by Georgia’s preexisting common law. Id. at 392.

<sup>52</sup> Holton v. Physician Oncology Services, L.P., \_\_\_ Ga. \_\_\_, 2013 WL 1859294, \*5, n.4 (May 6, 2013).

<sup>53</sup> Cone v. Marietta Recycling Corp., Dempsey, J., Fulton Sup. Ct., Case No. 2012-cv-22381 (Mar. 26, 2013).

<sup>54</sup> O.C.G.A. § 13-8-2.

<sup>55</sup> O.C.G.A. § 13-8-51(6).

<sup>56</sup> O.C.G.A. § 13-8-52(b).

<sup>57</sup> O.C.G.A. § 13-8-54(a).

<sup>58</sup> O.C.G.A. § 13-8-54(b).

<sup>59</sup> O.C.G.A. § 13-8-51(11).

<sup>60</sup> 2011 WL 4601028, \* 3 (N.D. Ga. 2011).

<sup>61</sup> Id.

<sup>62</sup> See, e.g., Baggett, 231 Ga. App. at 292.

<sup>63</sup> Smith v. HBT, Inc., 213 Ga. App. 560, 445 S.E.2d 315, 318 (1994) (concluding a five-year covenant not to compete was reasonable with respect to duration).

<sup>64</sup> ALW Marketing Corp. v. McKinney, 205 Ga. App. 184, 188, 421 S.E.2d 565 (1992) (provision stating that the restricted period is tolled while the employee is in violation of the covenant is void on its face because it “potentially extends the duration of the covenant without limit”). Cf. Paul Robinson, Inc. v. Haege, 218 Ga. App. 578, 579, 462 S.E.2d 396 (1995) (upholding provision stating that restricted period is tolled while employee is in violation of the covenant, **as found by a court of competent jurisdiction**). The former provision failed because it could extend the term limit of the covenant indefinitely, while the latter provision was tied to the happening of certain events.

<sup>65</sup> O.C.G.A. §13-8-57.

<sup>66</sup> Id.

<sup>67</sup> See, e.g. Howard Schultz & Assoc. v. Broniec, 239 Ga. 181, 236 S.E.2d 265 (1977) (covenant prohibiting employee from working in a business “similar to” that of employer was too vague for enforcement). There is one exception to the rule requiring that the covenant specifically describe the employer’s business. The exception provides that the business need not be specifically described if the employee/franchise owner is the “heart and soul” of the business. Allen v. Hub Cap Heaven, Inc., 225 Ga. App. 533, 539, 484 S.E.2d 259 (1977) (Covenant prohibiting, within a small geographic area and for a short time, a franchisee from owning or operating any “Hub Cap Heaven, Inc. type business” would not be too vague for enforcement if the former franchise owner was the “heart and soul” of the business).

<sup>68</sup> See, e.g., Ken’s Stereo Video Junction, Inc. v. Plotner, 253 Ga. App. 811, 813, 560 S.E.2d 708 (2002) (although the employee worked only as a car stereo and security system installer, the covenant unreasonably prevented him from working for a competitor company in any capacity – even as a janitor).

<sup>69</sup> Sunstates Refrigerated Svcs., 215 Ga. App. at 62.

<sup>70</sup> O.C.G.A. § 13-8-53(c)(1).

<sup>71</sup> Pratt, 253 Ga. App. at 685.

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- <sup>72</sup> O.C.G.A. § 13-8-53(c)(2).
- <sup>73</sup> Wiley v. Royal Cup, Inc., 258 Ga. 357, 370 S.E.2d 744 (1988).
- <sup>74</sup> O.C.G.A. §13-8-56(2).
- <sup>75</sup> 210 Ga. App. 767, 769, 437 S.E.2d 619 (1993).
- <sup>76</sup> Id. at 770 (citing McMurray v. Bateman, 221 Ga. 240, 256, 144 S.E.2d 345 (1965) (upholding a 50 mile restriction in a physician employment agreement). See also Rash v. Toccoa Clinic Medical Assoc., 253 Ga. 322, 326, 320 S.E.2d 170 (1984) (upholding 25 mile restriction in a partnership agreement).
- <sup>77</sup> See, e.g., McAlpin v. Coweta Fayette Surgical Assoc., 217 Ga. App. 669, 458 S.E.2d 499 (1995).
- <sup>78</sup> Id. at 673. Accord Augusta Eye Center v. Duplessie, 234 Ga. App. 226, 506 S.E.2d 242 (1999) (upholding one year and ten counties).
- <sup>79</sup> Id.
- <sup>80</sup> 289 Ga. App. 474, 476, 657 S.E.2d 581 (2008).
- <sup>81</sup> O.C.G.A. § 13-8-51(10)(C).
- <sup>82</sup> Gill v. Poe & Brown of Ga., 241 Ga. App. 580, 583, 524 S.E.2d 328 (1999). See also Wachovia Ins. Svcs., Inc. v. Fallon, 299 Ga. App. 440, 682 S.E.2d 657 (2009) (non-solicitation covenant that defined customer as “any individual or entity that *has purchased*” insurance was over broad) (emphasis added).
- <sup>83</sup> See, e.g., O.C.G.A. § 13-8-51 (defining “legitimate business interest” to include “substantial relationship with specific prospective or *existing* customers, patients, vendors, or clients”) (emphasis added).
- <sup>84</sup> Gill, 241 Ga. App. at 583.
- <sup>85</sup> Akron Pest Control v. Radar Exterminating Co., Inc., 216 Ga. App. 495, 455 S.E.2d 601 (1995).
- <sup>86</sup> 215 Ga. App. 310, 450 S.E.2d 219 (1994).
- <sup>87</sup> Avnet, Inc. v. Wyle Laboratories, Inc., 263 Ga. 615, 617, 437 S.E.2d 302 (1993) (list of actual customers could constitute a trade secret if it derives its economic value from being non-public and if its owner made reasonable efforts to maintain its secrecy).
- <sup>88</sup> American Medical Association Opinion 7.03 (<http://www.ama-assn.org/ama/pub/physician-resources/medical-ethics/code-medical-ethics/opinion703.page>) (last accessed May 15, 2013).
- <sup>89</sup> See, e.g., Baggett, 231 Ga. App. at 294.
- <sup>90</sup> O.C.G.A. § 13-8-56 & -57.
- <sup>91</sup> McGinnittie v. Hobbs Group, LLC, 420 F.3d 1234, 1242 (11th Cir. 2005) (citing Hulcher Servs., Inc. v. R.J. Corman R.R. Co., LLC, 247 Ga. App. 486, 543 S.E.2d 461 (2000)).
- <sup>92</sup> ALW Marketing Corp. v. Drunasky, 1991 WL 345313, \*\*6-7 (N.D. Ga. 1991) (“Without the time to develop a lasting relationship with other agents, the short-term agent presents no threat to the employer’s competitive advantage in the employee marketplace and the employer needs no protection as to that employee.”)
- <sup>93</sup> Lee v. Envtl. Pest & Termite Control, Inc., 271 Ga. 371, 373, 516 S.E.2d 76 (1999).
- <sup>94</sup> O.C.G.A. § 13-8-53(e). Cf. Sunstates Refrigerated Svcs., 215 Ga. App. 61, 63, 449 S.E.2d 858, 860 (1994) (striking down non-disclosure covenant under the old law because it was unlimited in time).
- <sup>95</sup> Cf. Lee, 271 Ga. at 374 (non-disclosure covenant that applies to confidential information is enforceable) and Nasco, Inc. v. Gimbert, 239 Ga. 675, 676, 238 S.E.2d 368 (1977) (non-disclosure covenant that applies to all of employer’s business information is too broad for enforcement).
- <sup>96</sup> O.C.G.A. § 13-8-54(b).
- <sup>97</sup> O.C.G.A. §§ 31-33-3 & 31-33-2(a)(2).
- <sup>98</sup> O.C.G.A. § 31-33-2(a)(2).
- <sup>99</sup> See, e.g., Lee, 271 Ga. at 374.
- <sup>100</sup> Id.
- <sup>101</sup> PepsiCo, Inc. v. Redmond, 54 F.3d 1262, 1269 (7th Cir.1995).
- <sup>102</sup> Holton, 2013 WL 1859294, at \*4.
- <sup>103</sup> Id. at \*2.

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<sup>104</sup> 269 Ga. 553, 501 S.E.2d 501 (1998).

<sup>105</sup> Id. at 558.

<sup>106</sup> Holton, 2013 WL 1859294, at \*1.

<sup>107</sup> Id. at \*4.

<sup>108</sup> O.C.G.A. § 10-1-762(a).

<sup>109</sup> Palmer & Cay, Inc. v. Marsh & McLennan Cos., 404 F.3d 1297, 1303-04 (11th Cir. 2005).

<sup>110</sup> See Sunstates Refrigerated Svcs., 215 Ga. App. at 62-63.

<sup>111</sup> O.C.G.A. § 13-8-54(b).

<sup>112</sup> O.C.G.A. § 13-8-55.

<sup>113</sup> See, e.g., Rash, 253 Ga. at 325 (upholding covenant in part because physician “expressly agreed that the covenant was ‘reasonable’ and that breach of the covenant ‘would work harm’ to the partnership”).

<sup>114</sup> O.C.G.A. § 13-8-58(d).

<sup>115</sup> O.C.G.A. § 13-8-54(b).

<sup>116</sup> 163 F.Supp.2d 1371, 1380 (N.D. Ga. 2001).

<sup>117</sup> Id. at 1376.