

SC87083

IN THE SUPREME COURT OF MISSOURI

**HEALTHCARE SERVICES OF THE OZARKS, INC.,
d/b/a OXFORD HEALTHCARE,**

Respondent/Appellant,

vs.

PEARL WALKER COPELAND and LUANN HELMS,

Appellants/Respondents.

**Appeal from the Circuit Court of Newton County, Missouri
40th Judicial Circuit
The Honorable Gregory Stremel**

**BRIEF AMICUS CURIAE BY
MISSOURI HOSPITAL ASSOCIATION**

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STATEMENT OF INTEREST

Amicus curiae Missouri Hospital Association (“MHA”) is a private, not-for-profit organization whose mission is to create an environment that enables member hospitals and health care systems to improve the health of their patients and community. The majority of MHA’s members are also not-for-profit entities. MHA regularly appears as *amicus curiae* in Missouri courts in support of its member hospitals and health care systems when fundamental issues affecting the delivery of health care are at stake.

MHA’s interest in this appeal is to encourage this Court to maintain existing law permitting not-for-profit corporations and similar entities to utilize restrictive covenants in the same manner as natural persons and for-profit corporations. Among the points on appeal raised by appellants is an argument asserting that this Court should declare a “public policy” prohibiting nonprofit entities from using restrictive covenants. The sweeping and pernicious ramifications of adopting such an unprecedented “public policy” have received limited development by the parties and minimal attention from the court of appeals. Because the fundamental interests of MHA and the majority of its members—as well as those of an almost limitless array of not-for-profit entities across Missouri—would be immediately and adversely impacted by adoption of the rule advocated by appellants, MHA offers this brief to aid the Court in its consideration of the issue.

POINT RELIED ON

I. Appellants' Contention That Public Policy Should Prohibit Not-For-Profit Corporations From Using Restrictive Covenants Fails Because It Is Unsupported In Law Or Logic In That It Ignores The Nature And Powers Of Not-For-Profit Corporations, Finds No Support In Case Authority On Restrictive Covenants, And Represents Bad Public Policy That Will Leave The Resources Of Not-For-Profit Organizations Vulnerable To Private Exploitation. (Response to Appellants' Point II)

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Mo. Rev. Stat. § 355.025

Mo. Rev. Stat. § 355.131

Mo. Rev. Stat. § 431.202

ARGUMENT

I. Appellants' Contention That Public Policy Should Prohibit Not-For-Profit Corporations From Using Restrictive Covenants Fails Because It Is Unsupported In Law Or Logic In That It Ignores The Nature And Powers Of Not-For-Profit Corporations, Finds No Support In Case Authority On Restrictive Covenants, And Represents Bad Public Policy That Will Leave The Resources Of Not-For-Profit Organizations Vulnerable To Private Exploitation. (Response to Appellants' Point II)

Appellants assert that their restrictive covenants with Respondent Oxford Healthcare should be unenforceable because Oxford is a not-for-profit corporation and, as a matter of “public policy,” such entities should not be allowed to restrict former employees from competing on a for-profit basis. In essence, appellants argue that a not-for-profit corporation should have no right to use a restrictive covenant, allegedly because that is somehow “beyond its statutory purposes.” Appellants' Substitute Brief at 33.

As explained below, appellants' unsupported argument and peculiar notion of “public policy” should be rejected for several reasons. First, appellants have ignored the nature and powers of not-for-profit corporations as recognized by precedent and established by statute. Second, appellants' theory does not conform to settled case law permitting restrictive covenants in appropriate circumstances. Finally, appellants are advocating bad public policy that would transform not-for-

profit corporations and similar entities into second-class citizens unable to protect their resources from exploitation for private gain.

A. Nature and Powers of Not-For-Profit Corporations

“A nonprofit entity is ordinarily understood to differ from a for-profit corporation principally because it is barred from distributing its net earnings, if any, to individuals who exercise control over it, such as members, officers, directors, or trustees.” *Camps Newfound/Owatonna, Inc. v. Town of Harrison*, 520 U.S. 564, 585 (1997) (internal quotation omitted). “Nothing intrinsic to the nature of nonprofit entities prevents them from engaging in interstate commerce.” *Id.* “[T]he fact that a corporation is one not for profit does not mean that its activities or enterprises may not be conducted for gain, profit or net income so long as it is used for the purposes set forth in its articles and there is no pecuniary gain to the incorporators or members nor distribution of the income or profits to them” 1 Fletcher Cyc. Corp. § 68.05 at 831 (Perm. Ed. 1999) (footnote omitted).

This Court has long recognized the important role of nonprofit organizations and charities and “their right to every benefit and assistance which the law can justly allow.” *Abernathy v. Sisters of St. Mary’s*, 446 S.W.2d 599, 603 (Mo. banc 1969). “Organized corporate charity takes over large areas of social activity which otherwise would have to be handled by government, or even by private business. Charity today is a large-scale operation with salaries, costs and other expenses *similar to business generally.*” *Id.* (emphasis added; internal

quotations omitted). *See also Camps Newfound/Owatonna, Inc.*, 520 U.S. at 586 n. 18 (collecting various statistics on the nonprofit sector, comparing market shares of for-profit and nonprofit participants in various industries, and describing nonprofit hospitals and health maintenance organizations as “serious business”). The evolving role of charities and nonprofit organizations led this Court to abolish charitable tort immunity with the observation “that all persons, organizations and corporations stand equal before the law and must be bound or excused alike.” *Abernathy*, 446 S.W.2d at 603. *See also Camps Newfound/Owatonna, Inc.*, 520 U.S. at 583-84 (federal constitution and statutes regulating commerce and competition apply with equal force to activities of nonprofit organizations). Contrary to this principle, appellants advocate unequal treatment for not-for-profit corporations, albeit at a disadvantage rather than a preference. This notion conflicts with Missouri law, especially the Missouri Nonprofit Corporation Act found in Chapter 355 of the Missouri Revised Statutes.

Appellants largely ignore the Act except for a portion of Mo. Rev. Stat. § 355.025 generally prohibiting use of Chapter 355 by those engaged “in business or activity for profit.” The defining criteria for use of Chapter 355 is motivation (profit or not-for-profit) rather than the precise nature of the business or activity; indeed, the remainder of this section lists a wide array of purposes for which nonprofit corporations may be organized, many of which readily fit within typical notions of business activity: “health,” “agricultural; horticultural; soil, crop, livestock and poultry improvement; professional, commercial, industrial or trade

association;” and the ownership and operation of “water supply facilities” and “sanitary sewer collection systems.” These broad purposes are coupled with equally broad powers, such as the power to “carry on a business or businesses, either directly or through one or more for profit or non-profit subsidiary corporations.” Mo. Rev. Stat. § 355.131(16) (Appendix A2). Those powers also include the ability to hire employees, make contracts, and do “all things necessary or convenient, not inconsistent with law, to further the activities and affairs of the corporation.” *Id.* § 355.131(7), (11), and (17) (Appendix A1-A2). Obviously, the use of restrictive covenants for employees is “not inconsistent with law” and has been permitted in many cases. *See, e.g., Systematic Business Services, Inc. v. Bratten*, 162 S.W.3d 41, 50-52 (Mo. App. 2005).

As the court of appeals recognized, the powers of not-for-profit corporations and for-profit corporations are identical. *City of St. Louis v. Institute of Medical Education & Research*, 786 S.W.2d 885, 887 (Mo. App. 1990). “A corporation possesses all powers of a natural person except those specifically forbidden to corporations by law.” *Id.* at 888. Appellants’ argument thus fails at this most fundamental level because they have not, and cannot, demonstrate a specific legal prohibition on the use of restrictive covenants by not-for-profit corporations.

B. Permissibility of Restrictive Covenants

Apart from their self-serving notion of “public policy,” appellants offer no authority for excluding not-for-profit corporations from the operation of settled

Missouri law permitting restrictive covenants. The cases and statutes authorizing restrictive covenants simply do not support the distinction urged by appellants.

Missouri courts in appropriate circumstances will enforce noncompetition covenants by former employees and do so without considering the status or nature of the employer. *See Washington County Memorial Hospital v. Sidebottom*, 7 S.W.3d 542, 545 (Mo. App. 1999) (enforcing restrictive covenant in favor of not-for-profit hospital without analysis of nonprofit status; recognizing hospital’s “interest lies in protecting its patient base, as income from patient billings constitutes its primary source of revenue”). Likewise, the interests for which employee covenants can be utilized in Missouri—to protect trade secrets and customer contacts—are not inherently or exclusively interests of for-profit enterprises. *See, e.g., Lyn-Flex West, Inc. v. Dieckhaus*, 24 S.W.3d 693, 698 (Mo. App. 1999) (discussing various factors in determining the existence of a trade secret, none of them dependent upon the nature or identity of the holder).

Outside the employment context, Missouri courts will enforce restrictive covenants to protect a wider range of business interests. *See AEE-EMF, Inc. v. Passmore*, 906 S.W.2d 714, 720 n. 2 (Mo. App. 1995). Thus, in a nonemployment transaction or relationship, an interest protectable by restrictive covenant may arise from the particular contractual rights and duties established therein. *See Herrington v. Hall*, 624 S.W.2d 148, 151 (Mo. App. 1981) (contract terms and other evidence showed party entering into business arrangement “clearly intended to preserve his business investment” thereby demonstrating a “legitimate business

purpose” to support enforcement of restrictive covenant). Nothing in this line of authority limits its application to for-profit activity, so not-for-profit corporations should have the same rights as all other persons to use restrictive covenants in employment and other contracts to protect their resources and business interests.

In 2001, the Missouri Legislature recognized the enforceability of employment covenants by enacting Mo. Rev. Stat. § 431.202 (Appendix A3-A4) to expressly authorize covenants restricting solicitation of employees for employment elsewhere.¹ Section 431.202(3) and (4) permit any “employer” to enter such covenants. This provision applies to not-for-profit corporations by operation of Mo. Rev. Stat. § 355.131(11) (Appendix A1-A2), which empowers them to appoint employees and fix their compensation. Even more broadly stated, the legislature in section 431.202 made clear its intent not to restrict the enforceability of such covenants as “reasonably necessary to protect a party’s legally permissible *business interests*.” *Id.* § 431.202.4 (emphasis added). Given the broad range of permissible business activities by not-for-profit corporations under Chapter 355, there can be no question that the public policy of Missouri, as expressed by its legislature, permits the use of restrictive covenants by not-for-profit corporations.

¹ Section 431.202 effectively overruled the holding of *Schmersahl, Treloar & Co. v. McHugh*, 28 S.W.3d 345, 348-51 (Mo. App. 2000), upon which appellants rely in point I of their brief.

C. Policy Considerations

In a paean to “sound economics in a competitive capitalist society,” appellants argue that a “not-for-profit entity should not be allowed to restrain or enjoin commerce, charitable, competitive, or otherwise.” Appellants’ Substitute Brief at 32. In reality, enforceable restrictive covenants are upheld precisely because they do *not* restrain competition generally, but only prevent *unfair* competition. *See Superior Gearbox Co. v. Edwards*, 869 S.W.2d 239, 247 (Mo. App. 1993). A typical restrictive covenant merely prohibits a departing employee from obtaining an undue competitive advantage in the marketplace by using trade secrets, confidential information, or customer contacts of the former employer.

The position advanced by appellants would mean that not-for-profits could not protect themselves from unfair competition; employees such as appellants would be free to take valuable business information and use it to the detriment of the not-for-profit which previously employed them. *But see Missouri Federation of the Blind v. National Federation of the Blind of Missouri, Inc.*, 505 S.W.2d 1, 5 (Mo. App. 1973) (benevolent or other not-for-profit corporation or association has the right to be free from unfair competition). As a result, assets imbued with a public trust would be diverted for private gain. A couple of examples readily illustrate the resulting mischief.

- A not-for-profit hospital in an underserved area of Missouri recruits and employs a doctor to provide a needed medical specialty. The hospital supports the doctor in building a patient base and referral relationships.

The doctor is privy to the hospital's confidential business information, including cost information, salary information, and future business plans. In the world according to appellants, the doctor would be free to depart at an opportune moment, open a for-profit practice, lure away key support personnel, and serve the very same patients. As a for-profit entrepreneur, the doctor could then require his employees to sign non-compete agreements, thereby protecting the doctor from the same injury he inflicted upon his former not-for-profit employer.

- A not-for-profit research institute employs a scientist, engineer, or physician to develop a new drug, medical technique, or other cutting-edge technology. The work is undertaken in great secrecy with the expectation that the research results will be used to advance the mission of the institute and to produce income supporting the expansion of its research activities. As the work nears completion, the employee jumps to the for-profit world and shares the secret for great personal gain. Appellants urge this Court to leave the research institute powerless to protect its trade secrets and other confidential information by restrictive covenants.

Not-for-profit corporations currently serve the public interest in a myriad of ways in communities large and small throughout Missouri. Their revenues and resources serve the greater good rather than producing pecuniary profits for shareholders. Nonprofit institutions may over time accumulate substantial assets, which continue to serve the public good even if the institution ceases activity. As

just one illustration, proceeds from the sale of assets by Health Midwest funded new foundations in Missouri and Kansas; the Healthcare Foundation of Greater Kansas City received over \$400 million. *See* HCF History (visited December 7, 2005) <<http://www.healthcare4kc.org/history.html>>. *See also* *City of St. Louis v. Institute of Medical Education & Research*, 786 S.W.2d at 887 (considering appropriate disposition of institute's remaining assets after chief source of funding ceased to exist). This Court should reject a misguided proposal that would leave these valuable public resources free for the taking by those motivated by personal profit.

CONCLUSION

As this Court made clear decades ago in *Abernathy*, not-for-profit organizations are entitled to the full protection of the law. 446 S.W.2d at 603. Competition is a fact of life and takes many forms. Not-for-profit organizations enjoy no immunity from competition, so they should not be penalized for competition in pursuit of their missions. *Cf. Community Memorial Hospital v. City of Moberly*, 422 S.W.2d 290, 296 (Mo. 1967) (property tax exemption for not-for-profit hospital is not to be denied based on considerations of annual profit or loss, competition with private business, or extent of payments received for services).

Fidelity to mission and prudent business practice require that not-for-profit corporations avail themselves of all legal means available to safeguard their resources and protect the organization from attack by unfair competition. When

employed within the parameters allowed by Missouri law, restrictive covenants are simply a defensive measure to prevent unfair exploitation of the tangible and intangible resources that an organization needs to fulfill its mission, whether that mission happens to be making a profit for shareholders or advancing charitable, scientific, educational or other nonprofit objectives. Natural persons and for-profit corporations are fully entitled to use restrictive covenants, and the same rule should continue to apply to not-for-profit corporations and similar organizations.

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

I certify that:

1. The brief includes the information required by Rule 55.03;
2. The brief complies with the limitations contained in Rule 84.06(b);
3. According to the word count function of counsel's word processing software (Microsoft® Word 2002), the brief contains 2,871 words; and
4. The floppy disk submitted herewith containing a copy of this brief has been scanned for viruses and is virus-free.

R. Kent Sellers

CERTIFICATE OF SERVICE

On this 12th day of December, 2005, I hereby certify that two copies of the above and foregoing together with a copy of this brief on disk were served by mail, first-class postage prepaid, addressed to:

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