UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF TENNESSEE
WESTERN DIVISION

IN RE:

VISIONAMERICA, INCORPORATED, et al.	**Case Nos. 01-24615-B through 01-24636 and 01-24638 through 01-24639 and 01-26887 through 01-26888**
Debtors.	**Chapter 11–Jointly Administered**

MEMORANDUM OPINION AND ORDER GRANTING DEBTORS' MOTION TO ASSUME AND ASSIGN ITS EMPLOYMENT AGREEMENTS WITH ROBIN M. BRADY, O.D., AND DENNIS L. COSGROVE, O.D.

VisionAmerica, Inc. and its related debtor companies, Omega Health Systems of Middle Tennessee, Inc., Omega Health Services of Jackson, Tennessee, Inc., Ophthalmic Practice Enhancement, Inc., and Ophthalmic Ambulatory Surgical Centers, Inc. (hereafter "Debtors"), seek to assume employment contracts with Drs. Robin Brady and Dennis Cosgrove and assign them to Eye Health Partners, Inc. ("EHP"), the purchaser of the Debtors' clinics in Nashville, Jackson and contiguous areas of Middle and West Tennessee. EHP has moved this Court to clarify its July 26, 2001 order approving the sale of the clinics and the assumption of executory contracts to state that the sale order approved the assumption and assignment of the two optometrists' contracts at issue. In the alternative, EHP seeks an order approving the assumption and assignment of all contracts requested by EHP which deal with the Nashville and Jackson operations. The Court finds that the issues of assumption and assignment of Drs. Brady and Cosgrove's employment contracts were not

adjudicated at the July 26 hearing, due to a lack of sufficient notice to the two doctors, but the issues of notice and opportunity to be heard have now been resolved. The two doctors are represented by counsel, who filed written objections on their behalf, and the doctors and their attorney were present for the August 16 hearing on the present motions. The Court now approves the Debtors' motion to assume and assign these employment contracts.

SUMMARY OF UNDISPUTED FACTS

These contested matters were presented to the Court, without testimony, upon the pleadings and their attached documents, which included the employment contracts of Drs. Brady and Cosgrove. There were no factual issues presented concerning the § 365(b)(1) elements of default, cure or adequate assurance of future performance.

Dr. Brady signed an employment agreement with VisionAmerica, which the contract called "a wholly owned subsidiary of Omega Health Systems of Middle Tennessee," on June 7, 1999. The agreement set July 1, 1999, as his beginning date of service as an optometrist and operational director for South Central Tennessee. The contract allowed either party to terminate the agreement without cause by giving the other party 90 days written notice of termination. Upon termination, Dr. Brady would be bound by the contract's noncompetition clause, which forbids him from being a part of another "ophthalmic practice within a 25-mile radius of any VisionAmerica operations (including satellite locations) for one year following termination of the agreement."[1] The agreement set forth Dr. Brady's compensation for the next five years and stated that it was "renewable unless mutually

[1] The parties agree that the noncompetition clause for both doctors does not prohibit them from acting as optometrists. Rather, they are prohibited for the one-year period from competing in an "ophthalmic practice," in the case of Dr. Brady, or an "ophthalmology practice," in the case of Dr. Cosgrove.

amended by both parties." The contract was silent as to successors and assigns.

Dr. Cosgrove signed a nearly identical employment agreement with VisionAmerica, referred to as "a wholly owned subsidiary of VisionAmerica, Inc.," on November 22, 1999, to commence services as an optometrist and operational director for Cookville, Tennessee, on January 1, 2000. His contract required 120 days written notice of termination without cause and included a similar noncompetition clause. It also did not mention successors or assigns.

Drs. Brady and Cosgrove began and continued working for VisionAmerica pursuant to their contracts. On March 30, 2001, VisionAmerica and twenty-three related entities filed voluntary petitions under Chapter 11 of the Bankruptcy Code, and on May 10, 2001, two more cases were filed. All are jointly administered in this Court. The Debtors sought purchasers for its various practices, including the Middle Tennessee and Jackson practices. On July 11, 2001, Dr. Brady notified Dr. Jim Venable of VisionAmerica by letter that upon the sale of the practice to a third party, Dr. Brady's employment would terminate and he "shall have no further obligations to VisionAmerica or any third party following such date. Furthermore, this letter confirms that I do not consent to any attempted assignment of my employment to, or assumption of my employment agreement by, any third party." Likewise, Dr. Cosgrove, by a July 24, 2001 letter to Dr. Venable, asserted that upon the sale of the practice, his employment would terminate and that he did not consent to assumption or assignment to a third party.[2]

ASSUMPTION AND ASSIGNMENT

Based upon the contracts and the effective dates of the doctors' termination letters, at the

[2]No party suggests that Drs. Brady or Cosgrove violated the employment agreement by failing to provide 90 or 120 days notice of termination. *See* 11 U.S.C. § 365(b).

time VisionAmerica filed for bankruptcy, the employment contracts were in effect, and as will be discussed later, the appropriate time for measuring whether a contract is executory is the date of the bankruptcy filing. On their face, the noncompetition clauses appear to be enforceable under applicable Tennessee law, and no proof of unenforceability has been presented. Should any party wish in the future to raise arguments of unenforceability, for example based upon unreasonableness of time or radius, it will be left for EHP and Drs. Brady and/or Cosgrove to adjudicate those issues in an appropriate state court rather than in this bankruptcy court.

Although in the bankruptcy context, assumption generally precedes assignment, since the thrust of the doctors' objection is to assignment of the noncompetition clauses, the Court will first address assignment of such agreements under Tennessee law. Noncompetition agreements are assignable in Tennessee absent language in the contract prohibiting assignment. *See Bradford & Carson v. Montgomery Furniture Co.*, 92 S.W. 1104 (Tenn. 1906) (allowing assignment of non-competition agreement where the contract was silent as to assignability); *Jackson v. Moskovitz Agency, Inc.*, 672 S.W.2d 400, 403 (Tenn. 1984) (barring assignment of contract which stated that it was personal to the parties and that no rights or obligations could be assigned or delegated without the consent of the other party). The *Jackson* Court observed that "*Bradford* holds that a covenant not to compete is a property right and as such, in the absence of a provision prohibiting assignment, is both assignable and transferable." *Id.*

While Kentucky law was silent as to assignability of covenants not to compete, the Sixth Circuit determined that the commonwealth would allow assignment, because it had enforced noncompetition agreements, a court of appeals case had allowed assignment, and a "'majority of courts permit the successor to enforce the employee's restrictive covenant as an assignee of the

original covenantee (the original employer).'" *Managed Health Care Assocs., Inc. v. Kethan*, 209 F.3d 923, 928-29 (6th Cir. 2000) (allowing assignment to purchaser of most of employer's assets) (quoting 6 Richard A. Lord, WILLISTON ON CONTRACTS § 13:13 (4th ed. 1995)). The *Kethan* Court also accepted the argument that if the purchaser had bought the seller's stock instead of its assets, a separate assignment would not have been necessary. As a distinct matter, therefore, it would appear that noncompetition clauses such as those found in these contracts are assignable under applicable Tennessee law as well as under general contract principles applied by the Sixth Circuit.

The doctors argue that an executory contract cannot be assigned if it is a personal services contract. *See* 11 U.S.C. § 365(c)(1); *In re Alltech Plastics Inc.*, 5 U.S.P.Q.2d 1806 (Bankr. W.D. Tenn. 1987) (reiterating that "'the rights conveyed under a patent license are personal to the licensee and are not assignable in the absence of words of assignability included in the license"). Upon the sale of these businesses, however, as a result of the doctors' termination letters all that remained to be performed in the contracts at the time of assignment were the doctors' covenants not to compete. Under Sixth Circuit authority in *Kethan*, noncompetition agreements are not personal services contracts: "A personal services contract, however, requires that one of the parties be bound to render personal services. In contrast, a noncompetition clause only requires that one of the parties abstain from certain activities." *Kethan*, 209 F.3d at 929. "Consequently, the noncompetition clause does not require any affirmative action on the part of [the former employee], and is thus assignable." *Id.* at 930. *Kethan*, *Bradford & Carson* and *Jackson*, however, did not discuss the first step of assumption under Bankruptcy Code § 365, as they were not bankruptcy cases.

Section 365(a) permits a debtor in possession or trustee to assume or reject executory contracts. The Code does not define "executory," and the Sixth Circuit has provided two approaches

to determining whether a contract is executory. *See, e.g., Chattanooga Mem'l Park v. Still (In re Jolly)*, 574 F.2d 349 (6th Cir. 1978) (functional approach); *Terrell v. Albaugh (In re Terrell)*, 892 F.2d 469 (6th Cir. 1989) (material breach analysis); *see also Huntington Nat'l Bank Co. v. Alix (In re Cardinal Indus., Inc.)*, 146 B.R. 720, 728 n.7 (Bankr. S.D. Ohio 1992) ("But note that the functional approach of defining executory contracts is not entirely separate and distinct from the Countryman definition. . . . Professor Countryman suggested that executory contracts be defined in light of the purpose for which the trustee is given the power to assume or reject: to benefit the estate."); *In re Structurlite Plastics Corp.*, 86 B.R. 922, 926 (Bankr. S.D. Ohio 1988) ("Thus, while the Sixth Circuit has employed the traditional definition of an executory contract enunciated in the legislative history and refined by Countryman, it has also applied a practical, or 'functional,' approach . . . in its determination of whether or not a contract is executory in a rejection context.") (citing *Jolly*, 574 F.2d 349 and *Sloan v. Hicks (In re Becknell & Crace Coal Co.)*, 761 F.2d 319 (6th Cir. 1985)).

While acknowledging that "executory contracts involve obligations which continue into the future," *Jolly* introduced the "functional" approach to determining whether a contract is executory under 11 U.S.C. § 365(a), at least where the debtor is seeking rejection of the contract.

> The key, it seems, to deciphering the meaning of the executory contract rejection provisions, is to work backward, proceeding from an examination of the purposes rejection is expected to accomplish. If those objectives have already been accomplished, or if they can't be accomplished through rejections, then the contract is not executory within the meaning of the Bankruptcy Act.

Jolly, 574 F.2d at 351 (determining contract was not executory because it had been breached and judgment had been entered). The rationale of this functional approach works as well when assumption rather than rejection is sought. If the result of the assumption is to add value or benefit

to the bankruptcy estate, the functional approach would suggest that the contract is executory.

The parties in the present dispute do not allege there has been a breach of the employment agreements. Upon the sale of the practices, Drs. Brady's and Cosgrove's employments terminated by their own choices. According to the contracts' terms, upon termination they had continuing obligations to refrain from competition throughout a one-year period. Assumption of the contracts would add to the value of the bankruptcy estates by retaining the doctors' noncompetition agreements. Under the functional approach, the contracts are executory and assumable.

Terrell did not discuss the "functional" approach but declared that "[t]he legislative history . . . indicates that Congress intended the term to be defined as a contract 'on which performance remains due to some extent on both sides.'" *In re Terrell*, 892 F.2d at 470 (quoting S. Rep. No. 95-989, *reprinted in* 1978 U.S.C.C.A.N. 5787, 5844; H.R. Rep. No. 95-595, *reprinted in* 1978 U.S.C.C.A.N. 5787, 5963, 6303). "Congress apparently had in mind the definition of executory contracts set forth [by Professor] Countryman," who defined executory contract as "'a contract under which the obligation of both the bankrupt and the other party to the contract are so far unperformed that the failure of either to complete performance would constitute a material breach excusing the performance of the other.'" *Id.* n.2 (quoting Vern Countryman, *Executory Contracts in Bankruptcy: Part I*, 57 MINN. L. REV. 439, 460 (1973)). *Terrell* found that the parties had material obligations unperformed, and under state law, "the failure of either party to perform his remaining obligations would give rise to a material breach allowing the other party to avoid continued performance." *Id.* at 472.

In identifying whether there are mutual obligations existing under these contract, the Court will look to the date of the Debtors' filing under Title 11. *See In re Rovine*, 6 B.R. 661, 666 (Bankr.

W.D. Tenn. 1980) ("In other words, the franchise agreement in question was unperformed in material part by both the plaintiff and defendant as of the filing date of the defendant's Chapter 11."); *accord Collingwood Grain, Inc. v. Coast Trading Co. (In re Coast Trading Co.)*, 744 F.2d 686, 692 (9th Cir. 1984) ("contract was not executory at the time Coast filed for bankruptcy"); *Carlson v. Farmers Home Admin. (In re Newcomb)*, 744 F.2d 621, 624 (8th Cir. 1984) ("[A]n 'executory contract' that can be rejected in bankruptcy is a contract on which performance remains due on both sides at the time of the bankruptcy petition."); *Leefers v. Anderson (In re Leefers)*, 101 B.R. 24, 26 (C.D. Ill. 1989) ("*First*, it must be ascertained whether either party has any unperformed obligation under the contract at the time the bankruptcy petition is filed."); *In re MCorp Fin.*, 122 B.R. 49, 50 (Bankr. S.D. Tex. 1990) ("The point in time for determining whether a contract is executory is the date the bankruptcy petition is filed."); *In re C.M. Turtur Invs., Inc.*, 93 B.R. 526, 535 (Bankr. S.D. Tex. 1988) ("I look only at the status of the contracts as of the date Turtur filed its petition. At that point, the contracts were not executory because the obligation on both sides had been fully performed."); *In re R.M. Cordova Int'l, Inc.*, 77 B.R. 441, 446 (Bankr. D. N.J. 1987) ("The Court recognizes the general principle that if performance no longer remains due on either side at the time the petition is filed, neither the Court nor the Trustee is confronted with an executory contract that can be either rejected or assumed.") (citing *In re Murtishi*, 55 B.R. 564, 567 (N.D. Ill. 1985) ("Initially, a court faced with a motion to reject an executory contract pursuant to section 365(a) should focus on the situation where both the debtor and the other party to the contract have significant obligations to perform under the contract *at the time the petition is filed*.")); *In re Bastian Co.*, 45 B.R. 717, 721-22 (Bankr. W.D.N.Y. 1985) ("[T]he appropriate time for determining whether a contract is executory and, therefore, rejectable is as of the date of filing the petition in

bankruptcy.") (citing *NLRB v. Bildisco & Bildisco*, 465 U.S. 513, 529-32 (1984)); *In re Norquist*, 43 B.R. 224, 230 (Bankr. E.D. Wash. 1984) ("I believe the correct time to apply the Countryman test, however, is the date upon which the petition for relief was filed."); *In re Farrar McWill, Inc.*, 26 B.R. 313, 314 (Bankr. W.D. Ky. 1982) ("The term executory contract, however, does cover a contract where the obligations of both parties remain at least partially and materially unperformed at the time of bankruptcy."); *In re California Steel Co.*, 24 B.R. 185, 187 (Bankr. N.D. Ill. 1982) ("[T]he crucial factor which establishes the executory nature of a contract is the existence of unperformed mutual obligations at the time of the filing of the bankruptcy petition."); *In re Ridgewood Sacramento, Inc.*, 20 B.R. 443, 445 (Bankr. E.D. Cal. 1982) ("contract remained executory on the date that the debtor filed its voluntary petition in bankruptcy"); NORTON BANKR. L & PRAC.2d § 39:5 (1997) ("Normally the date for this determination is the date of the commencement of the bankruptcy case.").

At the time VisionAmerica filed for bankruptcy, these two employment agreements were in effect. At that point in time, Drs. Brady and Cosgrove were working for the Debtor and continued to work for several months postpetition before notifying the Debtor that their employment agreements would terminate upon the sale of the business to a third party. Therefore, under the Countryman definition of mutuality of obligations, as well as under the functional approach, the employment contracts are executory. *See, e.g., Burger King Corp v. Rovine (In re Rovine Corp.)*, 5 B.R. 402, 404 (Bankr. W.D. Tenn. 1980) (holding covenant not to compete was executory), *motion to amend denied*, 6 B.R. 661; *In re Hearing Ctrs. Of Am., Inc.*, 106 B.R. 719 (Bankr. M.D. Fla. 1989). At the time of the bankruptcy filing, a breach of the employment agreements by either party would have been material and would have entitled the other party to a claim for damages.

Assumption would benefit the estate by increasing the value of its operations. The fact that the doctors terminated their employment contracts after the bankruptcy filing does not change this analysis.

Moreover, assumption in this case meets the flexible "business judgment" test for assumption that some courts have adopted. *See, e.g.*, *In re Beare Co.*, 177 B.R. 879, 882 (Bankr. W.D. Tenn. 1994) ("In order for it to be assumed, an executory contract must benefit a debtor's bankruptcy estate, and the assumption of the contract must be an exercise of 'reasonable business judgment.'") (citations omitted); *Phar-Mor Inc. v. Strouss Building Assocs.*, 204 B.R. 948, 951-52 (N.D. Ohio 1997) ("Whether an executory contract is "favorable" or "unfavorable" is left to the sound business judgment of the debtor."); *In re Structurlite Plastics Corp.*, 86 B.R. at 925 n.4; NORTON BANKR. L. & PRAC.2d §§ 39:12, 39:16 (1997); 3 COLLIER ON BANKRUPTCY ¶ 365.03[2] (15th ed. Rev. 2000) ("Under the Code, most courts have applied a 'business judgment' test to trustees' decisions to assume or reject contracts or leases.").

ASSIGNMENT ALONE

Although the Court has concluded that these employment contracts were executory at the time of the bankruptcy filing, should they be viewed as nonexecutory, the result would not change. In that event, there would be no need for the Debtors to assume the contracts, but the issue of assignment would still exist. Under both Tennessee and Sixth Circuit authority discussed earlier, since these contracts were silent concerning assignment, the Debtors would be able to assign what remained of them to EHP. *See Bradford & Carson,* 92 S.W. at 1104 and *Kethan,* 209 F.3d at 923.

CONCLUSION AND ORDER

Based upon the undisputed contractual terms and the Court's conclusions concerning assumption and assignment, the Court **GRANTS** VisionAmerica's motion to assume and assign the employment contracts it holds with Drs. Brady and Cosgrove. As stated previously, this conclusion and Order reserves the opportunity for the doctors and EHP to litigate in an appropriate state court any disputes concerning enforceability of the assigned noncompetition agreements. This Court's conclusion and Order only determines the issue before it, that the employment contracts may be assumed and assigned, but the Court does not determine any other issues related to the assigned contracts

SO ORDERED this 12th day of September, 2001.

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WILLIAM HOUSTON BROWN
UNITED STATES BANKRUPTCY JUDGE

cc:
John R. Dunlap
Thomas H. Fulton
James E. Bailey, III
Humphreys Dunlap Wellford
Accuff & Stanton, P.C.
Attorneys for Debtor
2200 First Tennessee Building
Memphis, TN 38103

Michael R. Paslay
Derek W. Edwards
Waller Lansden Dortch & Davis, PLLC
Attorneys for Eye Health Partners, Inc.
511 Union Street, Suite 2100
P.O. Box 198966
Nashville, TN 37219-8966

John L. Ryder
Harris, Shelton, Dunlap, Cobb & Ryder, PLLC
One Commerce Square, Suite 2700
Memphis, TN 38103
Attorney for Robin M. Brady, O.D. and Dennis L. Gosgrove, O.D.

Bruce C. Bailey
Chambliss, Bahner & Stophel, P.C.
1000 Tallan Bldg., Two Union Square
Chattanooga, TN 37402-2500
Attorney for Robin M. Brady, O.D.

Madalyn S. Greenwood
Assistant United States Trustee
200 Jefferson Avenue, Suite 400
Memphis, TN 38103