

corporation with its principal place of business in Colorado, provided management services to medical practice groups like ROA. In 1996, SCN and ROA entered into a Service Agreement. Using cash and shares of its own stock, SCN purchased some of ROA's assets. SCN also agreed to provide management services to ROA's Philadelphia office, including billing, collections, accounting and other administrative services. ROA would, in turn, pay SCN a monthly fee. The agreement had a term of forty years. SCN entered into similar agreements throughout the country with approximately twenty other medical practice groups. The precise financial terms of these initial management service agreements sometimes differed from ROA's.

In 1997, three owners of ROA, Doctors Booth, Bartolozzi and Balderston, left ROA to form their own practice group, 3B Orthopaedics, P.C. ("3B"). 3B and SCN entered into an informal agreement that required 3B to pay monthly fees for SCN's management services. The monthly fees were identical to those provided for in ROA's Service Agreement. SCN never purchased any of 3B's assets, although the owners of 3B already held stock in SCN by virtue of their previous partnership at ROA.

In 1998, the medical management services market faltered. As a result, SCN and many of its affiliated practice groups sought to restructure their long-term business arrangements. At a minimum, all of the interested parties wanted to replace their

forty year contracts with agreements of a much shorter duration. Although SCN wanted to eventually terminate those agreements, it also relied on collecting monthly service fees in order to maintain its corporate viability. Accordingly, SCN wanted to restructure its existing agreements so that they contained terms of approximately five years,¹ during which it could diversify its corporate ventures. SCN also wanted to reacquire most, if not all, of the stock originally sold to the owners of its affiliated medical practice groups. SCN approached each of its practice groups and made similar proposals. Although nearly half of the practice groups amicably restructured their agreements with SCN, some resorted to litigation before settling their claims. 3B, ROA's competitors and former partners, brought suit against SCN.

On March 9, 1999, SCN and ROA finalized a contract that restructured their business relationship (the "Restructure Agreement"). The Restructure Agreement provided that ROA would repurchase the non-medical assets it had sold SCN in 1996. In exchange, ROA would continue to make cash payments to SCN and would transfer back to SCN some shares of SCN common stock.

ROA also wanted assurances that no practice group would receive better treatment during restructuring than ROA received. ROA's owners were particularly concerned that their former

¹ Under SCN's proposed restructuring plan, any practice group could immediately terminate its relationship with SCN by pre-paying the total of its monthly management fees.

partners, 3B, would strike a better deal with SCN. SCN and ROA agreed upon inserting a most-favored nation clause ("MFNC") in the Restructure Agreement. The motivation behind the MFNC was not ROA's alone, however, as identical MFNCs appeared in at least eight other agreements between SCN and its affiliated practice groups. According to ROA, SCN represented that the MFNC would apply to settlements of litigation such as 3B's. SCN denies that allegation.

The MFNC in ROA's Restructure Agreement states that:

In the event that SCN shall within a period commencing on the closing date and ending December 31, 1999 close a transaction with an Affiliated Practice which is substantially similar to the restructure transaction contemplated by this Agreement ("a Restructuring Transaction") and, taken as a whole, the financial terms of such other Restructuring Transaction are materially more favorable to any Affiliated Practice (and its Physician Owners) than the financial terms, taken as a whole, of the restructuring transaction contemplated by this Agreement, then in such event SCN shall modify the financial terms of this Agreement in such manner as SCN shall reasonably determine so that the financial terms of the restructuring transaction contemplated by this Agreement for ROA[] . . . shall be no less favorable, when taken as a whole, than the Restructure Transaction undertaken with respect to any other Affiliated Practice.

Restructure Agreement § 10.15. The MFNC also defined an "Affiliated Practice" as "any physician medical practice . . . which, as of December 1, 1998, had in effect with SCN an agreement substantially similar to the Service Agreement" ROA had with SCN. Id. The closing date of the Restructure Agreement is

unclear; although originally slated for June 15, 1999, the parties apparently amended the agreement to include a closing date no later than July 15, 1999. The Restructure Agreement was fully integrated, id. § 10.3, and governed by Pennsylvania law. Id. § 10.8.

During the course of performing the Restructure Agreement, ROA found evidence that led it to believe SCN had breached the MFNC. Specifically, ROA believes that SCN entered into better restructure agreements with other medical practice groups, concealed that fact and then refused to adjust the Restructure Agreement accordingly. ROA filed suit, alleging breach of contract and bad faith. ROA also alleged that SCN fraudulently "parked" the 3B settlement agreement in an attempt to avoid the MFNC, and negligently misrepresented during renegotiations that the MFNC would apply to settlements of litigation such as 3B's.

District Judge Shapiro, to whom this case was originally assigned, conducted a hearing on February 24, 2000. During that hearing, Judge Shapiro expressed her concern that ROA not seek discovery of irrelevant or unnecessary information. In particular, Judge Shapiro noted that the parol evidence rule and the fact that the Restructure Agreement was fully integrated might preclude the use of certain evidence to construe the MFNC. Judge Shapiro stated, "[W]hat you are entitled to are the deals, the terms. Not all the negotiations and everything like that" or

"what people had in their minds at some time." Hr'g, February 24, 2000 at 16. Judge Shapiro intimated, however, that she might permit discovery on these matters at a later stage of discovery. See id.

On April 19, 2000, ROA served a notice of deposition upon SCN. ROA sought discovery of the terms of any other restructure agreement entered into by SCN. Specifically, ROA sought discovery of the terms of these agreements, consideration paid, valuation methods, liabilities assumed, post-closing "true-up" procedures and any rebates made by or for SCN. In all, ROA sought discovery regarding twenty other restructure agreements. SCN sought a protective order on May 2, 2000, claiming that the deposition exceeded the scope of initial discovery set out by Judge Shapiro. On June 27, 2000, Magistrate Judge Angell granted SCN's Motion for Protective Order, limiting initial discovery to "the terms of the restructure agreements and the litigation settlement agreements. . . ." Prot. Order, June 27, 2000 ¶ 1. ROA filed Objections to that Order.

On October 2, 2000, the Court amended Magistrate Judge Angell's Order in order to allow ROA to conduct discovery of SCN's settlement agreement with 3B. The Court selected the 3B agreement because it seemed to be a particular source of concern to ROA. The Court also provided that ROA could petition for an extension in the scope of discovery. In all other respects, the

Court affirmed Magistrate Judge Angell's Order. A few weeks later, ROA filed the instant Motion to Expand the Scope of Discovery, which the Court will now consider.

II. STANDARD OF REVIEW

The instant Motion to Expand the Scope of Discovery is, in essence, a request that the Court modify a Protective Order granted by Magistrate Judge Angell. Federal Rule of Civil Procedure 72 governs objections to magistrate judges' orders, both dispositive and non-dispositive. A discovery order is considered non-dispositive because it does not dispose of a party's claim or defense. Haines v. Ligget Group, Inc., 975 F.2d 81, 92 (3d Cir. 1992). District courts must typically modify or set aside any non-dispositive magistrate judge order if it is "found to be clearly erroneous or contrary to law." Fed. R. Civ. P. 72(a). The Court has plenary power to alter Magistrate Judge Angell's Order, however, as that Order anticipated the Court's amending it. See Order, June 27, 2000 ¶ 4 ("[N]othing precludes Judge Kelly from expanding the scope of discovery prospectively as he deems appropriate."). In deciding whether to do so, the Court is guided by Federal Rule of Civil Procedure 26. Rule 26 states that a party "may obtain discovery regarding any matter, not privileged, which is relevant to the subject matter involved in the pending action. . . ." Fed. R. Civ. P. 26(b)(1). The

information sought through discovery need not itself be admissible at trial, so long as it appears to be "reasonably calculated to lead to the discovery of admissible evidence." Id. A court can limit the scope of discovery, however, if "the burden or expense of the proposed discovery outweighs its likely benefit. . . ." Fed. R. Civ. P. 26(b)(2). With regards to protective orders, a court may "make any order which justice requires to protect a party or person from . . . undue burden or expense, including . . . that certain matters not be inquired into, or that the scope of the disclosure or discovery be limited to certain matters. . . ." Fed. R. Civ. P. 26(c)(4).

III. DISCUSSION

ROA asks the Court to extend the scope of discovery to include up to thirteen agreements between SCN and other medical practices. ROA seeks this discovery because it believes evidence of those other agreements is vital to its breach of contract claim against SCN. SCN opposes that request, suggesting that further discovery should be foreclosed in its entirety. In the alternative, SCN suggests limiting discovery to only eight of SCN's other agreements. The Court must therefore determine whether to permit any additional discovery and, if so, its appropriate scope under Rule 26.

A. The Propriety of Further Discovery in General

SCN suggests that additional discovery is unwarranted in this case. In support of this contention, SCN states that the financial terms of its many restructure agreements consisted solely of uniform formulae that were used to calculate what each affiliated practice group should pay in order to restructure its relationship with SCN. These formulae were based on an individual practice's revenues, value of assets to be repurchased and services fees due SCN. SCN argues that the financial favorableness of those other agreements can be determined simply by reference to the formulae, which are contained within the four corners of the restructure agreements themselves.

The Court disagrees. First, SCN's argument implicitly concedes that some limited discovery concerning the different practices' initial affiliation payments, annual revenues, service fees and value of repurchased assets is appropriate. Second, the Court has considered this matter before. See Order of October 2, 2000 at 6-10. The Court previously found that the language of the Restructure Agreement anticipated at least limited discovery beyond the four corners of the other restructure agreements. See id. 5-6. Indeed, a party to a contract that places in issue the favorableness of twenty other contracts cannot complain that limited discovery regarding those contracts is unduly burdensome. Nor is the Court persuaded that any evidence gathered through

discovery would clearly be inadmissible or irrelevant. For example, the Court already suggested that "the book value of SCN's accounts receivable, as well as SCN's post-closing 'true-up' price adjustment procedures, may affect the favorableness of the other agreements in a way that the written documents themselves will not reflect." Id. at 7-8. SCN has not persuaded the Court otherwise. The Court cannot say that limited discovery of the financial terms of certain agreements would not be reasonably calculated to lead to the discovery of admissible evidence. Accordingly, the Court finds that some discovery relating to the financial favorableness of the other restructure agreements is needed in order to provide ROA with evidence to support its breach of contract claim.

B. The Appropriate Scope of Further Discovery

Having decided that some additional discovery in this matter is appropriate, the Court must then determine its scope. The Court is guided by Rule 26, which generally allows discovery of any relevant matter that is "reasonably calculated to lead to the discovery of admissible evidence," Fed. R. Civ. P. 26(b)(1), but also empowers the courts to limit discovery if "the burden or expense of the proposed discovery outweighs its likely benefit. . . ." Fed. R. Civ. P. 26(b)(2). The Court must therefore examine the discovery sought in terms of ROA's claims against SCN.

Because ROA's primary claim is one for breach of the MFNC,² discovery of agreements that would clearly not trigger that contractual provision would be irrelevant and, consequently, unduly burdensome in light of its negligible evidentiary value.

Based upon its clear language, a breach of the MFNC only occurs if SCN entered into a transaction that was: (1) closed after the closing date of ROA's Restructure Agreement and before December 31, 1999; (2) with an "Affiliated Practice," "any physician medical practice . . . which, as of December 1, 1998, had in effect with SCN an agreement substantially similar to the Service Agreement"; (3) "substantially similar" to ROA's Restructure Agreement; and (4) taken as a whole, the financial terms were "materially more favorable" to the Affiliated Practice than ROA's Restructure Agreement was to ROA. Restructure Agreement § 10.15. Discovery of any agreement that clearly does not satisfy one of these conditions would be unnecessary because it would not support a claim for breach of contract.

Based on those criteria, the parties agree that the MFNC

² ROA also alleges fraud and misrepresentation. Because the Court's Order of October 2, 2000 afforded ROA ample time to conduct discovery regarding the 3B agreement, the Court will not address at length ROA's fraud claim. With regard to ROA's misrepresentation claim, ROA asserts, without elaboration, that "the deals that were struck in the litigation context are . . . relevant to the claims for . . . misrepresentation." Plf.'s Supplemental Memo. in Supp. of Plf.'s Mot. to Expand Disc. at 16. The Court disagrees. The evidence required to prove this claim can be found through discovery of the renegotiations between those two parties, which has already been conducted.

would clearly be triggered by agreements, assuming they were materially more favorable than ROA's Restructure Agreement, between SCN and: (1) Orthopaedic Surgery Centers, P.C. II; (2) Steven P. Surginer, M.D., P.A., II; (3) Orthopaedic Associates of West Florida, P.A.; (4) Riyaz H. Jinnah, M.D., P.A.; (5) Floyd Jaggears, M.D., P.C.; (6) Orthopaedic Institute of Ohio; (7) Orthopaedic & Sports Medicine Center, II, P.A.; and (8) Princeton Orthopaedic Associates, II, P.A. See Def.'s Supplemental Memo. in Opp'n to Plf.'s Mot. to Expand Disc. at 5-6; Plf.'s Supplemental Memo. in Supp. of Plf.'s Mot. to Expand Disc. at 11-14. The Court agrees that these agreements would clearly trigger the MFNC. Accordingly, discovery relating to the financial favorableness of these agreements should proceed.

ROA seeks discovery of five other agreements that it believes would also trigger the MFNC. Four of those agreements were actually settlements of formal litigation, rather than then result of traditional contractual renegotiation. Those settlements include agreements between SCN and: (1) TOC Specialists, P.L.; (2) The Specialists Orthopaedic Medical Corporation; (3) 3B Orthopaedics, P.C.; and (4) Southeastern Neurology Group. ROA also seeks discovery of a fifth agreement, one between SCN and Ortho-Associates, P.A., which was not a settlement of litigation.

Given the procedural posture of this case, it should suffice

for the Court to find that further discovery of these agreements is unlikely to produce relevant, admissible evidence.³ These agreements all appear, in substance, dissimilar from ROA's Restructure Agreement.⁴ The substance of the Restructure Agreement, like many of SCN's other contemporaneous agreements, had distinct characteristics that these particular agreements all lack.

In contrast to ROA's Restructure Agreement, SCN's agreement with Orth-Associates did not contain any MFNC. Moreover, this agreement was merely an asset purchase agreement that did not require Orth-Associates to enter into an amended management services agreement. Although ROA correctly suggests that merely referring to an agreement as an asset purchase agreement is not controlling, the Court nonetheless finds that this agreement is so dissimilar from the Restructure Agreement that it would not trigger the MFNC.

³ The Court will not engage in a lengthy analysis of the meaning of the "substantially similar" language of the MFNC. Indeed, neither party has presented the Court with any contractual analysis of this language, or for that matter any other language in the Restructure Agreement.

⁴ SCN also contends that the 3B agreement and Ortho-Associates agreement would not trigger the MFNC because of their respective closing dates. For the purposes of this motion, the Court finds that the exact closing dates of these two agreements is unclear. For example, SCN claims it closed its agreement with Ortho-Associates no later than June 14, 1999. ROA notes, however, that a balance sheet places the closing date on June 15, 1999. Accordingly, the Court cannot foreclose discovery of these agreements based solely on that factor.

Even more dissimilar are the litigation settlement agreements. Unlike the Restructure Agreement, a product of traditional contractual renegotiation, these agreements all resulted from the settlement of formal litigation. Moreover, none of these agreements contains a MFNC. Finally, each of these agreements terminated the business relationship between the other practice group and SCN, rather than restructuring a continuing relationship.⁵ To that end, none of these agreements contained an amended management services agreement, because one would have been unnecessary. Although termination clearly alters an existing business relationship, it does not appear to constitute a restructuring as that term is used in the MFNC.

ROA suggests that all of these agreements are substantially similar to its own Restructure Agreement because they all derive from a common background, circumstances and intent. In essence, ROA suggests that these agreements are substantially similar because SCN intended to either terminate or abbreviate its business relationship with all of its affiliated medical practice groups. While that may be the case, ROA's argument misses the mark; though the agreements may have been similarly motivated, they are dissimilar in their substance. Motivation and

⁵ With regard to the 3B agreement, SCN also notes that, because SCN never purchased 3B's assets as part of 3B's initial affiliation, their settlement agreement did not require 3B to repurchase its assets from SCN.

circumstance alone cannot serve to render two contracts substantially similar.

Discovery of these additional agreements would not likely lead to admissible or relevant evidence concerning ROA's breach of contract claim. In light of Rule 26, the Court finds that further discovery regarding the financial terms of these agreements would be unduly burdensome to SCN, given the limited utility of such discovery. Accordingly, ROA may not seek further discovery concerning the financial terms of these agreements. Finally, the Court notes that, even though discovery should be conducted regarding certain agreements beyond the 3B agreement, the scope of that discovery is not unlimited in breadth. The additional discovery now permitted should be strictly confined to exposing evidence relating to whether the other agreements were financially more favorable than ROA's Restructure Agreement.

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

RECONSTRUCTIVE ORTHOPAEDIC	:	CIVIL ACTION
ASSOCIATES II, P.C.	:	
	:	
v.	:	
	:	
SPECIALTY CARE NETWORK, INC.	:	99-5329

O R D E R

AND NOW, this day of March, 2001, in consideration of the Motion to Expand the Scope of Discovery filed by the Plaintiff, Reconstructive Orthopaedic Associates II, P.C. (Doc. No. 39), the Response filed by Defendant, Specialty Care Network, Inc., and the various supplemental memoranda filed by the parties, it is **ORDERED** that:

1. Plaintiff's Motion to Expand the Scope of Discovery is **GRANTED IN PART**.

A. Plaintiff may conduct further discovery regarding the restructure agreements between SCN and: (1) Orthopaedic Surgery Centers, P.C. II; (2) Steven P. Surginer, M.D., P.A., II; (3) Orthopaedic Associates of West Florida, P.A.; (4) Riyaz H. Jinnah, M.D., P.A.; (5) Floyd Jaggears, M.D., P.C.; (6) Orthopaedic Institute of Ohio; (7) Orthopaedic & Sports Medicine Center, II, P.A.; and (8) Princeton Orthopaedic Associates, II, P.A.

B. Such discovery shall be strictly limited to matters

that are reasonably calculated to lead to admissible evidence showing whether the financial terms of those agreements were materially more favorable to the third party than ROA's Restructure Agreement was to ROA.

2. Plaintiff's Motion to Expand the Scope of Discovery is **DENIED IN PART**. Plaintiff may not conduct further discovery regarding agreements between SCN and: (1) TOC Specialists, P.L.; (2) The Specialists Orthopaedic Medical Corporation; (3) 3B Orthopaedics, P.C.; (4) Southeastern Neurology Group; and (5) Ortho-Associates, P.A.

BY THE COURT:

JAMES MCGIRR KELLY, J.