

FTC Proposes Rule to Strike Noncompete Agreements Nationwide

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On January 5, 2023, the Federal Trade Commission (FTC) announced a proposed new rule that would effectively prohibit employers from requiring employees to agree to noncompete clauses. The public is invited to submit comments on the proposed rule for 60 days (until March 6, 2023) and would take effect after the July 4, 2023, holiday.

In issuing the notice of proposed rulemaking, the FTC estimated that it would increase workers' earning in the U.S. by nearly \$300 billion each year and double the number of new businesses founded by former employees. Because doctors and other healthcare providers are frequently required to sign noncompetes, the FTC also estimated that the rule would save consumers \$148 billion annually on health care costs.

The rule would effectively deem noncompete clauses as an unfair method of competition in the market for workers. If the rule goes into effect, employers will not only be prohibited from requiring employees to sign noncompete clauses, it would also rescind existing noncompetes and require employers to "actively inform their employees that the contracts are no longer in effect." (Note: The proposed rule would create an exception for noncompetes connected to the sale of a business.)

Enforcement of noncompetes in the U.S. is subject to a patchwork of state laws ranging from outright statutory prohibition in California to the "legitimate employer interest" rule in New York.

Though noncompetes are often associated with senior executives or key sales employees, the FTC noted examples of hourly workers who were impacted by noncompete, including:

"Michael, a single father, found work as a security guard for a Florida firm. A few weeks after accepting the job, which paid around \$11 an hour, his overnight childcare fell through, and he resigned. Months later, he took a job as a daytime security guard at a bank making almost \$15 per hour. But, his new employer let him go when the previous employer sent a letter stating that Michael had signed a two-year noncompete."

Closely related to employee noncompetes are “antipoaching” agreements that were part of many franchise agreements until 2017. Antipoaching agreements prevented a franchisee’s employee from seeking employment from another franchisee in the same franchise system. Washington was the first state to attack these provisions as being in violation of state competition law, and a number of other states followed its lead. As a result, most franchisors have removed antipoaching provisions from franchise agreements.

In addition to general comments on the proposed rule, the FTC is soliciting comments on whether franchisees should be covered by the rule, whether senior executives should be exempted or subject to a rebuttable presumption rather than a ban, and whether low and high-wage workers should be treated differently.

If the rule goes into effect it is expected to face legal challenges related to the FTC’s rulemaking authority, which may delay its implementation. However, even if the rule does not go into effect, the FTC is likely to continue to test its enforcement authority under Section 5 of the FTC Act.

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