

FTC Seeks to Ban Noncompete Agreements in Employment Contracts

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On January 5, 2023, the Federal Trade Commission (“FTC”) announced a broad proposed rule that would ban employers from imposing noncompete clauses on their workers. The FTC press release announcing the proposed rule states that noncompete clauses—which apply to about one in five American workers—suppress wages, hamper innovation, block entrepreneurs from starting new businesses and reduce American workers’ earnings between \$250 billion and \$296 billion per year.^[1] The proposed rule would prohibit employers from: (1) entering into or attempting to enter into a noncompete with a worker; (2) maintaining a noncompete with a worker; or (3) representing to a worker, under certain circumstances, that the worker is subject to a noncompete. The term “worker” covers paid staff in addition to independent contractors and unpaid staff. The proposed rule does not apply to noncompete provisions imposed upon 25% owners of a business in transaction documents related to the sale of the business. The proposal is subject to a 60-day public comment period commencing when the *Federal Register* publishes the proposed rule.

Notably, the rule would require employers to rescind all existing noncompete clauses and inform both former and current workers that their noncompete clauses are no longer in effect. Under the rule, existing noncompete clauses must be rescinded no later than 180 days after the final rule is published. Although the proposed rule does not ban non-disclosure or customer non-solicitation agreements, the rule does seek to prohibit “de facto” noncompete clauses that are “written so broadly that it effectively precludes the worker from working in the same field.” The rule would supersede any state statute, regulation, or order that is inconsistent with the rule. The only exception to the ban permits noncompete clauses entered into by a person who is selling a business or disposing of ownership interest in an business entity in which the individual holds at least a 25%

interest.

The FTC voted 3-1 to publish the Notice of Proposed Rulemaking, which is the first step in the FTC's rulemaking process. FTC Chairperson, Lina M. Khan stated, "[n]oncompetes block workers from freely switching jobs, depriving them of higher wages and better working conditions, and depriving businesses of a talent pool that they need to build and expand. By ending this practice, the FTC's proposed rule would promote greater dynamism, innovation, and healthy competition."^[2] FTC Commissioner Christine S. Wilson wrote a dissent arguing that the FTC lacks rulemaking authority to eliminate unfair methods of competition and that noncompete agreements must be analyzed under a fact-specific inquiry because they could have legitimate business justifications.^[3] The FTC's announcement of its proposed rule comes only one day after issuing a [press release](#) that it was taking legal action against three companies and two individuals who "illegally" imposed non-compete restrictions on thousands of workers.

The FTC's proposed blanket ban on noncompete agreements furthers the agency's commitment to advancing the Biden Administration's policy to promote competition in U.S. labor markets. On July 9, 2021, President Biden signed an [Executive Order](#) encouraging the FTC to use its rulemaking authority "to curtail the unfair use of noncompete clauses and other clauses or agreements that may unfairly limit worker mobility." President Biden called this proposed rule "a huge step forward in banning noncompete agreements that are designed simply to lower people's wages." It also arrives on the heels of the FTC's recent policy statement expanding its powers under Section 5 of the Federal Trade Commission Act "to identify unfair forms of competition."^[4]

The business community is voicing significant criticism of the proposed rule. Banning noncompete agreements without exception (unless in the context of the sale of a business) would allow employees who could disclose highly valuable business information to go to a competitor without any real barrier. Employers would be forced to rely on trade secret statutes and common law remedies to seek redress to protect their interests. If implemented, we would expect litigation challenging the scope of the proposed rule as well as the scope of the FTC's administrative and constitutional authority to promulgate and enforce the rule. Once the rule is finalized, companies and individuals will need to carefully consider both their present and prospective employment agreements with respect to noncompete clauses and NDAs to determine the proper means to comply with the proposed rule's broad set of prohibitions.

Jake Walker also contributed to this article.

FOOTNOTES

^[1] Federal Trade Commission, Non-Compete Clause Rulemaking (January 5, 2023).

^[2] Federal Trade Commission, FTC Proposes Rule to Ban Noncompete Clauses, Which Hurt Workers and Harm Competition (January 5, 2023).

^[3] Federal Trade Commission, Dissenting Statement of Commissioner Christine S. Wilson Regarding the Notice of Proposed Rulemaking for the Non-Compete Clause Rule (January 5, 2023).

^[4] Federal Trade Commission, Statement of the Commission on the Withdrawal of the Statement of Enforcement Principles Regarding "Unfair Methods of Competition" Under Section 5 of the FTC Act (July 9, 2021).

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