sussman shank LLP

ARTICLES

FTC Issues Final Rule Banning Non-Compete Agreements

MAY 01, 2024

By Steven F. Cade, Tyler J. Volm, and Paxton L. Deuel

On April 23, 2024, the federal government banned nearly all non-compete agreements by administrative action. If it survives legal challenges, the ban will represent a tidal sea change in employment law. Agreements to protect confidential information are not affected. Employers with existing agreements which have non-compete components will have new notice obligations to their employees.

The 3-2 vote by the Federal Trade Commission ("FTC") is already being challenged in court as an improper exercise of the FTC's statutory authority, and so it is possible the rule will be delayed or struck down before the effective date. However, employers should start planning now because absent court action, the rule will take effect in approximately four months.

The FTC estimates that about 18 percent of U.S. workers (or approximately 30 million people) are presently covered by non-compete agreements. Further, the FTC claims that these non-compete agreements reduce workers' wages, suppress innovation, and run counter to sustaining a free and fair economy. According to the FTC, banning non-competes will increase workers' earnings by nearly $300 billion and strengthen America's workforce. Consequently, such a ban will also require employers to pivot and rely on trade secret protections and non-solicitation provisions to protect confidential information.

A. Key Provisions

The FTC's new rule provides that it is an unfair method of competition—and thus a violation of section 5 of the Federal Trade Commission Act ("FTC Act") (15 U.S.C. §45) — for an employer to enter into or enforce, or attempt to enter into or enforce, a non-compete clause with a worker. 16 CFR § 910.2. The rule defines a "non-compete clause" as a "term or condition of employment that prohibits a worker from, penalizes a worker for, or functions to prevent a worker from (i) seeking or accepting work in the United States with a different person where such work would begin after the conclusion of the employment that includes the term or condition; or (ii) operating a business in the United States after the conclusion of the employment that includes the term or condition." 16 CFR § 910.1(1).

The rule applies to nearly all workers, and includes both employees and independent contractors. There are only three narrow exceptions:

1. *Senior Executives.* The rule does not apply to *existing* non-compete agreements entered into with senior executives. Thus, non-compete agreements with senior executives entered into before the rule goes into effect will remain enforceable. "Senior executives"are defined as workers at the level of president, chief executive, or a substantially similar position that have policy-making authority and earn more than $151,164 annually. Notably, enforceable non-compete agreements with senior executives will still need to comply with Oregon's restrictions on non-compete agreements under ORS 653.295.

- *Sale of Business.* The rule does not apply to non-competes entered into by a person pursuant to a bona fide sale of a business, sale of a person's ownership interest in a business, or sale of substantially all of a business's assets.
- *Existing Causes of Action.* The rule does not apply where a cause of action related to a non-compete clause accrued *prior* to the effective date of the rule. A cause of action for a non-compete agreement accrues when there exist sufficient facts to initiate a legal action against another party.

It is also worth mentioning that the rule will not apply to workers outside of the FTC's jurisdiction, which includes employees of certain not-for-profit corporations.

B. Notice Requirement

For each existing non-compete agreement that is subject to the rule (including non-competes with former workers), the rule requires the employer to deliver a notice. The notice must include "clear and conspicuous notice" that the non-compete clause is no longer legally enforceable. Methods of delivery include: hand-delivery, mailing, emailing, or text message, these notices must go out in a timely fashion.

C. Legal Challenges

The rule has already spurred legal challenges, including a lawsuit filed by the U.S. Chamber of Commerce in federal court in the Eastern District of Texas and another by Ryan Tax Firm in the Northern District of Texas. Additional lawsuits will likely be filed over the coming weeks. The legal issues include whether the FTC has the statutory authority under section 5 of the FTC Act to promulgate the non-compete ban and whether the FTC's decision to ban non-competes was "arbitrary and capricious" under the Administrative Procedure Act.

D. Takeaway

Absent a court order enjoining the rule from taking effect, the FTC's rule banning non-compete agreements will go take effect 120 (or approximately four months) after publication in the Federal Register. In the meantime, employers should begin identifying which past and present workers are covered by non-compete agreements to be prepared to provide the required notice to workers if and when the rule takes effect. Employers should also review their trade secret protocols, confidentiality agreements, and non-solicitation agreements.

Sussman Shank LLP is actively monitoring new developments as they unfold. For more information and guidance on the rule and how it will affect employers and workers alike, please contact the attorneys at Sussman Shank LLP.

The full text of the FTC's rule is available here.

About the Authors

Steven F. Cade is a partner and trial lawyer in the litigation department at Sussman Shank LLP. With a diverse practice, he navigates the complexities of working with creditors and debtors, handling cases ranging from agriculture, to construction litigation and products liability.

Tyler J. Volm is a partner of the firm's Business and Employment Practice Groups. Tyler's practice is focused on business matters, including labor and employment, civil litigation, real estate and tax.

Paxton L. Deuel is an attorney in the business and litigation departments at Sussman Shank LLP. His practice consists of a wide range of matters including business transactions, business disputes, employment matters, and litigation.

Related Attoneys

Steven F. Cade

Partner
503.243.1655
scade@sussmanshank.com