

FTC Votes to Ban Noncompetes

April 25, 2024 Laura O'Donnell, Michael Lombardino, Dominique Baldwin

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As foreshadowed in our prior [update](#) about the proposed rule, on April 23, 2024, the Federal Trade Commission (“FTC” or “Commission”) voted 3-2 to issue a [final rule](#) that will prevent “for-profit” employers from enforcing noncompetes against their employees and other workers, including traditional employees, independent contractors, interns, and volunteers—and, potentially, partners or members of business entities. As we explained in a [post](#) last fall, noncompete clauses are found in a variety of contracts ranging from IP licenses to employment agreements. The FTC’s new rule becomes effective 120 days after it is published in the Federal Register.

The Final Rule

The final rule, similar to the draft rule previously circulated, prohibits employers from enforcing noncompete clauses that restrict or penalize the workers for seeking employment with competitors after leaving their current position. The rule deems the use of noncompete clauses as an unfair method of competition. Once effective, the rule will apply to all future agreements containing noncompete restrictions. It will also apply retroactively to preexisting noncompetes, with an exception for those entered into with “senior executives.” According to the FTC, existing noncompetes with senior executives will be exempt from the ban “because this subset of workers is less likely to be subject to the kind of acute, ongoing harms currently being suffered by other workers. The rule defines a “senior executive” is a worker who (i) was in a policy making position and (ii) received (on an annualized basis) at least \$151,164 in the preceding year, excluding most benefits. The final rule requires employers to send notice to workers who have signed agreements containing noncompete clauses, informing them of their unenforceability.

Exceptions

There are a few minor exceptions to the application of the final rule. The most notable exception provides the ban does not apply to a noncompete clauses entered into by a person pursuant to a bona fide sale of (i) a business entity, (ii) the person’s ownership interest in a business entity, or (iii) all or substantially all of a business entity’s operating assets.

FTC’s Reasoning

The Commission reasons that noncompete clauses are an unfair method of competition that will suppress new business formation and innovation. The FTC predicts that the final rule will increase individual worker earnings by close to \$500 billion dollars over the next ten years. The FTC also predicts that the new rule will lead to over 8,500 new businesses per year and increase workers’ pay by an average of \$524 per year.

In its summary of the proposed final rule, the FTC noted the overwhelming amount of support received via public comment. The FTC stated that 26,000 comments were received, more than 25,000 of which favored the proposed final rule.

Opposition to the Rule

Two of the five FTC commissioners voted against the rule. The opposing commissioners explained their principal concern is whether the FTC has the legal authority to issue such a ban on noncompetes; not with the rationale or justification of the ban itself.

The opposing commissioners voiced concerns the new rule may exceed the authority congress vested in agencies and infringes on Article 1 of the Constitution, which vests law making power in Congress. The U.S. Supreme Court has repeatedly invoked the major questions doctrine to strike down other regulations issued by federal agencies for just this reason. At least one of the dissenting commissioners also raised concerns about whether the FTC has the authority to nullify preexisting and private contracts. There have already been challenges to the final rule, with at least one company filing a complaint in federal court yesterday afternoon and, consistent with U.S. Chamber of Commerce President and CEO Suzanne P. Clark's [statement](#) vowing to sue the FTC and "block this unnecessary and unlawful rule and put other agencies on notice that such overreach will not go unchecked." The U.S. Chamber filed a Complaint yesterday in the United States District Court for the Eastern District of Texas seeking declaratory and injunctive relief.

Takeaway

The final rule will experience numerous legal challenges that will likely delay the effective date of the final rule and possibly defeat the application of the final rule all together. Even if the final rule does not go into effect, issuance of this rule is a further example of the disfavor that government agencies continue to show noncompete agreements. All businesses that require workers to sign agreements with noncompete restrictions should keep an eye out for additional developments as well as further developments at the state law level. Please contact your Haynes Boone attorney if you have any questions or guidance of how the FTC's new rule may impact your business or workforce.