CLIENT ALERT: FTC Focuses Attention on Noncompetition Agreements and Proposes Ban On Non-Compete Clauses

On January 5, 2023, the Federal Trade Commission ("FTC"), the agency that enforces federal antitrust statutes, issued a proposed rule that, if enacted, would ban all employee non-compete clauses (the "FTC Rule"). The FTC takes the position that non-compete clauses stifle competition and depress employee wages, in violation of federal law. If enacted, the FTC Rule would radically change how businesses operate, and eliminate the use of many types of post-employment contractual obligations typically used to protect confidential information and customer goodwill. The FTC Rule was announced shortly after the FTC issued press releases of its enforcement actions against three private companies that utilized non-competes.

Proposed FTC Rule

The proposed FTC Rule provides that "it is an unfair method of competition for an employer to enter into or attempt to enter into a non-compete clause with a worker; maintain with a worker a non-compete clause; or," under certain circumstances, "represent to a worker that the worker is subject to a non-compete clause." The FTC Rule views non-compete clauses broadly, adopting a "functional test," such that any clause that is a "*de facto* non-compete" – namely, a clause that "has the effect of prohibiting the worker from seeking or accepting employment with a person or operating a business after the conclusion of the worker's employment with the employer" – would be banned. The only exception to the ban of non-compete clauses are those entered into in connection with the sale of a business.

The FTC Rule would also require employers that entered into a non-compete clause with a worker to rescind the non-compete clause, providing notice to the employee of the rescission in language proposed by the FTC. If the FTC Rule goes into effect, employers will be required to rescind all of their non-compete clauses within 180 days after publication of the final rule, and to provide notice to all affected workers within 45 days of the clauses' rescission.

The FTC's publication of the FTC Rule is only the first step in the rulemaking process. After publishing a proposed rule, the FTC invites public comment. Thereafter, the final rule (in whatever form it takes) will need to survive legal challenges. Indeed, within hours of publication of the FTC Rule, the United States Chamber of Commerce argued that the ban is "blatantly unlawful," and we expect there will legal challenges to the FTC's authority to promulgate this rule.

FTC Enforcement Actions

The FTC Rule comes shortly after the FTC announced enforcement actions against three companies using non-competes. In those three cases, the FTC alleged a violation of the Federal Trade Commission Act in situations where three private companies used non-compete clauses with their workforce. In each of the three cases, the FTC ordered the companies to cease enforcing, threatening to enforce, or imposing non-compete restrictions on relevant workers. The companies must also notify each affected employee that they are no longer bound by the restrictions. As set out in information released by the FTC, in one case (Prudential Security), the challenge appears to be based on the company's use of non-competes for low-wage workers (security guards). In the second and third cases (O-I Glass and Ardagh Group), the FTC appears to focus on the nature of the industries involved and the limited supply of personnel with the specific skills required for glass container manufacturing. The FTC will be publishing descriptions of the consent agreements in the Federal Register soon.

The FTC is clearly active in the area of noncompetition agreement reform – whether through

rulemaking or enforcement actions. The FTC has indicated that it continues to investigate companies that utilize noncompetition agreements as what it believes to be an unfair business practice. Employers must not only be mindful of state laws that impact the drafting and enforcement of post-employment restrictive covenants, but also any FTC Rule (if it is enacted and survives challenge), as well as the agency's position on enforcement.

MBJ will continue to monitor these developments. In the meantime, please reach out to your MBJ attorney with any questions about drafting and enforcing post-employment restrictions.

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