

Practice Update

FTC Proposes Rule Banning Non-Compete Agreements

January 6, 2023

On January 5, 2023, the Federal Trade Commission (“FTC”) released a proposed rule (the “Proposed Rule”), which, if adopted, would essentially ban virtually all non-compete agreements, with very limited exceptions. The Proposed Rule would supersede any state statute, regulation, or interpretation that is inconsistent with the FTC’s Proposed Rule, marking a significant change to the law applicable to such agreements nationwide.

The Proposed Rule defines “non-compete clause” as “a contractual term between an employer and a worker that prevents 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.” Under the Proposed Rule, employers would be: (i) prevented from entering into non-compete agreements with workers; (ii) required to issue a rescission of existing non-compete agreements with current and former employees; and (iii) required to provide current and former workers with notice that the worker’s non-compete clause is no longer in effect and may not be enforced against the worker, within 45 days of rescinding the non-compete clause.

Further, the Proposed Rule implements a “functional test for whether a contractual term is a non-compete clause” whereby a non-compete clause is “a contractual term that is a *de facto* non-compete

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clause because it 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," including a non-disclosure agreement "that is written so broadly that it effectively precludes the worker from working in the same field after the conclusion of the worker's employment with the employer." Accordingly, the Proposed Rule could apply to not only non-compete clauses, but to broadly written non-disclosure agreements, as well.

As drafted, the Proposed Rule would impact almost all workers, including employees, independent contractors, externs, interns, volunteers, apprentices, and sole proprietors. The Proposed Rule would include a limited exception for non-compete clauses between the seller and buyer of a business. This exception would only be available where the party restricted by the non-compete clause is an owner, member, or partner holding at least a 25% ownership interest in a business entity. However, the application of the Proposed Rule, as drafted, remains especially unclear with respect to this exception, as the FTC does not clearly indicate whether non-competes will be permitted (i) for individuals selling their ownership interest in a business entity regardless of percentage owned; in addition to (ii) the owners of a business selling the business entity's assets, where the owner has at least a 25% ownership interest in the entity.

The Proposed Rule is now subject to a 60-day public comment period. Thereafter, the Proposed Rule will be enacted by the FTC, subject to legal challenges regarding the FTC's statutory authority to promulgate unfair methods of competition rulemaking in this manner. The U.S. Chamber of Commerce already has released a statement, recognizing that the FTC's "outright ban [on] noncompete clauses in all employer contracts is blatantly unlawful. Since the [FTC's] creation over 100 years ago, Congress has never delegated the FTC

anything close to the authority it would need to promulgate such a competition rule.”

Akerman will continue to closely monitor the developments and can be reached with any questions on currently drafted restrictive covenants and the enforcement thereof.

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