

Practice Update

New FTC Rule Spares Non-Compete Clauses That Bind Franchisees, But Bans Most “Worker” Non-Compete Clauses

April 26, 2024

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On April 23, 2024, the Federal Trade Commission (FTC) voted to issue a Non-Compete Clause Rule that would ban most non-compete clauses in agreements between businesses and their “workers.” The final rule will take effect 120 days after it is published in the Federal Register, unless a court enjoins it from taking effect. That is certainly a possibility, since Ryan, LLC, a global tax services firm, and the U.S. Chamber of Commerce and three other trade associations filed lawsuits challenging the final rule on April 23, 2024 and April 24, 2024 in Texas federal courts (*Ryan, LLC v. FTC*, N.D. Texas, No. 3:24-cv-00986-E, and *Chamber of Commerce, et al. v. FTC and Lina Kahn*, E.D. Texas, No. 6:24-cv-00148-JCB).

If the final rule takes effect, it will ban most non-compete clauses in agreements involving “workers.” A “worker” is defined broadly to include “a natural person who works or who previously worked, whether paid or unpaid, without regard to the worker’s title or the worker’s status under any other State or Federal laws, including, but not limited to, whether the worker is an employee, independent contractor, extern, intern, volunteer, apprentice, or a sole proprietor who provides a service to a person.” Even a “senior executive” is considered a “worker” for purposes of any agreement executed after the final rule takes effect.

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The final rule will prohibit or nullify many non-compete clauses that bind staffers of franchisors and franchisees. The final rule also will prohibit or nullify certain expansive non-compete clauses included in franchise agreements that extend to franchisees' managers or other personnel.

Franchisors will need to review the agreements in their franchise disclosure documents, as well as all related agreements that they may be using, such as confidentiality or non-disclosure agreements, non-solicitation or non-recruitment agreements, training-repayment agreements (which the FTC calls TRAPs), and severance agreements, to ensure that those agreements do not function as non-compete agreements or contain banned non-compete clauses.

If the final rule takes effect, it will not apply to a "franchisee in the context of a franchisee-franchisor relationship," which the FTC finds to be "more analogous to the relationship between two businesses than the relationship between an employer and a worker." This, at least, should be a relief to franchisors since they commonly use non-compete clauses to protect their goodwill, trade secrets, and other investments in their brands.

The rule deviates little from the proposed rule published in January 2023. However, in the notice of proposed rulemaking for the rule, the FTC specifically sought comment on whether the rule should also cover non-compete clauses in franchise agreements. In the statement accompanying the final rule, the FTC summarizes the comments received for and against this point, explains that the evidentiary record before it "continues to relate primarily to non-competes that arise out of employment," and concludes that the rule should not extend to non-compete clauses arising out of the franchisor-franchisee relationship.

As noted by the FTC, non-compete clauses in agreements between franchisors and franchisees remain subject to state common law and federal and state antitrust laws.

Even though the final rule does not apply to the franchisor-franchisee relationship, it remains to be seen whether judges and arbitrators will take a harder look at non-compete clauses in franchise agreements. We expect to see more challenges to franchisee non-competes given the current political climate. Indeed, we have observed a similar phenomenon regarding joint employer liability, which has resulted in more plaintiffs' lawyers attempting to hold franchisors liable for franchisees' conduct.

For more information on the final rule, check out [this recent Blog Post](#) on Akerman's HR Defense blog. Contact a member of Akerman's Franchise and Licensing Sector Team if you need further guidance on this or other franchise-related issues.

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