CLIENT ALERTS & INSIGHTS

The FTC Voted to Enact its Non-Compete Ban – What You Need to Know and What You Need to Do

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A few minutes ago, the FTC voted to enact its Rule to ban Non-Compete Agreements/Clauses. The vote to enact the Rule comes as no surprise but there were two noticeable changes to the Rule that was originally proposed and the Rule that the FTC is now trying to enact. One, the Rule does not apply to the sale of a business. Two, non-competes with "senior executives" (defined below) that are currently in effect will remain enforceable but companies will not be able to enter into new non-competes with senior executives.

The Rule will receive significant media attention. Yet, the Rule is not, or at least not yet, a death blow to non-competes. Lawsuits will be filed shortly to enjoin the Rule and we expect the Rule will be enjoined. Below is a short Q&A about the Rule and what companies should do now that the Rule has been enacted. (Spoiler Alert: the answer is "**nothing**")

Q: What does the Rule exactly state about banning Non-Competes?

Here is the text of the Rule:

Unfair methods of competition-(1) Workers other than senior executives. With respect to a worker other than a senior executive, it is an unfair method of competition for a person:

(i) To enter into or attempt to enter into a non-compete clause;

(ii) To enforce or attempt to enforce a non-compete clause; or

(iii) To represent that the worker is subject to a non-compete clause.

(2) Senior executives. With respect to a senior executive, it is an unfair method of competition for a person:

(i) To enter into or attempt to enter into a non-compete clause;

(ii) To enforce or attempt to enforce a non-compete clause entered into after the effective date; or

(iii) To represent that the senior executive is subject to a non-compete clause, where the non-compete clause was entered into after the effective date.

Q: How does the Rule define a Non-Compete clause?

According to the rule, a "*non-compete clause* means a contractual term between an employer and a worker that prevents the worker from a) seeking or accepting work in the United States with a person" or b) "operating a business in the United States after the conclusion of the [worker's] employment."

Q: Does the Rule affect Non-Solicits?

Possibly. The Rule's non-compete definition essentially creates a test for whether the clause/agreement is considered a non-compete. Under the Rule, any clause that has the effect of prohibiting the worker from seeking or accepting employment or operating a business after the conclusion of the worker's employment is banned. In other words, the label of the restriction does not matter. Rather, if the restriction prohibits the employee from taking a role with a new employer, then the restriction violates the Rule and is unenforceable. For example, if a court finds that a customer nonsolicit prevents a salesperson from going to work for a competitor, then the nonsolicit violates the Rule and is unenforceable. Naturally, if the Rule is enacted (and, again, we believe the Rule will be enjoined shortly), the legal fight will be over whether the nonsolicit, confidentiality clause or other restriction prevents the employee from working for a competitor.

Q: Is the ban retroactive?

Mostly yes. All non-competes, outside of those with senior executives, are banned regardless of when the non-competes were executed. For senior executives, all existing non-competes with senior executives will remain enforceable. A senior executive under the Rule is a worker who:

(1) Was in a policy-making position; and

(2) Received from a person for the employment:

(i) Total annual compensation of at least $151,164 in the preceding year; or

(ii) Total compensation of at least $151,164 when annualized if the worker was employed during only part of the preceding year; or

(iii) Total compensation of at least $151,164 when annualized in the preceding year prior to the worker's departure if the worker departed from employment prior to the preceding year and the worker is subject to a non-compete clause.

A "policy-making position" means:

> a business entity's president, chief executive officer or the equivalent, any other officer of a business entity who has policy-making authority, or any other natural person who has policy-making authority for the business entity similar to an officer with policy-making authority. An officer of a subsidiary or affiliate of a business entity that is part of a common enterprise who has policy-making authority for the common enterprise may be deemed to have a policy-making position for purposes of this paragraph. A natural person who does not have policy-making authority over a common enterprise may not be deemed to have a policy-making position even if the person has policy-making authority over a subsidiary or affiliate of a business entity that is part of the common enterprise.

As noted above, companies cannot enter into a noncompete with a senior executive after the Rule goes into effect. And yes, there will be litigation over whether a worker is in a "policy making position."

Q: Does the Rule apply to Independent Contractors?

Yes. The Rule covers "employees, individuals classified as independent contractors, externs, interns, volunteers, apprentices, or sole proprietors who provide a service to a client or a customer."

Q: Does the Rule apply to the Sale of a Business?

No. The Rule does not apply "to a non-compete clause that is entered into by a person pursuant to a bona fide sale of a business entity, of the person's ownership interest in a business entity, or of all or substantially all of a business entity's operating assets." This is a significant departure from the original text of the Rule that invalidated a non-compete against a seller who held less than a 25% ownership interest in the selling entity.

Q: What about state laws that cover noncompetes?

The Rule "supersedes," replaces and voids any state statute or case law that upholds a non-compete.

Q: When does the Rule go into effect?

If not enjoined, the Rule will go into effect 120 days after the Rule is published in the Federal Register.

Q: What should I do?

For now, **nothing**. As we previously reported in our 2023 Year in Review and Q1 2024 Trade Secrets/Non-Compete reports, several lawsuits will be filed in the next couple of days seeking to enjoin the Rule from being enacted. The courts will likely decide whether to enjoin the Rule in the next couple of weeks and we expect the courts to enjoin the Rule. The Rule will then be stayed while the litigation works its way through the court system. In addition, the Rule is likely to be rescinded if a new President is elected in November.

Q: What if the courts allow the Rule to go into effect?

If the courts allow the Rule to go into effect, then companies "must provide clear and conspicuous notice to the worker by the effective date that the worker's non-compete clause will not be, and cannot legally be, enforced against the worker." The notification has to a) identify the company that entered into the noncompete with the worker and b) be "paper delivered by hand to the worker, by mail at the worker's last known personal street address, by email at an email address belonging to the worker, including the worker's current work email address or last known personal email address, or by text message at a mobile telephone number belonging to the worker."

The FTC has provided the following sample notice:

A new rule enforced by the Federal Trade Commission makes it unlawful for us to maintain a non-compete clause in your employment contract. As of [DATE 180 DAYS AFTER DATE OF

PUBLICATION OF THE FINAL RULE], the non-compete clause in your contract is no longer in effect. This means that once you stop working for [EMPLOYER NAME]:

- You may seek or accept a job with any company or any person-even if they compete with [EMPLOYER NAME].
- You may run your own business-even if it competes with [EMPLOYER NAME].
- You may compete with [EMPLOYER NAME] at any time following your employment with [EMPLOYER NAME].

The FTC's new rule does not affect any other terms of your employment contract. For more information about the rule, visit https://www.ftc.gov/legal-library/browse/federal-register-notices/non-compete-clause-rulemaking.

Q: Who can I talk to if I have additional questions about the Rule?

Benesch's Trade Secrets, Restrictive Covenants and Unfair Competition Group is here to answer any questions you may have regarding the Rule, the upcoming litigation, whether your restrictions may be covered by the Rule, and/or how to notify your workers if the Rule actually takes effect.

For more information, contact:

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