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# FTC Adopts Broad Ban on the Use of Non-Compete Clauses in Employment Agreements


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The Federal Trade Commission has adopted a final rule (the "Rule") declaring it to be an unfair method of competition:

- With respect to ***a worker*** other than a senior executive:
    1. To enter into or attempt to enter into a non-compete clause;
    2. To enforce or attempt to enforce a non-compete clause; or
    3. To represent that the worker is subject to a non-compete clause.
- With respect to a ***senior executive***:
    1. To enter into or attempt to enter into a non-compete clause;
    2. To enforce or attempt to enforce a non-compete clause entered into after the effective date of the Rule; or
    3. 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 of the Rule.

A non-compete clause is:

- A term or condition of employment that prohibits a worker from, penalizes a worker for, ***or functions to prevent***, a worker from:
    - Seeking or accepting work in the United States with a different person where such work would begin after the conclusion of the employment that includes the term or condition; or
    - Operating a business in the United States after the conclusion of the employment that includes the term or condition.

The Rule:

- was published in the Federal Register on May 7, 2024, and will take effect on September 4, 2024;
- preempts state law and state regulation with respect to such clauses, unless state law or state regulation is more restrictive;

- requires “clear and conspicuous” notice to each worker, other than senior executives, subject to a non-compete clause, that enforcing or attempting to enforce the non-compete clause will not be and cannot legally be, enforced against the worker;

- permit the continued enforcement of existing non-compete agreements with senior executives, whereas for other workers all non-competes (even existing) will become unenforceable;

- 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;

- does not prohibit non-compete agreements between a franchisor and franchisee (but such agreements remain subject to the antitrust laws), but does prohibit non-compete agreements between natural persons who work for either a franchisee or franchisor; and

- adopts a functional test towards identifying non-compete clauses, noting that other restrictive employment covenants may be a non-compete clause if the covenant expressly prohibits a worker from, or penalizes a worker for, seeking or accepting other work or starting a business, or, if it does not do so expressly but is so broad or onerous in scope that it functionally has the same effect as preventing a worker from doing the same.

The Rule identifies a few exceptions: (i) the bona fide sale of a business, discussed above; (ii) existing causes of action related to a non-compete clause accrued prior to the effective date of the Rule; and (iii) good faith belief that the Rule is inapplicable. Additionally, because the FTC does not have jurisdiction over non-profit entities, the Rule does not apply to non-profit entities.

The vote to adopt the Rule was 3-2, with the two newest Commissioners voting against adoption, and both noting their belief that the FTC did not have authority to promulgate rules defining conduct as an unfair method of competition, nor a rule with the breadth and scope of this Rule. There is substantial recent literature on the authority of the FTC to issue so-called “competition rules” with much of it questioning whether the FTC will be able to sustain such rules. Affected businesses and their trade association representatives are likely to have substantial grounds for seeking to delay implementation of the Rule, and, ultimately, to reverse or substantially narrow the Rule. Litigation has already commenced, including in Federal District Court in Pennsylvania and Texas. The U.S. Chamber of Commerce also filed a complaint in Federal Court in Texas for Declaratory and Injunctive Relief, and its President and CEO, Suzanne P. Clark, declared the FTC’s decision to ban employer noncompete agreements as “not only unlawful but also a blatant power grab that will undermine American businesses’ ability to remain competitive.” However, in line with the first to file rule, the Court sided with the FTC and suspended the Chamber’s action, allowing the Chamber instead to join existing litigation already filed in District Court in Texas.

Uncertainty with respect to whether the FTC can sustain the Rule, after judicial review, makes it likely that states and localities will continue to legislate and regulate on this issue. Recently, after the Governor of New York and the State Legislature could not agree on legislation that would have limited the use of non-compete clauses, the New York City Council proposed its own legislation prohibiting non-compete clauses. The Rule does not preclude additional efforts such as these, and we expect they will continue. Affected parties should take notice of these efforts.

A version of this article was originally produced as a Clients & Friends Memo here.