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A Synopsis of the FTC's Historic Non-Compete Ban

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As you may have heard, on April 23, 2024, in a historic measure, the Federal Trade Commission ("FTC") voted 3-2 to ban almost all employment-based non-competes. Below is a synopsis of what this new ban entails, what types of non-competition restrictions are still enforceable, and how employees and employers should prepare for the future.

What happened?

The FTC approved a final rule (the "Rule") banning a vast majority of employment-based non-competes. The ban goes into effect 120 days after the Rule is published in the Federal Register, which is currently scheduled to occur on 5/7/24. The Rule prohibits a business from imposing a term or condition of employment on a "worker" (including employees, contractors and even volunteers) that "prohibits", "penalizes" or "functions to prevent" a worker from (i) seeking or accepting work in the United States or (ii) operating a business in the United States. The ban applies only to restrictions imposed after a worker's engagement with a business ends; non-competes may still be imposed while a worker is employed/contracted with a business.

Does the rule apply to pre-existing non-competition restrictions?

The Rule is retroactive, meaning that it applies to all employment-based non-competes, regardless of when they were entered into. The Rule does, however, create an exception whereby non-competes entered into with "senior executives" prior to the effective date of the Rule will not be affected by the Rule. After the effective date, new non-competes for senior executives may not be entered into, however.

Who are senior executives?

A "senior executive" is defined as a worker who (i) earned at least $151,164 in "total annual compensation" over the last year (annualized if the person worked less than a full year) and (ii) possesses "policy-making authority", which is "final authority to make policy decisions that control significant aspects of a business entity and does not include authority limited to advising or exerting influence over such policy decisions". The authority must be over the entire enterprise, not just a department or division. The commentary published by the FTC along with the Rule makes it clear that the FTC intends to interpret "senior executive" very narrowly.

What do you have to do?

For any businesses that have imposed non-competes on workers, the FTC is requiring those businesses to send out formal notices to the impacted workers advising the worker that the business will not and cannot enforce the non-compete clause. The notices must be sent out on or before the effective date of the Rule. Model notice language has been provided by the FTC.

Should you cease any pending non-compete litigation?

Despite being retroactive, the Rule "do[es] not apply where a cause of action related to a non-compete clause accrued prior to the effective date." This means that, to the extent a worker breaches (or has already breached) a non-compete prior to Rule becoming effective, a business may still bring (or continue) a cause of action against the worker.

Does the Rule apply to all businesses?

The Rule applies to the vast majority of business; however, by statute, the FTC does not have authority over certain types of businesses, and thus this Rule does not apply to all businesses. Most importantly, the Rule does not apply to any business that is not "organized to carry on business for its own profit or that of its members". Typically, this has been read to mean that the FTC does not have authority over non-profits. However, in commentary published along with this new Rule, the FTC was very clear that not all non-profits are exempt. The FTC will undertake its own fact-specific analysis to determine if an entity was "organized to carry on business for its own profit", and will not simply rely on the determination of other entities, such as the Internal Revenue Service. In fact, the FTC has boldly stated that it believes at least some non-profit hospitals will likely be subject to the Rule.

What about non-competition restrictions outside the employment context?

The Rule does not apply in the context of "bona fide" sales of (i) a business entity, (ii) a person's ownership interest in a business entity, or (ii) all or substantially all of a business entity's operating assets. Thus, non-competes imposed as a condition of becoming a shareholder of a business may still be enforceable. However, the bona fide sales exception applies only to owners / "sellers" (as described in the commentary to the Rule), not mere non-equity employees who continue employment after a sale.

Can you still impose NDAs or non-solicits?

While the Rule does not outright ban non-disclosure agreements ("NDAs") or non-solicits, an NDA or non-solicit may not be so broad as to function as a de facto non-compete. Per the FTC, an example of an over-broad NDA that functions as a de facto non-compete would be "an NDA that bars a worker from disclosing any information or knowledge the worker may obtain during their employment whatsoever, including publicly available information."

How will the FTC enforce the Rule?

Interestingly, there is no private right of action to enforce this Rule, and the FTC does not have the power to impose civil penalties against businesses for trying to enforce a non-compete. As of now, all we know about enforcement of the Rule is that, starting as of the effective date, suspected violations may be reported to the FTC via email at noncompete@ftc.gov.

Won't this Rule be challenged in court?

Promptly following the FTC's vote approving the ban, multiple lawsuits were filed (including one by the US Chamber of Commerce) challenging the FTC's authority to promulgate and enforce such a ban. The FTC

certainly anticipated such challenges, as much of the 570+ pages of commentary published with the Rule involves a detailed analysis of how the FTC is within its authority to ban employment-based non-competes. It remains to be seen whether the pending litigation will delay implementation or strike the Rule down in its entirety.

So what now?

Employers and employees should remain alert and observe the pending litigation that may affect the implementation of the Rule. Employers should consult with legal counsel as to what the Rule requires, prepare a form of notice, and begin to identify employees that should receive such notice. Employers should also revisit their current agreements in an effort to determine whether other provisions, such as confidentiality and non-solicitation provisions, should be amended.

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