FOULSTON
ATTORNEYS AT LAW

ISSUE ALERTS

FTC ISSUES PROPOSAL TO BAN NONCOMPETE AGREEMENTS

January 10, 2023

By: Morgan E. Geffre and Scott C. Nehrbass

Last week the Federal Trade Commission ("FTC") proposed a new rule that, as drafted, would ban noncompete clauses in the employment context and void those currently in effect. Noncompete agreements are agreements that restrict an employee's ability to work in their industry for a certain amount of time in a certain geographic location following separation of employment. This rule could have a sweeping effect on noncompete agreements in the United States.

The potential ban will not go into effect until after the 60-day comment period, and 180 days after the FTC issues a final rule, which may look markedly different from the proposed rule. In addition, employers may still be able to protect their legitimate business interests in other ways, such as narrowly tailored non-solicitation agreements.

WHAT DOES THE RULE SAY?

The proposed rule would preclude employers from entering into noncompete agreements with employees, trying to do so, or even suggesting that employees are bound by a noncompete when they are not. The rule covers not just employees but also independent contractors, interns, volunteers, and others.

The proposed rule does not explicitly extend to nonsolicitation or nondisclosure agreements, but it does say that nondisclosure agreements are "de facto" noncompetes if they would effectively preclude an employee from continuing to work in the same field. Contractual terms that require an employee to reimburse the employer for training costs if employment ends within a certain amount of time also operate as a "de facto" noncompete, according to the rule. To avoid FTC scrutiny, the payment must be reasonably related to the costs the employer incurred while training the employee.

There are two exceptions to the ban where noncompete agreements would be allowed: (1) when they stem from an owner or partner who is selling a business or disposing of all ownership interest in a business, and (2) for franchisees in a franchisee-franchisor relationship.

FOULSTON
ATTORNEYS AT LAW

For existing noncompete agreements, the new rule would require employers to give written notice to employees and former employees that their noncompete agreements are being rescinded within 45 days after the final rule goes into effect. The rule provides sample notice language, which advises employees and former employees that they are no longer subject to limitations on working for a competitor or starting a competing business.

WHY?

According to the FTC, noncompete clauses are an unfair method of competition in violation of Section 5 of the Federal Trade Commission Act, which carries steep civil penalties. As stated by the FTC, noncompete agreements "block workers from freely switching jobs, depriving them of higher wages and better working conditions, and depriving businesses of a talent pool that they need to build and expand."

The FTC estimates this new rule would affect 30 million employees currently covered by noncompete agreements. The FTC also calculates that the proposed rule would increase employee earnings between $250 billion and $296 billion per year because noncompete clauses restrict mobility and thus suppress wages.

WHAT'S NEXT?

The FTC is requesting public comment on the proposed rule over the next 60 days. Specifically, the FTC is looking for comments on whether franchisees should be covered, and whether there should be exemptions for senior executives. The FTC is also seeking comment on whether low- and high-wage earners should be treated differently, similar to the carve-outs of states that already limit noncompete agreements. California, North Dakota, and Oklahoma already ban noncompete agreements, while Illinois, Washington, Colorado, Oregon, and others have passed laws that limit their use.

The FTC will then consider those comments before issuing a final version of the rule. A potential noncompete ban would not go into effect until 180 days after the final version is published and may look much different than the proposed rule. Further, it is almost certain that any noncompete ban, and the FTC's authority to issue it, will face legal challenges in the courts.

In the meantime, employers should proactively consider which employees and former employees are currently operating under a noncompete agreement and how the employer's legitimate business interests can be best protected going forward. Employers should review their agreements and consider whether to include additional or alternative language to protect their legitimate business interests, including the use of confidentiality clauses and nonsolicitation clauses, which are framed in such a way as not to be de facto noncompete agreements, to provide an extra layer of protection as a fallback in the event the proposed ban goes into effect and survives legal scrutiny.

FOR MORE INFORMATION

If you have questions or want more information regarding the proposal to ban noncompete agreements, contact your legal counsel. If you do not have regular counsel for such matters, Foulston Siefkin LLP would welcome the opportunity to work with you to meet your specific business needs. For more information, contact **Morgan Geffre** at 316.291.9577 or mgeffre@foulston.com or **Scott C. Nehrbass** at 913.253.2144 or snehrbass@foulston.com. For more information on the firm, please visit our website at **www.foulston.com**.

Established in 1919, Foulston is the largest Kansas-based law firm. With offices in Wichita, Kansas City, and Topeka, Foulston provides a full range of legal services to clients in the areas of administrative & regulatory; antitrust & trade regulation; appellate law; banking & financial services; business & corporate; construction; creditors' rights & bankruptcy; e-commerce; education & public entity; elder law; emerging small business; employee benefits & ERISA; employment & labor; energy; environmental; ERISA litigation; estate planning & probate; family business enterprise; franchise & distribution; government investigations & white collar defense;

governmental liability; government relations & public policy; healthcare; immigration; insurance regulatory; intellectual property; litigation & disputes; long-term care; mediation/dispute resolution; mergers & acquisitions; Native American law; oil, gas & minerals; OSHA; privacy & data security; private equity & venture capital; product liability; professional malpractice; real estate; securities & corporate finance; supply chain management; tax exempt organizations; taxation; trade secret & noncompete litigation; water rights; and wind & solar energy.

RESOURCES

Sign up to receive these issue alerts straight to your inbox **here**.

PRACTICE AREAS

- Noncompete & Trade Secret Litigation
- Employment & Labor