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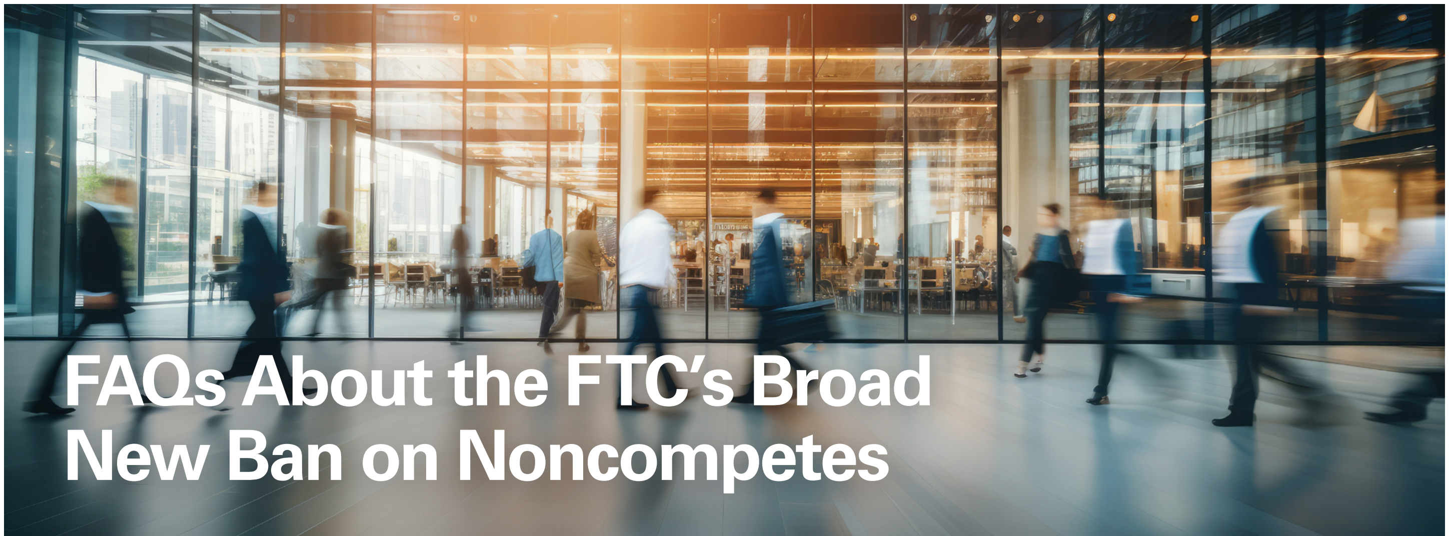

FAQs About the FTC's Broad New Ban on Noncompetes

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Key Points

- The FTC's ban on worker noncompetes is broad, but it allows a few key exceptions, including current noncompetes with "senior executives" and those relating to sales of businesses. And certain entities, including true nonprofits, banks and common carriers are exempt from the rule.
- The rule is set to go into effect on September 4, 2024, but multiple legal challenges have been filed, and decisions are expected in July 2024 that may delay or prevent implementation.
- If it does take effect, employers will need to notify current and former employees with noncompetes that those agreements are no longer enforceable.
- Whether or not the rule takes effect, employers can still use various other contractual means, including NDAs, notice periods and gardening leave provisions, to protect intellectual property and other proprietary information.

When the Federal Trade Commission (FTC) issued its long-awaited final rule banning virtually all noncompete clauses between workers and employers, it also published 500-plus pages of commentary.

Yet since becoming final on April 23, 2024, the rule has presented a host of practical questions that many companies are still working through. And it has already been met with intense criticism and significant legal challenges that may impact when, or even if, the rule will take effect.

We summarized the rule in detail when it was issued. In this article, we consider some of the key takeaways and practical questions relating to the final rule.

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FAQs About the FTC's Broad New Ban on Noncompetes

1. Does the rule really ban *all* noncompetes?

Most, but not all. The rule is very broad. It covers any contract that "prohibits," "penalizes" or "functions to prevent" a "worker" from seeking or accepting work at another employer, or operating a business after they leave a company. The FTC intentionally left flexibility in the rule to potentially encompass practices that are not explicitly prohibited but have the effect of a noncompete.

The definition of "worker" includes all full-time and part-time employees, unpaid volunteers and independent contractors. It is important to note, however, that the ban does not apply to business-to-business noncompetes (*e.g.*, such as participants to a joint venture agreeing to ancillary restrictions on business conduct), though such arrangements must still comply with the antitrust laws.

Despite its breadth, there are a few key exceptions to the rule:

- **Certain companies not bound by the FTC Act.** Banks, loan institutions, federal credit unions, common carriers like railroads and airlines, and nonprofit institutions are not subject to the ban. However, the FTC claims that it does have jurisdiction over tax-exempt corporations that act like for-profit businesses by deriving some profit from their work or paying top management for-profit-level salaries, with a particular focus on health care entities.
- **Noncompetes with "senior executives" entered into prior to the effective date of the rule.** Noncompetes with senior executives will be permitted to stand so long as they are executed before the effective date of the rule. "Senior executives" are employees earning more than $151,164 per year and with "policy-making positions" (a term that will be the subject of interpretation and likely dispute). Notably, companies are free to enter into noncompetes with senior executives before the rule takes effect.
- **Bona fide sales of businesses.** The FTC excluded from the rule noncompetes entered into by a person as part of a sale of (1) a business entity, (2) an ownership interest in a business entity, or (3) all or substantially all of the operating assets of a business entity.
- **Franchisee-franchisor agreements.** Noncompetes included in agreements between franchisors and their franchisees are not banned, but agreements between a franchisor or franchisee and its workers are banned.

2. Does the FTC really have this authority?

The FTC's authority is in sharp dispute. Multiple lawsuits were filed shortly after the FTC announced its final rule. They argue that the rule exceeds the FTC's statutory authority, violates constitutional and federal administrative law, interferes with the domain of state legislatures and ignores potential pro-competitive benefits of noncompetes.

Three challenges of note have been filed:

- *Ryan, LLC v. FTC*, in the U.S. District Court for the Northern District of Texas.
- *Chamber of Commerce v. FTC*, in the U.S. District Court for the Eastern District of Texas.
- *ATS Tree Services, LLC v. FTC*, in the U.S. District Court for the Eastern District of Pennsylvania.

Under the "first to file" rule, the Eastern District of Texas stayed the lawsuit filed by the Chamber of Commerce. The Chamber and various business groups, including the Business Roundtable, then intervened in May 2024 in the *Ryan* lawsuit.

The *Ryan* court indicated it will rule on the request for a stay and preliminary injunction by early July 2024. The ATS Tree Services court promised a decision on the preliminary injunction motion before it by July 23, 2024. That means at least two courts are expected to issue decisions on the FTC's authority before the rule's effective date.

3. When and how must companies comply?

When: The rule is scheduled to go into effect on September 4, 2024. But the cases mentioned above raise significant questions about the FTC's rulemaking authority and could very well — and are widely expected to — delay or prevent the rule from taking effect. Companies should continue to consider compliance strategies, but we expect court actions to provide some clarity early this summer, well before the rule takes effect.

How: By providing written notice to current and former employees. The rule does not require legal recission of existing noncompetes or employment agreements. But, to comply, employers must provide notice to their employees and former employees by paper, mail, email or text message that their noncompetes are no longer in effect and will not be enforced. The FTC issued model language that will be considered compliant with the notice requirement.

4. What about noncompetes in dissolution provisions of partnership or LLC agreements?

It may depend on the structure. Where a noncompete agreement is executed before the final rule's effective date involving a partner in a business who is responsible for its operations, the FTC has said such a person could qualify as a senior executive — assuming they may have authority to make policy decisions about the business. Further, the FTC noted that partners leaving a business could potentially fall under the "sale of business exception" if the partner was to leave the practice and sell its interests.

As a consequence, it could be advantageous to structure dissolution provisions in partnership or LLC agreements in such a way that the sale of business exception could apply to departing partners or members.

5. My business involves significant proprietary information. What can I do?

Employers can use various alternative terms in employment agreements to protect their legitimate interests. The FTC rule does not preclude employers from using other contractual protections such as customer nonsolicits, nondisclosure agreements, garden leave provisions and notice periods, as long as these provisions do not act as *de facto* noncompetes. Employers may also incentivize employees to not leave for a competitor through compensation, vesting schedules, bonuses with time-based contingencies and other retention tools, though the rule does not permit forfeiture-for-competition clauses.

6. How will the FTC enforce the ban?

The FTC is likely to use its internal administrative process or seek injunctions in court. The FTC has not yet publicly addressed its enforcement strategy. It may pursue administrative proceedings, which can lead to a cease-and-desist order against the offending employer, or it could seek federal court injunctions to force an offender to follow the rule, rescind existing noncompetes or provide proper notice.

The FTC asserts it could impose financial penalties for failure to obey cease-and-desist orders, but it is unlikely to be able to seek direct monetary relief for violations of this competition rule. It contends that its authority for this rule flows from its FTC Act powers to investigate and prevent unfair methods of competition. But that section does not provide a private right of action, nor does it expressly contemplate civil penalties or other monetary relief.

In Sum

Given the pending legal challenges and the ambiguities discussed above, we expect there to be additional developments relating to this rule over the summer. We will be following them closely.

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