

Client Alert: The FTC Proposes Ban on Non-Competes

Publications

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By: Jason M. Bradford, Debbie Berman, Andrew W. Vail, Joseph Torres, Casey L.M. Carlson

Bottom Line: On January 5, 2023, the Federal Trade Commission (FTC) proposed a sweeping new rule which, if enacted in its draft form, would ban virtually all non-competition agreements (non-competes), including those already in effect. The FTC's action comes in response to President Biden's July 2021 Executive Order, which directed the Commission to issue rules limiting non-competes "and other clauses or agreements that may unfairly limit worker mobility."^[1] While the DOJ and FTC have recently pursued litigation and other enforcement actions tackling non-competes and other restrictive covenants,^[2] the FTC had not issued any rules or regulations pursuant to the Order. That changed this week, when the FTC announced a new subchapter entitled "Rules Concerning Unfair Methods of Competition," and presented five proposed provisions under a new Part 910, "Non-Compete Clauses."^{[3][4]}

The proposed rule is open for public comment for 60 days.^[5] Interested companies may submit comments throughout that period—Jenner & Block's experienced FTC team can offer support and guidance in doing so. After the comment period, the agency will finalize the rule, and, 180 days after the final version is published, the rule will become effective.

The Proposed Rule Sweeps Wider Than Most Anticipated

The proposed rule takes a hardline approach to non-competes. It deems "non-competes clauses" prohibitively unfair, and broadly defines such a clause as any "contractual term between an employer and a worker that prevents the worker from seeking or accepting employment with a person, or operating a business, after the conclusion of the worker's employment with the employer."^[6] The rule forbids any workaround that achieves a similar effect. For example, the proposed rule specifically bans nondisclosure agreements that would effectively preclude a worker from working in the same field and prohibits employers from requiring repayment of training costs where the required payment is not related to the costs the employer incurred for training the worker.

Further, the rule requires employers to rescind all violating non-competes and provide employees *and former employees* with notice that any such clause is no longer in effect.^[7] The rule provides model language for such a notice,^[8] although employers are free to fashion their own language so long as the notice informs workers that the non-compete is no longer in effect and may not be enforced against the worker. Importantly, the rules require employers to provide notice to current and former employees before the date that the rule is set to go into effect.

Unlike most state efforts to regulate non-competes,^[9] the FTC's proposed rule only has a single exception for non-competes in connection with the sale of a business. And this exception is far narrower than the clauses used in most major M&A transactions. It only permits non-competes as applied to substantial owners or members of corporations, which is defined as persons owning more than 25% of a business entity. This would prohibit most of the sorts of non-compete terms used in major public company transactions which prohibit senior officers from working for competitors of an acquiring business for a period of time.

Opposition to the Far-Reaching Rule, Including Through Legal Challenges, Is Likely

The rule's vast prohibitions have taken many by surprise and are likely to face legal challenges. Notably, while three FTC Commissioners voted in favor of the proposed rule, Commissioner Christine S. Wilson dissented, stating that the rule "represents a radical departure from hundreds of years of legal precedent" and "bans conduct that courts have found to be legal";^[10] emphasizing that fact-specific inquiries, not bright-line rules, are more appropriate for analyzing non-competes; and pointing to the benefits of non-competes, including incentivizing employers to provide training that could be used in the employment of industry competitors.^[11]

Moreover, the rule is likely to be challenged under the recent evolution of the major questions doctrine, which the Supreme Court expanded last term in *West Virginia v. EPA*, 142 S. Ct. 2587 (2022). In that case, the Court considered administrative agencies' authority to enact rules on "major questions." Specifically, the Court held that administrative agencies may not enact rules that amount to "major policy decisions" or "decisions of vast economic and political significance" without "clear congressional authorization" for such regulatory power.^[12] The FTC invoked Section 5 of the Federal Trade Commission Act in issuing the proposed rule.^[13] This Section empowers the FTC to "prevent persons, partnerships, or corporations . . . from using unfair methods of competition in or affecting commerce and unfair or deceptive acts or practices in or affecting commerce."^[14] "Unfair methods of competition" is precisely the sort language lacking the "clear congressional authorization" required for the historic policy change that the proposed rule sets forth.

Takeaways

Notwithstanding the strong legal challenges that the FTC's proposed rule will likely face, companies that have historically used non-competes should begin to prepare for the proposed rule's

requirement that employers inform current and former employees that their non-competes have been rescinded prior to the effective date of the rule. Outside counsel can assist in drafting the notice to ensure that it complies with the rule while minimizing issues and confusion in the event that the proposed rule is ultimately blocked. And if the proposed rule is instead adopted and upheld, experienced counsel can help navigate issues that may arise with the rule's rescission requirement, particularly as to non-competes where the consideration includes more than just employment (e.g., garden leave or a lump-sum payment upon termination). Experienced outside counsel is also a valuable partner in exploring alternatives to non-competes that help companies achieve legitimate business objectives, such as protection of trade secrets, without running afoul of the proposed rule's prohibition on other restrictive covenants and terms with same effect as non-competes. Jenner & Block's robust Trade Secrets and Restrictive Covenants practice is here to help.

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Footnotes

[1] Biden Administration Announces Plans to Curtail Non-compete Agreements for Workers (July 12, 2021), <https://jenner.com/library/publications/21119>.

[2] *See, e.g.*, Latest Decisions in Criminal No-Poach and Civil Non-Compete Cases Indicate Continuing Scrutiny of Restrictive Covenants (July 12, 2022), <https://www.jenner.com/en/news-insights/publications/client-alert-latest-decisions-in-criminal-no-poach-and-civil-non-compete-cases-indicate-continuing-scrutiny-of-restrictive-covenants>; Department of Justice Prosecutions in Employment-Related Antitrust Suits Fall Flat in Davita, Inc. and Jindal (Apr. 27, 2022), <https://jenner.com/library/publications/21770>; DOJ Continues to Push Against Non-Competes, Non-Solicitations, and Other Post-Employment Restrictions (Mar. 1, 2022), <https://jenner.com/library/publications/21633>.

[3] Non-Compete Clause Rulemaking, Federal Trade Commission (Jan. 5, 2023), <https://www.ftc.gov/legal-library/browse/federal-register-notices/non-compete-clause-rulemaking>.

[4] That same day, the FTC also initiated a series of enforcement actions alleging violations of 15 U.S.C.A. § 45 through non-competes. Consent decrees were entered immediately after the complaints were filed.

[5] Noam Scheiber, "U.S. Moves to Bar Noncompete Agreements in Labor Contracts," The New York Times (Jan. 5, 2023), <https://www.nytimes.com/2023/01/05/business/economy/ftc-noncompete.html>.

[6] Non-Compete Clause Rulemaking, Federal Trade Commission (Jan. 5, 2023), <https://www.ftc.gov/legal-library/browse/federal-register-notices/non-compete-clause-rulemaking>.

[7] *Id.*

[8] *Id.* In pertinent part, § 910.2(b)(2)(C) of the rule recommends the following language: "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].”

[9] State laws limiting the enforceability of non-competes vary, but many include exceptions for high wage workers (e.g., Illinois (820 ILCS 90); Washington (RCW 49.62.020)). Others include an exception for non-competes accompanied by a garden leave provision (e.g., Massachusetts (Mass. Gen. Laws, ch. 149, § 24L)).

[10] To this end, Commissioner Wilson cited to the 7th Circuit case *Snap-On Tools Corp. v. Fed. Trade Comm’n*, 321 F.2d 825 (7th Cir. 1963). This case held that restrictive covenants, such as non-competes, “are legal unless they are unreasonable as to time or geographic scope.” *Id.* at 837.

[11] Dissenting Statement of Commissioner Christine S. Wilson Regarding the Notice of Proposed Rulemaking for the Non-Compete Clause Rule, Federal Trade Commission, Commission File No. P201200-1 (Jan. 5, 2023), https://www.ftc.gov/system/files/ftc_gov/pdf/p201000noncompetewilsondissent.pdf. *See also*, Commissioner Wilson’s Dissenting Statements in three enforcement actions against companies with non-competes announced January 4, 2023 (Dissenting Statement of Commissioner Christine S. Wilson, *In the Matter of O-I Glass, Inc.* and *In the Matter of Ardagh Group S.A.*, Federal Trade Commission, Commission File No. 211-0182 (Jan. 4, 2023), https://www.ftc.gov/system/files/ftc_gov/pdf/wilson-dissenting-statement-glass-container-cases.pdf; Dissenting Statement of Commissioner Christine S. Wilson, *In the Matter of Prudential Security*, Federal Trade Commission, Commission File No. 211-0026 (Jan. 4, 2023), https://www.ftc.gov/system/files/ftc_gov/pdf/wilson_dissenting_statement_-_prudential_security_-_final_-_1-3-23.pdf).

[12] *West Virginia v. EPA*, 142 S. Ct. 2587 (2022).

[13] Non-Compete Clause Rulemaking, Federal Trade Commission (Jan. 5, 2023), <https://www.ftc.gov/legal-library/browse/federal-register-notice/non-compete-clause-rulemaking>.

[14] 15 U.S.C.A. § 45.

Related Attorneys



Jason M. Bradford

Partner

jbradford@jenner.com

+1 312 840 7225



Debbie Berman

Partner

dberman@jenner.com

+1 312 923 2764



Andrew W. Vail

Partner

avail@jenner.com

+1 312 840 8688



Joseph Torres

Partner

jtorres@jenner.com

+1 312 840 8685

Casey L.M. Carlson

Associate

ccarlson@jenner.com

+1 312 982 4839

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