

Non-Competes Under Attack

Publications

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By: Debbie Berman

In January 2023, the Federal Trade Commission (FTC) issued a proposed rule that would render virtually all non-competes, including even most agreed to as part of a sale of a business, unfair methods of competition and, therefore, illegal in response to a Presidential Executive Order. The FTC's rule also would apply to both current and future non-competes and would require employers to proactively notify current and former employees that their non-competes are no longer in effect and cannot be enforced against them. Additionally, the rule contains a "functional test" that captures any workaround that could achieve the same effect as a non-compete, including certain non-disclosure or non-solicitation agreements. While California, North Dakota, and Oklahoma have long banned non-competes, they are used in many other states, including major business states like New York and Delaware, so this rule would interfere with a major way that companies do business in the United States. Because the proposed rule was met with significant pushback from the business community with over 5,000 comments filed, the FTC has delayed the date for the issuance of its final rulemaking to April 2024. However, companies should begin planning now.

In addition, several traditionally pro-business states recently enacted or have proposed legislation that ban most non-competes. For example, a prospective non-compete ban was recently signed into law in Minnesota that bans agreements that restrict employees or independent contractors from working for another employer for a specified period of time, within a certain geographic area, or in a capacity similar to that of their current employment. It also prohibits provisions in employment contracts to evaluate non-competes under a different state's law if the employee is located in Minnesota. Surprisingly, the New York legislature has passed a bill that currently is on the governor's desk to sign or veto that bans agreements restricting virtually all employees or independent contractors from obtaining employment after conclusion of their current term of employment. Like the FTC rule, this bill also applies to other agreements that function similarly to non-competes.

Also, recently the Delaware court, which tends to be very pro-business, invalidated two non-competes that were part of a sale of a business even though such non-competes generally are evaluated using a more lenient standard. Both cases, *Kodiak Bldg. Partners, LLC v. Adams*, C.A. No. 2022-0311-MTZ (Del. Ch. Oct. 6, 2022) and *Intertek Testing Servs. NA, Inc. v. Eastman*, C.A. No. 2022-0853-LWW (Del. Ch. Dec. 7, 2022), involved non-competes with the sold entities' high-level employees made in exchange for significant financial consideration. Yet the court still struck down both agreements as overly broad and not tailored to any legitimate business interest, particularly

because they both prohibited future work far beyond the sold entities’ business activities and geographic reach. In doing so, the court refused to “blue pencil”—or revise to make enforceable—the agreements, finding that rewriting the provisions in favor of the buyer companies would be inequitable.

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Debbie Berman

Partner

dberman@jenner.com

+1 312 923 2764

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