

FTC Publishes Final Rule Effectively Banning Most Employee Non-Compete Clauses

On April 23, 2024, the Federal Trade Commission (FTC) issued a final rule that will effectively prohibit most non-competition clauses and will rescind most existing non-competition clauses. Most paid and unpaid workers, independent contractors, interns and volunteers are covered. The rule may take effect in late August 2024, 120 days after its eventual publication in the Federal Register. However, it has already been challenged in court which may delay or prevent the rule from taking effect. Although no immediate action is necessary, employers should make sure they understand how the rule would affect them and continue to monitor the developments.

The Rule

The rule broadly defines a non-compete clause as: "a term or condition of employment that prohibits a worker from, penalizes a worker for, or functions to prevent a worker from: (i) seeking or accepting work in the United States with a different person where such work would begin after the conclusion of the employment...; or (ii) operating a business in the United States after the conclusion of the employment...." A non-compete clause includes contractual terms and workplace policies, whether written or oral.

The rule prohibits a person from (i) entering or attempting to enter into a non-compete clause; (ii) enforcing or attempting to enforce a non-compete clause; or (iii) representing that a worker is subject to a non-compete clause.

While not specifically prohibiting non-solicitation or non-disclosure covenants, the FTC warns that such covenants, as well as certain employee repayment agreements, can satisfy the definition of a non-compete clause if "they function to prevent a worker from seeking or accepting other work or starting a business after their employment ends." Whether such a covenant meets this threshold is a fact-specific inquiry, which focuses on the *effects* of the clause—meaning that an employer may not know whether its non-solicitation or non-disclosure covenant is lawful or enforceable until *after* it is challenged.

Notice Requirement

The rule requires employers to provide written notice "on paper" to each worker

POSTED:

Apr 25, 2024

RELATED PRACTICES:

[Labor and Employment](#)

<https://www.reinhartlaw.com/practices/labor-and-employment>

[Corporate Law](#)

<https://www.reinhartlaw.com/practices/corporate-law>

[Banking and Finance](#)

<https://www.reinhartlaw.com/practices/banking-and-finance>

[Health Care](#)

<https://www.reinhartlaw.com/practices/health-care>



informing the worker that their non-compete clause will not be, and cannot legally be, enforced against the worker. The FTC has provided a model notice for employers to use to inform workers. This requirement is not limited to current employees; rather, it extends to any worker, current or former, who has entered into an unlawful non-compete clause.

Exceptions

The rule does not apply to non-compete clauses with "senior executives" that exist *before* the rule becomes effective. A "senior executive" is defined under the rule as a worker who (i) is in a policy-making position, and (ii) received total compensation of at least \$151,164 in the preceding year or would have received at least a total of \$151,164 in total compensation if employed for the full year. Total compensation includes salary, commissions, nondiscretionary bonuses and other nondiscretionary compensation. An employee is in a "policy-making" position when he or she is the employer's president, CEO or equivalent, or any other officer, or a worker in an officer-equivalent position, of a business entity who has policy-making authority. The employee must have this authority over the entire enterprise; policy-making authority over a subsidiary or business affiliate is insufficient. Entering into *new* non-compete clauses with "senior executives" after the rule's effective date will be prohibited.

The rule contains the following additional limited exceptions:

- **Sale of a Business:** Non-compete clauses entered into as a part of a bona fide sale (i) of a business; (ii) of a person's ownership interest in a business; or (iii) of all or substantially all of a business's operating assets are excepted. Unlike the initial draft, the final rule does not identify a threshold for interest size to qualify for the exception.
- **Accrued Claims:** The rule does not apply to causes of action that accrue before the rule takes effect, including conduct claimed to violate a non-compete where the conduct preceded the rule's effective date.
- **Good Faith:** The rule provides that it is not an unfair method of competition for a person to seek to enforce a non-compete if the person has a good faith belief that the rule is inapplicable.
- **Non-profits:** The rule does not apply to nonprofit organizations, including nonprofit health care organizations. However, entities claiming tax exempt status, but which are in fact organized for profit, are subject to the rule.



The rule preempts any inconsistent state law, but state laws, regulations, orders or interpretations that provide workers greater protection are not inconsistent with the rule.

What is Next?

Several groups and entities have already filed lawsuits seeking to prevent the rule from taking effect. The lawsuits echo harsh critiques from dissenting FTC Commissioners Holyoak and Ferguson and challenge (i) whether the FTC had constitutional or delegated statutory authority to issue the rule; and (ii) whether the rule violates the "major questions" doctrine.

In response to the lawsuits, a court may enjoin the rule, preventing it from effect pending the outcome of the litigation.

What Employers Should Do Now

No immediate action is required. Employers should continue to monitor legal developments surrounding this rule to know when, and if, it will go into effect. In the meantime, it continues to remain important that all non-compete clauses are tailored as narrowly as possible, and that such restrictions are only imposed on employees who pose a competitive risk. Employers considering entering into a non-compete agreement with an "executive" as defined in the rule, or who may need to revise current agreements with such workers, should do so before the rule takes effect.

Please contact a member of Reinhart's Labor and Employment Team, or your Reinhart attorney if you have any questions or need help reviewing a non-compete agreement.

These materials provide general information which does not constitute legal or tax advice and should not be relied upon as such. Particular facts or future developments in the law may affect the topic(s) addressed within these materials. Always consult with a lawyer about your particular circumstances before acting on any information presented in these materials because it may not be applicable to you or your situation. Providing these materials to you does not create an attorney/client relationship. You should not provide confidential information to us until Reinhart agrees to represent you.