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The FTC's Rulemaking on Non-Compete Agreements with Workers

What You Need to Know

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February 2023

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Christopher Leach is a partner in Mayer Brown's Washington DC office and a member of the Litigation & Dispute Resolution practice, as well as the Cybersecurity & Data Privacy practice. As a former attorney with the US Federal Trade Commission (FTC), his practice focuses on consumer-facing issues, including data privacy, false advertising, marketing practices, and other aspects of customer acquisition. He represents and advises clients in a broad range of industries, including the fintech, financial services, food and beverage, automotive, and telecommunications industries, defending those companies in litigation, before government agencies, and in self-regulatory proceedings such as the National Advertising Division (NAD).



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Gail Levine is a partner in Mayer Brown's Washington DC office, where she co-leads the firm's global Antitrust & Competition practice. She joined Mayer Brown from the US Federal Trade Commission's (FTC) Bureau of Competition, where she served as a deputy director under Chairman Joseph Simons and Acting Chairwoman Rebecca Slaughter. Gail joined the FTC as a deputy director of the Bureau of Competition in 2018. In this role, she supervised over 100 lawyers in five divisions, handling all aspects of antitrust review. She oversaw a wide variety of merger reviews, anticompetitive conduct investigations, and antitrust litigation, particularly in areas such as high-tech, pharmaceuticals, biotech, and health care.



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Nicole A. Saharsky is co-head of Mayer Brown's Supreme Court & Appellate Practice. She focuses her practice on briefing and arguing cases in the US Supreme Court and in the federal and state appellate courts and on developing legal strategy for the trial courts and agency proceedings. She has been identified by the Legal 500 as a "Leading Lawyer" in the Dispute Resolution (Appellate) practice area and ranked in Chambers USA for Appellate Law. She also has been recognized by Washingtonian as one of Washington DC's best lawyers for Supreme Court practice and as one of Washington DC's "most powerful women." In the US Supreme Court, Nicole has argued 30 cases, briefed 46 cases on the merits, and filed hundreds of certiorari-stage briefs and motions.

Non-Compete Ban: A Big Deal



"\$300 BILLION PER YEAR"
– Chair Lina Khan on the estimated effect of the rule on worker earnings



"30 MILLION WORKERS"
contracts would be invalidated
– FTC Proposed Rule



"A SWEEPING PROPOSAL"
– Noam Scheiber, U.S. Moves to Bar Noncompete Agreements in Labor Contracts, NY Times, Jan. 5, 2023



"A RADICAL DEPARTURE"
from hundred of years of legal precedent"
– Commissioner Christine Wilson

Overview



FTC Experience
With Non-
Compete Clauses



Overview Of The
Proposed Rule



Possible Legal
Challenges



What Does This
Mean for Your
Business?

FTC & Non-Compete Clauses

- Starting in 2018, agency repeatedly focuses on non-compete clauses in its non-enforcement work
 - Oct 2018 & June 2019: discussed during Competition & Consumer Protection in the 21st Century
 - Jan 2020: Workshop on Non-Competes in the Workplace
 - Aug. 2021: RFI on Contract Terms that May Harm Competition
 - Dec. 2021: Event on Promoting Competition in Labor Markets
- On January 4, 2023, FTC announced three new enforcement actions alleging that worker non-competes were “unfair methods of competition.”
 - Security guards and glass manufacturing employees

The Proposed Rule - Overview



On Jan. 5, 2023, the FTC released a notice of proposed rulemaking that would prohibit nearly all non-compete contracts between employers and workers



3-1 party-line vote, with Commissioner Christine Wilson dissenting



Would preempt less protective state laws, but allow more restrictive laws



Comments due March 20, 2023

The Proposed Rule - Ban on Worker/Employer Non-Competes

- 3 requirements for employers within 180 days of Final Rule
 - Prohibits non-compete clauses in new contracts between employer & worker
 - Rescission of existing non-compete clauses between employer & worker
 - Notice to workers of rescission
- “Worker” is very broad
 - Any employee, independent contractor, unpaid worker; line worker to the CEO
- Functional definition of “Non-Compete Clause”
 - “has the effect of prohibiting the worker from seeking or accepting employment ... after the conclusion of the worker’s employment”
 - Examples: overly broad non-disclosure agreement or punitive training-repayment requirement

The Proposed Rule – FTC Justifications

- Barring Non-Competes for Non-Senior Executives:
 - Non-compete clauses are “coercive and exploitative at the time of contracting and at the time of a worker’s potential departure.”
 - Impedes competition by restricting the pool of available workers
- Barring Non-Competes for Senior Executives:
 - No concerns regarding coercion or exploitation
 - But may “block potential entrants, or raise their costs, to a high degree”
- Employers to protect interests via non-disclosure agreements and trade secret law

The Proposed Rule – Carveouts

- Applies only to companies subject to FTC jurisdiction
- Only covers agreements with workers
- M&A exception: allows employer/worker non-compete in purchase of a business, but only for worker/owner selling 25% or more of equity
- Exempts non-competes between franchisor/franchisee

The Proposed Rule – Alternatives Considered

- Different application for different type of worker
 - Job function vs. FLSA exemptions vs. earnings threshold
- Operation of the ban on non-competes
 - Total ban vs. rebuttable presumption vs. no prohibition
- Mix & Match
 - *E.g.*, total ban on non-executives and rebuttable presumption of prohibition for senior executives

The Proposed Rule – Rulemaking Process

- Feb. 16, 2023, at noon ET, public forum on proposed rule
 - Event will feature panels of workers subjected to non-compete clauses and businesses with experience with non-compete clauses. Followed by comments from the public via livestream.
- Comments due Mar. 20, 2023 (already >5k submitted)
- FTC will review comments and, possibly, issue a final rule.
 - This comment period is the *only* opportunity to comment before a final rule is published.

Possible Legal Challenges

- Administrative Procedure Act allows challenges to agency rulemaking
 - Must be final agency action
 - Allege that the rule is arbitrary and capricious, exceeds statutory authority, or is unconstitutional (among other grounds)
- File lawsuit in federal district court
 - Because FTC not proceeding under Section 18, 15 U.S.C. § 45(c), which covers cease-and-desist orders, a challenger cannot file in Court of Appeals directly
 - Based on administrative record

Possible Legal Challenges – Unauthorized Rulemaking

- FTC is relying on Section 6(g) of the FTC Act, 15 U.S.C. § 46
 - “From time to time classify corporations and ... to make rules and regulations for the purpose of carrying out the provisions of this subchapter.”
- Can Section 6(g) be used for substantive rulemaking on competition?
 - For decades, FTC treated this as providing only procedural rulemaking authority
 - 1960s/1970s – two substantive competition rules—one withdrawn, the other challenged in court
 - 1973 D.C. Circuit decision in *National Petroleum Refiners* upheld substantive rulemaking authority (but that decision may be open to question)
 - 1975 Magnuson Moss Act codified FTC power to issue substantive consumer protection rules—but did not include a similar power for the FTC to promulgate competition rules

Possible Challenges – Major Questions Doctrine

- Supreme Court decision in *West Virginia v. EPA*:
 - Requires “clear congressional authorization” where “history and the breadth of the authority that the agency has asserted, and the economic and political significance of that assertion, provide a reason to hesitate before concluding that Congress meant to confer such authority.”
- Commissioner Wilson: The FTC’s non-compete rule trips each wire
 - FTC has asserted this authority only once in more than 100 years, and not since 1967
 - Massive economic effect: rescind 30 million contracts and affect \$300 billion a year
 - 47 states allow non-compete clauses that would be rescinded

Possible Challenges – Non-Delegation Doctrine

- Separation-of-powers concept: When Congress delegates legislative authority to administrative agencies, it must provide sufficient guidance/limits. Requires an “intelligible principle.”
- *Schechter Poultry* (1935): Supreme Court struck down FTC rules written under authority to write “codes of fair competition.”
 - Court allowed FTC adjudication on unfair competition, which is “determined in particular instances, upon evidence, in light of particular competitive conditions.”
- Supreme Court is poised to reconsider/strengthen the non-delegation doctrine.

Possible Challenges – Arbitrary and Capricious

- “Arbitrary and capricious” standard looks at the agency’s justifications for a final rule to see if it amounted to sufficiently “reasoned decisionmaking.”
- Possible issues to look for on final rule:
 - How well agency addresses concerns from commenters
 - Agency explanations for different arbitrary lines drawn (e.g., 25% M&A threshold, if certain types of employees are exempt from rule)
 - Whether alternative approaches (NDAs and trade secret law) actually will protect employer interests

What Does This Mean For My Business?

- While ambitious, there is no guarantee that the proposed rule will take effect.
 - FTC could decide not to publish a final rule, or a court could enjoin/vacate the rule
- But even without a non-compete ban, the agency is still interested.
 - Sustained, multi-year attention (2018-present)
 - 3 recent enforcement actions
- Even without a rule, companies that come on the FTC's radar still could be subject to investigation, publicity, and a multi-decade consent order.

Practical Tips

- Consider ensuring that your non-compete agreements protect **legitimate business interests**, like trade secrets and other confidential or proprietary information.
- Make sure those non-compete agreements are **narrowly tailored** to do what you need them to do.
 - Are they longer than you need? *The FTC's three enforcement actions challenged agreements that lasted one year or more.*
 - Same questions for geographic scope and industry scope.



Questions?

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