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FTC Passes Rule Banning Non-Competes

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April 25, 2024 – Earlier this week, on April 23, the Federal Trade Commission ("FTC") promulgated a [Final Rule](#) banning almost all post-employment non-compete agreements between employers and workers in the United States. The Final Rule has limited exceptions for (1) non-compete agreements with "senior executives" that are "existing" as of the effective date of the rule; (2) non-compete actions that have accrued before the rule becomes effective; and (3) non-competes entered into in connection with the sale of a business.

The Final Rule is slated to go into effect 120 days after its publication in the Federal Register (the "Effective Date"). On April 24, the U.S. Chamber of Commerce filed a complaint in the U.S. District Court for the Eastern District of Texas challenging the FTC's authority to issue the rule. The Chamber or other potential challengers to the rule are likely to seek a preliminary injunction blocking the rule from taking effect pending court resolution of its legality.

The Broad Ban

The FTC's Final Rule 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: (1) seeking or accepting work in the United States with a different person where such work would begin after the conclusion of the employment that includes the term or condition; or (2) operating a business in the United States after the conclusion of the employment that includes the term or condition."¹ The Final Rule defines the term "worker" broadly to include employees, independent contractors, externs, interns, volunteers, apprentices and sole proprietors who provide a service to a person (whether an individual or a legal entity).²

All non-competes covered by the Final Rule will be unenforceable following the Effective Date of the rule as "unfair methods of competition" under Section 5 of the FTC Act. Specifically, the Final Rule deems unlawful all these actions following the Effective Date: (i) "to enter into or attempt to enter into a non-compete clause;" (ii) "to enforce or attempt to enforce a non-compete clause;" and (iii) "to represent that the worker is subject to a non-compete clause."³

The Limited Carveouts

While the Final Rule broadly bans non-compete agreements, three limited exceptions apply.

(1) *Limited Grandfathering for Certain Senior Executives*: The non-compete ban does not cover "existing" non-compete agreements with "senior executives." "Existing" non-competes refers to those non-compete agreements "entered into before the final rule's effective date."⁴

The Final Rule defines "senior executives" to include those workers who are both: (i) in "a policy-making position" and (ii) have a total annual compensation of at least \$151,164.

For purposes of this exception:

- a "policy-making position" means "a business entity's president, chief executive officer or the equivalent, any other officer of a business entity who has policy-making authority, or any other natural person who has policy-making authority for the business entity similar to an officer with policy-making authority;" and
- "policy-making authority" means "final authority to make policy decisions that control significant aspects of a business entity or common enterprise," but "does not include authority limited to advising or exerting influence over such policy decisions or having final authority to make policy decisions for only a subsidiary of or affiliate of a common enterprise").⁵

This means that the Final Rule does not prevent businesses from entering into non-compete agreements with "senior executives" prior to the Effective Date. It also does not prevent businesses from enforcing those agreements or representing to a senior executive that they are subject to a non-compete clause *provided* the non-compete was entered into prior to the Effective Date. However, the senior executive exception does not apply to future non-competes, *i.e.*, those not already entered into with a senior executive prior to the Effective Date.

(2) *Accrued Causes of Action*: The Final Rule does not apply where a cause of action related to a non-compete clause accrued prior to the Effective Date.⁶

(3) *Sale of Business Exception*: The Final Rule does not apply to non-competes entered into in connection with a bona fide sale of a business entity, of the person's ownership interest in a business entity, or of all or substantially all of a business entity's operating assets.⁷

Notification Requirement

By the Effective Date, employers must provide workers (including former workers) who are not senior executives written notification that any non-competes existing prior to the Effective Date that they were subject to are no longer enforceable following that date. The notification must be provided before the Effective Date. The Final Rule includes model language for the notification.⁸ The Final Rule does not impose a requirement on businesses to formally rescind existing non-compete provisions that are no longer enforceable following the Effective Date.⁹

Other Restrictive Covenants

The Final Rule does not categorically prohibit other types of restrictive covenants, such as non-disclosure agreements, non-solicitation agreements and no-hire agreements, but the FTC explains in its rulemaking commentary that if such agreements or arrangements are "so broad or onerous" that they have the "functional effect" of a non-compete provision, those will be treated as non-competes under the Final Rule.¹⁰

Violations of the Final Rule

According to the FTC, violations of the Final Rule constitute violations of Section 5 of the FTC Act. Those violations do not provide a private right of action. This means that a private individual, such as an employee, cannot sue an employer for violating the Final Rule; rather any such action would need to be brought by the FTC, consistent with its jurisdiction. This does not prevent employees from suing employers under other applicable laws concerning non-competes, such as applicable state laws.

Relationship with State Laws

The Final Rule purports to supersede any state laws governing non-competes if those laws conflict with the Final Rule. However, the Final Rule does not limit states from enacting and enforcing more restrictive non-compete laws.¹¹

Next Steps

The Final Rule is likely to be tied up in the courts for some time. Currently, the Effective Date of the Rule is four months from when the Final Rule is published in the Federal Register, which could be a matter of days. However, if a preliminary injunction is granted as part of a court challenge to the legality of the Final Rule, that could move the Effective Date further in time.

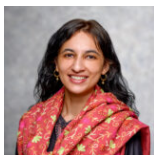
We advise that businesses work with their internal and outside counsel to closely monitor the developments around the Final Rule and work on a plan for various contingencies, including that the Final Rule survives any challenges to its legality.

We also encourage businesses to continue to monitor state law developments related to non-competes. Many states either have or are considering laws that would limit the use of non-competes. For example, California, North Dakota and Oklahoma already prohibit non-competes as void against public policy except in limited circumstances, including in connection with the sale of a business.

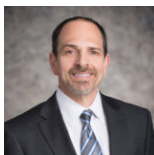
Finally, regardless of whether the Final Rule survives any challenges to it, it is indicative of the general trend towards increased scrutiny and limitation of non-competes. Accordingly, we encourage businesses to assess the need and scope of non-competes for their various business roles. For new contracts, businesses should consider whether they are able to use other forms of restrictions that are less likely to be considered de facto non-compete clauses, such as tailored confidentiality and non-solicitation provisions.

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1. 16 C.F.R. § 910.1 (definitions). [↵](#)
 2. *Id.* (defining a “worker” as, “a natural person who *works* or *who previously worked*, whether paid or unpaid, without regard to the worker’s title or the worker’s status under any other State or Federal laws, including, but not limited to, whether the worker is an employee, independent contractor, extern, intern, volunteer, apprentice, or a sole proprietor who provides a service to a person. The term worker includes a natural person who works for a franchisee or franchisor, but does not include a franchisee in the context of a franchisee-franchisor relationship.”) (emphasis added). [↵](#)
 3. 16 C.F.R. § 910.2(a). [↵](#)
 4. 16 C.F.R. § 910.2(a)(2). [↵](#)
 5. 16 C.F.R. § 910.1 (definitions). [↵](#)
 6. 16 C.F.R. § 910.3(b). [↵](#)
 7. 16 C.F.R. § 910.3(a). [↵](#)
 8. 16 C.F.R. § 910.2(b). [↵](#)
 9. See FTC Final Rule Publication (avail. at <https://www.ftc.gov/system/fil...>) at 210-211. [↵](#)
 10. See, e.g., *id.* at 77-85. [↵](#)
 11. 16 C.F.R. § 910.4. [↵](#)

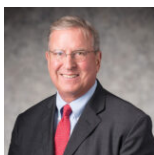
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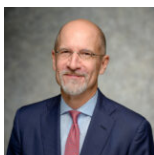
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