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Labor & Employment Alert

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FTC proposes nationwide ban on non-competes

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This proposed rule, which would ban new non-competes and negate many existing agreements if adopted, will have sweeping impacts across all industries.



What's the Impact?

- / The proposed rule covers all "workers," including employees, independent contractors, volunteers, interns, and externs
- / The FTC will accept public comment on the proposed rule for 60 days

On January 5, 2023, the Federal Trade Commission (FTC) issued a proposed rule that would ban non-compete clauses for workers nationwide across all industries. The proposed rule would also require employers to rescind existing non-competes and notify workers, including former employees, that they are no longer in effect.

The FTC will accept public comment on the proposed rule for 60 days and is expected to issue a final rule shortly thereafter. The proposed rule provides that any final rule would become effective 180 days after publication in the Federal Register. Once a final rule is in place, it would be an "unfair method of competition" for any employer to "enter into or attempt to enter into a non-compete clause with a worker; maintain with a worker a non-compete clause; or represent to a worker that the worker is subject to a non-compete clause where the employer has no good

faith basis to believe that the worker is subject to an enforceable non-compete clause.” FTC rules authorize civil penalties of up to \$10,000 for each violation.

The proposed rule covers all “workers,” which, under the Proposed Rule, includes not just employees but also independent contractors, volunteers, interns, and externs. It would apply to all employers, regardless of size or industry.

The term “non-compete clause” is defined broadly as any contractual term “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.” While the proposed rule does not expressly address other restrictive covenants, like customer non-solicitation restrictions, it would impose a “functional test” to determine whether other contractual terms may function like a non-compete and would ban those terms as well. For example, a non-disclosure agreement “that is written so broadly that it effectively precludes the worker from working in the same field after the conclusion of the worker’s employment with the employer” would be banned under this Proposed Rule. So would any contractual term “that requires the worker to pay the employer or a third-party entity for training costs if the worker’s employment terminates within a specified time period, where the required payment is not reasonably related to the costs the employer incurred for training the worker.”

In addition to barring non-competes prospectively, the proposed rule also imposes a “rescission requirement.” As a result, “an employer that entered into a non-compete clause with a worker prior to the compliance date must rescind the non-compete clause no later than the compliance date,” meaning 180 days after any final rule is published. Employers forced to rescind such clauses must also provide notice to affected employees—current and former—that those provisions are no longer effective and cannot be enforced. Notice must be provided within 45 days of rescission in an “individualized communication.”

A key exception under the proposed rule is in the context of the sale of a business. Specifically, the proposed rule does not apply to a non-compete that is “entered into by a person who is selling a business entity or otherwise disposing of all of the person’s ownership interest in the business entity.”

The proposed rule would expressly supersede any state law that is less protective of workers but would allow states to impose rules that afford workers greater protection at their discretion.

Of course, this proposed rule would have sweeping impacts across all industries if enacted. Employers should consider what those impacts might look like for their unique business and work to ensure they are prepared to respond quickly to any final rule. Initial steps could include identifying any current and former employees subject to an existing non-compete, considering how to handle any rescission that may be necessary, ensuring that company trade secrets are protected beyond simply relying on non-compete provisions, and preparing to adjust existing agreements and policies as necessary.

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