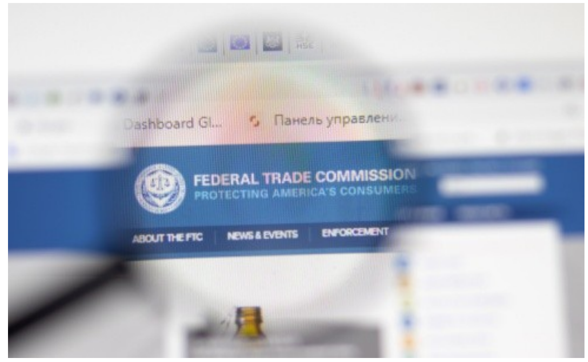
Navigating the FTC's New Non-Compete Rule: Steps to Prepare by September 4, 2024



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By Sarah Goodman

On April 23, 2024, the Federal Trade Commission (FTC) approved a new rule (FTC Rule) that invalidates most existing non-compete agreements for employees at for-profit businesses, except for those agreements for "senior executives" signed before September 4, 2024 (Effective Date). This FTC Rule fundamentally alters the longstanding practice of using non-compete clauses to safeguard an employer's interests.

Overview of the FTC's New Non-Compete Rule and Its Implications

Under the new rule, non-compete agreements will only remain enforceable for senior executives—defined as those earning more than $151,164 annually and holding significant policy-making roles, such as president or CEO—and will remain enforceable if signed before the Effective Date. After September 4, 2024, employers will be prohibited from imposing non-compete agreements on new hires, even if they are senior executives. Employers are also required to inform both current and former employees bound by non-compete agreements that these agreements will not be enforced. The FTC has provided model language for this notice, available on its website in multiple languages. Employers should use this notice carefully and avoid issuing it to senior executives who the FTC Rule does not impact.

Key points to consider:

- The term "worker" is broadly defined and includes employees, independent contractors, interns, volunteers, apprentices, and even sole proprietors.
- The FTC's jurisdiction generally does not cover non-profit organizations, banks, savings and loan institutions, federal credit unions, common carriers, and air carriers, so the rule may not apply to these sectors.
- The rule does not address non-compete agreements that prevent employees from soliciting customers or other employees unless these agreements are overly broad and interfere with a worker's ability to seek or accept new employment.
- Agreements designed to protect trade secrets and confidential information, such as non-disclosure agreements, remain enforceable.
- The FTC Rule does not apply to non-compete agreements related to the bona fide sale of a business entity and does not affect any pending enforcement actions pertaining to non-competes established before the Effective Date.
- The rule applies to post-employment non-compete agreements and does not impact agreements that limit competitive activities during employment.
- The FTC Rule overrides conflicting state laws but does not supersede state laws that provide greater protections, such as California's comprehensive ban on non-competes for all employees, including senior executives.

Current Legal Challenges to the FTC Rule

It is no surprise that several federal lawsuits have been filed to challenge the enforcement of the FTC Rule. In one case, *ATS Tree Services, LLC v. FTC*, the U.S. District Court for the Eastern District of Pennsylvania ruled that the plaintiffs were unlikely to succeed in their claims against the FTC and denied their request for a preliminary injunction to halt the rule's enforcement. Consequently, it is reasonable to anticipate that the *ATS* court may ultimately support the FTC's position.

In contrast, in *Ryan LLC v. Federal Trade Commission*, the U.S. District Court for the Northern District of Texas issued a limited preliminary injunction preventing the enforcement of the FTC Rule against the plaintiffs and intervenors involved in that case. The *Ryan* court is expected to decide by August 30, 2024, whether to grant a nationwide permanent injunction, just before the FTC Rule is set to take effect.

Additionally, on June 21, 2024, *Properties of the Villages, Inc. v. Federal Trade Commission* was filed in the Middle District of Florida before Judge Timothy J. Corrigan. The plaintiff is seeking a preliminary injunction against the FTC Rule as it applies to them and an order to vacate it entirely under the Administrative Procedure Act. Judge Corrigan is scheduled to hear arguments on the motion for a preliminary injunction on August 14, 2024.

Recommended Action for Businesses Before the FTC Rule Takes Effect

Businesses should be prepared to act by the Effective Date. Despite ongoing litigation challenging the FTC Rule, no nationwide injunction has been issued, so employers should proactively:

1. Strengthen other restrictive covenants (*e.g.*, non-solicitation clauses) and develop strategies to address potential risks associated with the rule.
2. Consider how the rule might impact valuations in mergers or acquisitions due to the potential for increased competition. (Note that the FTC Rule does not apply to non-compete clauses related to the bona fide sale of a business, a person's ownership interest in a business, or substantially all of a business's operating assets.)
3. Evaluate options for updating or introducing agreements for senior executives before the Effective Date.
4. Review and analyze the impact of the FTC Rule on existing non-compete agreements.
5. Plan for issuing the required notices to affected employees and former employees.

Offit Kurman has a dedicated practice group focused on issues related to employee mobility, including restrictive covenants and trade secrets. Our attorneys are uniquely positioned to guide you through these challenges, helping you weigh the risks specific to your business and make informed decisions that align with your business objectives.

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