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NEW FTC RULE CREATES UNCERTAINTY ABOUT NON-COMPETE AGREEMENTS

By Dan Hall and Samantha Buckman

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On April 23, 2024, the Federal Trade Commission announced a final rule that, if upheld, will ban noncompetition clauses nationwide. The rule, which is scheduled to become effective 120 days after its publication in the Federal Register, would prevent the enforcement of existing noncompetition clauses – with limited exceptions – while prohibiting new noncompetition clauses in the future. The FTC rule, if it goes into effect, will be more expansive than Minnesota's existing state ban on non-compete agreements, which took effect on July 1, 2023. *See* Minn. Stat. § 181.988. Unlike the Minnesota state law prohibition, which applies only prospectively, the FTC rule is retroactive and invalidates existing non-compete agreements. Both the FTC rule and Minnesota law include certain exceptions, such as for agreements entered pursuant to the sale of or in anticipation of the dissolution of a business. *See id.* at subd. 2(b)(1-2).

Within hours after the FTC's announcement, business groups challenged the rule and sought injunctions in federal court. One such challenge comes from the U.S. Chamber of Commerce, alongside other business-group plaintiffs, who filed suit in the U.S. District Court for the Eastern District of Texas. The 52-page Complaint condemns the FTC's rule as an impermissible overreach of the Commission's authority and simultaneously emphasizes the longstanding practice of states establishing their own noncompetition laws. *See Complaint, Chamber of Commerce v. FTC,* No. 6:24-cv-00148, ¶¶ 41–44 (E.D. Tex. Apr. 24, 2024). The Complaint puts forth a complementary assertion that "[n]oncompetes have never been regulated at the federal level." *Id.* at ¶ 5.

Although the FTC is breaking new federal ground with its comprehensive condemnation of noncompetition clauses, outright limitations and rules that limit the enforceability of non-compete agreements have existed at the state level since the late 1800s. Minnesota is one of four states – along with California, Oklahoma and North Dakota – that have effectively banned noncompetition clauses for most employees. Many other states limit the circumstances in which noncompetition provisions are permissible or enforceable. Other federal entities and organizations have also expressed skepticism about whether noncompetition provisions are not just harmful, but whether they are permissible under various acts.

The landscape of noncompetition law faced numerous changes and challenges in 2023, reaching far beyond the FTC's initial proposal of its noncompetition rule in early 2023. California, one of the few states with a history of forbidding noncompetition provisions, amended its existing ban with even more stringent prohibitions in late 2023. See California Business and Professional Code §§ 16600 - 16607. The National Labor Relations Board General Counsel issued a memorandum in May 2023, adopting the viewpoint that noncompetition provisions, with limited exceptions, violate the National Labor Relations Act. Significantly, Minnesota became the first state in more than a century to effectively prohibit noncompetition agreements.

If the FTC rule is enforceable, it will not deny employers all possible protections, just as Minnesota's existing prohibition on non-competes explicitly exempts non-disclosure agreements, confidentiality agreements, and non-solicitation agreements. Minn. Stat. § 181.988, subd. 1(a)(3). The FTC's rule similarly allows for non-disclosure and non-solicitation agreements, so long as they are not functionally equivalent to a non-competition clause as defined in § 910.1(1) of the rule. The FTC's press release relating to the rule's issuance even suggests non-disclosure agreements as a valid alternative to non-competition clauses. Non-solicitation and non-disclosure agreements protect against some of the same concerns that employers attempt to address with the use of noncompetition provisions and will continue to provide an important avenue of recourse for employers who have been harmed by the actions of former employees. Causes of action such as breach of the duty of loyalty and associated business torts also remain available to Minnesota employers.

While the FTC rule may be among the most comprehensive and publicly visible attempts to roll back the enforceability of noncompete agreements, it is also a lodestar as to the current trends and attitudes towards such agreements generally. Clarity is still lacking in this area of law, both federally and in states whose laws are still changing and being tested in court, and the challenges related to the FTC rule are likely far from over. Employers that want to be proactive should address non-solicitation agreements and confidentiality agreements, which are likely to be enforceable even if the FTC rule is upheld.

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