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FTC Issues Rule Banning Most Existing Non-Competes

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On April 23, 2024, the Federal Trade Commission (FTC) issued the Non-Compete Clause Rule which bans most existing non-competition agreements and comprehensively bans employers from entering into new non-competition agreements. The FTC's rationale for issuing the broad prohibition is that non-competition agreements are "unfair methods of competition." The Rule is scheduled to go into effect on September 4, 2024, but legal challenges to the validity of the Rule have already been filed.

When (or if) the Rule becomes effective, all existing non-competition agreements will be unenforceable except for: (1) non-competition agreements with "senior executives"; and (2) non-competition agreements entered into pursuant to a bona fide sale of a business entity or ownership interest in a business entity. "Senior executives" are defined as an employee who: (1) was in a policy-making position; and (2) received total annual compensation of at least \$151,164. A policy-making position includes an entity's president, chief executive officer, other officers with policy-making authority, or other employees who have policy-making authority for the business. "Policy-making authority" is defined as "final authority to make policy decisions that control significant aspects of a business entity or common enterprise." Employees that solely serve in advisory positions are not in "policy-making positions."

On or before the effective date, employers are required to issue notices to employees who are parties to an "unenforceable non-competition agreement" stating that the employer will not, and cannot, legally enforce the non-competition agreement against the employee.

The Rule is currently being challenged by various parties in the United States District Court for the Northern District of Texas. The challengers include: a tax and software services provider, the Texas Association of Business, and the U.S. Chamber of Commerce. SHRM filed a brief in the lawsuit expressing its support for delaying the Rule while the litigation is pending, arguing that employers and human resource professionals should not be placed in the position of making recruiting, hiring, and other employment related decisions while the legality of the Rule is uncertain. The Court indicated that it will issue a decision regarding whether the Rule should go into effect as planned by July 4, 2024.

At this point, employers should identify all non-competition agreements that would be "unenforceable" under the Rule and stay tuned for a federal court decision in the next several weeks.

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