Employment Law Alert: The FTC's New Proposed Rule on Non-Competes

What Employers Need to Know

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On January 5, 2023, the Federal Trade Commission ("FTC") proposed a new rule that would ban the use of non-competes in most employment and contractor contexts (the "Proposed Rule").

In recent years, several states, including Massachusetts, have sought to limit the enforceability of employment-related non-competes. However, the national ban contemplated by the Proposed Rule is sweeping in its scope, is more restrictive than such state laws which seek to constrain employment-related non-competes, and, if formalized, will materially change the way employers contractually engage with their workers.

The key aspects of the Proposed Rule are summarized below:

Key Non-Compete Provisions

The Proposed Rule has two primary components:

1. ***GENERAL BAN***: A general prohibition on employers (a) entering into new non-compete clauses with workers; and (b) maintaining existing non-compete clauses with workers (the "General Ban"); and
2. ***RESCISSION***: A requirement that employers affirmatively rescind all existing non-compete clauses (the "Rescission Mandate").

The General Ban would apply to both actual and "*de facto*" non-compete covenants – *i.e.*, all contractual provisions that have "*the effect of prohibiting 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.*" As such, except in limited circumstances, broadly drafted non-disclosure and non-solicitation covenants would be within the general prohibitions contained in the Proposed Rule. In addition, the General Ban would apply both prospectively and retroactively – banning new and existing non-compete clauses, and would apply to non-competes with employees and any other type of worker – banning non-compete clauses for non-employees, including independent contractors, externs, interns, volunteers, apprentices, or sole proprietors.

The Rescission Mandate would require employers to affirmatively rescind existing non-compete clauses unless a narrow exception (as discussed below) applies. This Rescission Mandate anticipates individualized communications from the employer to all current *and former* employees subject to existing non-compete clauses.

There is a *limited exception* in the Proposed Rule for non-compete agreements entered into in a sale-of-business context. Under the Proposed Rule, non-compete agreements may still be used to prevent owners who are selling their businesses from competing with the purchasers of their businesses. However, this exception is extremely narrow in scope – available only where the restricted party is an owner, member or partner holding at least a 25% ownership interest in the

business entity.

When Would the Proposed Rule Go into Effect?

The Proposed Rule is just that – a draft regulation that has been proposed by the FTC for public comment. The Proposed Rule is not effective law, and must still proceed through a formal "rulemaking" process before its prohibitions would apply to employers.

The public comment period for the Proposed Rule is open for the next 60 days. After the comment period closes, the FTC may then move to amend/or finalize the Proposed Rule into effective law.

It is unclear how long the FTC will take to finalize the Proposed Rule (if it does in fact finalize the rule). However, given standard rulemaking procedures, if the FTC moves to finalize the Proposed Rule, an effective date for the Proposed Rule is not anticipated before the end of 2023. In addition, inevitable legal challenges stand to further delay or completely derail implementation of the Proposed Rule.

What Does This Mean for Employers?

Whether the Proposed Rule ever becomes effective law is certainly an open question. However, the fact that a national ban on non-competes has been proposed by the Federal Government (coupled with recent state law challenges to such covenants) demands that employers assess their use and enforcement of non-compete agreements on a going-forward basis.

The Morse Employment Law Team is following the Proposed Rule closely, and will continue to report on this important legal development.

Please contact Matthew Mitchell or Rebecca Alperin should you have questions concerning this subject.