

May 2024

Business Signals – Client Alert

*An alert about the legal implications of issues affecting businesses
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THE FTC’S NEW RULE: NON-COMPETITION AGREEMENTS NO LONGER ENFORCEABLE

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On April 23, 2024, the Federal Trade Commission (“FTC”) issued a final rule that will significantly alter the legal landscape for businesses across the country. Specifically, the FTC has now issued final regulations promulgating a rule that effectively bans non-competition agreements for all employers nationwide. It did so by declaring that non-competition agreements were “unfair methods of competition” under Section 5 of the FTC Act. The agency justifies this new rule by relying on many different policy considerations, such as the protection of the fundamental freedom of workers to change jobs and the increase of innovation for American businesses. But regardless of their reasons, the FTC has taken what was once a purely state law issue, with many variations across the country, and made it into a nationwide policy.

Upon the new rule’s effective date, existing non-compete agreements for the vast majority of workers will no longer be enforceable, nationwide. There are limited exceptions to this new rule, including the following:

- Pre-existing noncompetes for workers qualifying as senior executives (although new non-competes will be prohibited). Senior executives are defined as workers earning more than \$151,164 in the preceding tax year who are considered working in a policy-making position.
- Non-competition agreements entered into as part of the bona fide sale of a business, but only for seller/workers who owned at least some portion of the entity being purchased. The original proposed rule would have limited this exception to those seller/workers owning at least 25% of the business entity, but the final rule has expanded this exception to any seller/worker owning a portion of the business.
- Non-competition agreements between franchisors and franchisees will still be valid and enforceable.

- The final rule clarified that non-profit entities and other specifically listed types of companies that are not subject to the FTC Act will not be subject to the new rule.

The new rule is set to go into effect on September 4, 2024. All businesses are required to notify their employees that their non-competition agreements are no longer enforceable.

This new rule is a substantial change in the law for large and small businesses alike. Non-competes are one of the more standard provisions contained in employment and independent contractor agreements across the country, for good reason, since they are critical to many businesses to protect themselves from losing business, customers, and confidential information to former employees. With the FTC taking such provisions completely out of consideration, business owners will need to consider how they will protect themselves, their businesses, and their confidential information from former employees (and from their competitors!)

Although this new rule is a drastic deviation from a longstanding practice for many businesses, the FTC has left certain options available to circumvent some of the new restrictions. For example, as noted above, senior executives with existing non-compete agreements are treated differently than other workers, and their non-compete agreements will still be enforceable. Furthermore, other types of protective agreements, like non-solicitation agreements and trade secret protections, are still available under the Act, although such provisions can violate the new regulations if they are found to be overbroad or overly restrictive.

The FTC's action has already been challenged in court by a variety of litigants, including the U.S. Chamber of Commerce, so it is possible that the regulations will be overturned. Regardless, this is a substantial change in the law, and owners of small, medium, and large businesses would be well advised to contact their business attorney in order to see how this rule affects their current employment relationships and agreements.

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