CLIENT ALERT

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Schneider Smeltz Spieth Bell LLP

FTC NON-COMPETE

A LASTING IMPACT ON EMPLOYMENT CONTRACTS

The Federal Trade Commission (FTC) proposed a rule in January 2023 that could have a lasting impact on employment contracts. As proposed, the rule would render noncompete clauses invalid and unenforceable, with only a limited exception for non-competes in connection with the sale of a business. The proposed rule would apply nationally, superseding contradictory state laws. This would require employers to find new ways to maintain their competitive advantage, without relying on noncompete clauses to protect themselves from former employees competing in the same industry. With about 30 million workers in the United States currently bound by non-compete agreements, this proposed rule is one to keep eyes on.

The proposed rule defines non-competes broadly and sets out a test to determine whether a contract term falls under the umbrella of a "non-compete." The test examines whether a contract term prohibits a worker from continuing to work after the end of their employment with an employer. It is worth noting that this test is not limited to the employer-employee relationship. Clauses that restrict independent contractors, externs, interns, volunteers, apprentices, and sole proprietors from working after the end of their engagement with a company are also "non-competes" and would be unenforceable under the proposed rule.

This rule proposal sparked a lot of debate, with over 26,000 comments submitted to the FTC. On one hand, non-compete agreements are associated with lower wages, fewer job offers, and decreased

mobility for workers. On the other hand, 67% of employers use non-compete clauses to protect proprietary information and trade secrets, while 55% use them to prevent employees from working for competitors. The comment period closed in April and the FTC is currently reviewing the comments before issuing a final rule.

It is unknown when the final rule will be issued, but it is anticipated that the final rule will closely resemble the proposed rule. If so, worker contracts will be significantly impacted moving forward. Therefore, it is not advisable for employers to wait for the final rule to be issued before making changes to their employment contracts.

Companies should explore alternative ways to maintain their market position and safeguard their competitive edge without the use of noncompete clauses. One option is to focus on protecting trade secrets. Although the proposed rule invalidates noncompete clauses, it does not allow departing employees to take trade secrets and proprietary information with them. Companies should assess which employees have access to such information and take measures to secure their intellectual property from misappropriation.

Educating management on the importance of protecting trade secrets and examining policies that may compromise the security of such information is a proactive approach that employers can take. In this way, companies can minimize risk and protect their valuable intellectual property, which is critical to their competitiveness and success.

If you have any questions about the proposed rule or need assistance protecting your intellectual property, please contact the attorneys at Schneider Smeltz Spieth Bell.

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