Legal Update Article

Takeaways from President Biden's Executive Order on Non-Competes

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Restrictive Covenants, Trade Secrets and Unfair Competition

In the latest step toward federal regulation of non-compete agreements, President Joe Biden has issued a wide-ranging Executive Order that, among many other competition-focused objectives, encourages the Federal Trade Commission (FTC) to "curtail the unfair use of non-compete clauses and other clauses or agreements that may unfairly limit worker mobility."

Past Efforts

Federal regulation of non-compete agreements has been discussed for years. In March 2016, the U.S. Treasury Department issued a report, "Non-Compete Contracts: Economic Effects and Policy Implications," based mostly on non-public studies, asserting pervasive misuse of non-competition agreements.

In October 2016, President Barack Obama issued a "State Call to Action on Non-Compete Agreements" to "address wage collusion, unnecessary non-compete agreements, and other anticompetitive practices."

In Congress, multiple bipartisan bills aiming to ban non-competes have fallen by the wayside. Further, the FTC hosted a workshop in January 2020 "to examine whether there is a sufficient legal basis and empirical economic support" to restrict non-competes.

Federal Ban on Non-Compete Agreements?

The Executive Order does not change the law of restrictive covenants. It merely "encouraged" the FTC to act. Much remains to be done before any ban or limitations on restrictive covenant agreements by the FTC become reality.

Key Provisions

Although the White House Fact Sheet and most media reports characterize the Executive Order as affecting only "non-compete agreements," the actual text of the Executive Order goes further. It applies to non-compete provisions "and *other clauses or agreements that may unfairly limit worker mobility."* This language arguably may include other restrictive covenants that are currently enforceable in most jurisdictions, such as customer and employee non-solicitation provisions, no-hire provisions, and non-servicing provisions.

After the release of the Obama Administration's "State Call to Action on Non-Compete Agreements," more than 20 states (plus the District of Columbia) have enacted some change to law governing non-compete provisions. But only a few (such as Illinois and Nevada) regulate other restrictive covenants, such as customer non-solicitation or non-servicing provisions, in the same statutory framework as non-competes. Some states (like Massachusetts) expressly exclude such provisions from their non-compete regulation. It is unclear whether, and to what extent, the FTC will interpret the Executive Order as a call to regulate restrictive covenants beyond non-competes.

Moreover, the Executive Order encourages regulating "the *unfair* use" of non-compete clauses and other restrictive covenants. This language might suggest that not *all* use of such agreements is "unfair," in Biden's view. Indeed, most jurisdictions have enforced reasonable non-competes for centuries. Only three states in the country generally prohibit non-competes (California, North Dakota, and Oklahoma), and the non-compete prohibitions in these states have been in place since the 1800s. Tellingly, the jurisdictions that recently curtailed non-competes through legislation did not ban them outright (but the District of Columbia came close).

Against this backdrop, Biden's choice of the phrase "unfair use" suggests he is asking the FTC to act against the abuses of restrictive covenants and not their reasonable use.

FTC's Role

The FTC conducted a thorough examination of non-competes in January 2020 and, so far, nothing has come of it. Significantly, the FTC examined not only "why" it should consider regulating non-competes (a question hotly debated with ample evidence on both sides, despite the White House's citation only to pro-regulation evidence), but also "how" the FTC could potentially act.

Several panelists at the FTC workshop questioned whether the FTC could regulate this area of law through rulemaking, even if it were inclined to do so. Many alternatives to FTC rulemaking were discussed that day, including litigation, publishing a general statement of policy or guidelines, and action by Congress or another federal agency.

However, the Executive Order specifically encourages the FTC to "exercise the FTC's statutory rulemaking authority under the Federal Trade Commission Act" to regulate restrictive covenants. This process may require several steps, including publishing a detailed and specific notice of any proposed rulemaking, the draft text of the rule, and the reason for the proposed rule. Rulemaking potentially could be a years-long process.

Questions Abound

The Executive Order raises many questions, even though it does not cause any immediate changes to the law.

If the FTC engages in rulemaking, it is unclear what level of regulation it may pursue. Will the FTC seek to ban non-competes entirely? Will it take a more nuanced approach, imposing non-competition restrictions only for low-wage workers, as a number of states have done? Will the FTC also try to regulate other restrictive covenants, such as non-solicitation and non-servicing provisions? And, if the FTC exercises its rulemaking authority to regulate restrictive covenants, will anyone challenge its legal authority to do so and what will the courts say? All these questions, and many more, remain unanswered.

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For now, if they are not already doing so, employers should start thinking about how to protect their business interests if the FTC were to ban or limit some or all non-competition agreements or other restrictive covenants. Using restrictive covenants is just one of several business protection strategies. Companies should discuss alternative strategies, policies, and best practices with their counsel. Jackson Lewis attorneys in the Restrictive Covenants, Trade Secrets and Unfair Competition practice group are available to advise on these issues.

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