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Federal Court Vacates FTC's Non-Compete Rule

By Jordan B. Schwartz

As readers of this blog know, this past Spring, the Federal Trade Commission (FTC) issued its final Non-Compete Clause Rule (the "Non-Compete Rule") in late April 2024, purporting to ban nearly all employment-related non-compete agreements. Under the Non-Compete Rule, which was scheduled to take effect on September 4, 2024, an employer generally would have been prohibited from entering or attempting to enter into a non-compete with a worker, maintaining a non-compete with a worker, or representing to a worker that the worker was subject to a non-compete. The Non-Compete Rule also would have required employers to cease enforcement of existing non-competes (aside from agreements with Senior Executives, as defined by the Rule) and actively inform workers that existing non-compete clauses would no longer be enforced.

The FTC's announcement of the Non-Compete Rule sparked immediate legal challenges. As a result, since that time, those of us in the employment law legal community have been waiting on pins and needles for a decision regarding the validity of the Rule, so that we could effectively guide and counsel our clients accordingly. Finally, that time has now arrived.

On Tuesday, August 20, 2024, Judge Ada E. Brown of the U.S. District Court for the Northern District of Texas, granted summary judgment for Ryan LLC and, in so doing, vacated the Non-Compete Rule. The plaintiff in this case, a tax services firm called Ryan LLC (along with the U.S Chamber and Commerce and other intervenor plaintiffs who joined Ryan), had challenged the FTC's authority to issue the Non-Compete Rule banning the use of non-compete agreements across the country and sought summary judgment against the FTC.

In granting Ryan's motion for summary judgment, Judge Brown held, in no uncertain terms, that "the Rule shall not be enforced or otherwise take effect on its effective date of September 4, 2024 or thereafter." Importantly, Judge Brown's decision nullifies the Non-Compete Rule nationwide, not just for the plaintiffs in the lawsuit, as was the case when she granted the plaintiffs' motion for a preliminary injunction in early July.

In her decision, Judge Brown found, among other things, that the FTC's promulgation of the Non-Compete Rule was in excess of its statutory authority and was an arbitrary and capricious "categorical ban" that violated the Administrative Procedure Act. In reaching that conclusion, Judge Brown rejected the FTC's arguments that amendments to the FTC Act in recent years allowed it to create such a substantive rule, calling the FTC's arguments "a piecemeal attempt to confer rulemaking authority that Congress has not affirmatively granted to the FTC."

Notably, while Judge Brown acknowledged that Congress vested the FTC with the power to prevent unfair methods of competition, she concluded that the plain reading of Section 6(g) of the FTC Act did not provide the FTC with any authority to create "substantive rules regarding unfair methods of competition." Accordingly, this decision does not simply vacate the Non-Compete Rule on a narrow basis. Rather, it curtails the FTC's overall attempt to expand its rulemaking authority beyond its traditional consumer protection regulations and into a new category that it had deemed "unfair methods of competition," which is welcome news for employers who want to continue to keep using – and enforcing – non-compete agreements.

The U.S. Chamber of Commerce praised the court's decision, stating that it is a "significant win in the Chamber's fight against government micromanagement of business decisions," and that the Non-Compete Rule was an "unlawful extension of power that would have put American workers, businesses and our economy at a competitive disadvantage."

On the other side of the coin, a spokeswoman for the FTC stated that the agency was disappointed by the decision and would "keep fighting to stop non-competes that restrict the economic liberty or hardworking Americans, hamper economic growth, limit innovation and depress wages." She further stated that the FTC is "seriously considering a potential appeal" and that the "decision does not prevent the FTC from addressing non-competes through case-by-case enforcement actions."

It is worth nothing, however, that even if the FTC does appeal, it is unlikely that such an appeal would be successful, either in the conservative leaning Fifth Circuit, or at the U.S. Supreme Court, especially given the current make-up of the Court. As a result, the Non-Compete Rule will not take effect, at least for the foreseeable future.

Thus, for employers who were scrambling to comply with the requirements of the Non-Compete Rule and, in particular, its notice requirements, those efforts should cease immediately. In other words, employers **should not** notify workers that existing non-compete clauses will no longer be enforced, as would have been required under the Non-Compete Rule. Employers also **should not** modify existing non-competes in an effort to comply in any way with the now invalidated Non-Compete Rule.

That being said, there is still a nationwide trend against the use of non-competes. Indeed, in recent years, more and more states have either invalidated or at least curtailed non-compete agreements. Thus, it is imperative that company representatives know – and follow – the relevant and applicable state laws and monitor any new legal developments that could impact the validity of your company's non-compete agreements or other restrictive covenants.

We will continue to monitor and keep you apprised of all developments relating to this important issue.