Hogan Lovells

Key takeaways from the FTC's noncompete workshop

17 January 2020

On 9 January 2020 the Federal Trade Commission (FTC) held a public workshop in Washington, D.C. to assess whether it should "promulgate a Commission Rule that would restrict the use of non-compete clauses in employer-employee employment contracts."[1] Noncompete clauses are provisions in employee contracts restricting them from working for a competing employer for some period of time after their employment ends.[2]

The workshop focused on the growing use of noncompete agreements by employers across industries, whether the use of these agreements is anti-competitive, and what authority the FTC has to regulate the use of these agreements in the labor markets.

The FTC is now seeking further public comments, due on 10 February 2020. Below we discuss the key takeaways.

The panel agreed that there is no justification for noncompetes restricting low-wage and low-skill workers

The panelists were largely in agreement that there is no legal or business justification for the use of noncompete agreements for low-wage and low-skill workers (such as fast food franchise employees). Citing evidence that such agreements result in depressed wages, diminished labor mobility, and disproportionally affect workers who lack bargaining power in employment negotiations, there was broad support for the FTC to – at a minimum – regulate or ban the use of noncompete agreements as they apply to low-wage workers.

The effect of noncompetes on other workers is less clear

In contrast to the effects on low-skill and low-wage workers, studies show that noncompete agreements may benefit other types of employees, such as CEOs[3] and physicians.[4] The panelists

[1] Federal Trade Commission press release, FTC to Hold Workshop on Non-Compete Clauses Used in Employment Contracts (5 December 2019) available at https://www.ftc.gov/news-events/press-releases/2019/12/ftc-hold-workshop-non-compete-clauses-used-employment-contracts.

[2] Non-compete clauses are distinct from "no-poach" agreements, in which competing employers agree not to hire each other's workers. No-poach agreements, wage-fixing agreements, labor market definition, and labor monopsony in merger enforcement were the subject of a companion workshop hosted by DOJ in September 2019. Public Workshop on Competition in Labor Markets (23 September 2019) available at https://www.justice.gov/atr/public-workshop-competition-labor-markets.

[3] CEOs often enter employment negotiations with significant bargaining power, and can negotiate an increased salary in exchange for agreeing to the noncompete provision. From the employer's perspective, the noncompete provision allows the employer to demand better CEO performance because terminating the CEO does not risk the potential economic harm that could result from a terminated CEO immediately joining a competitor.

agreed that more research needs to be conducted to assess the effects of the widespread use of noncompete agreements by companies across various sectors.

Noncompetes are prevalent even in states where they are unenforceable

The rate of use of noncompete agreements in states where they are unenforceable (such as California) is similar to the rate of use in states where they are legal. The panelists were unable to fully explain this phenomenon, but stated that it could be partly due to the fact that many workers – especially low-wage workers – are unfamiliar with relevant state laws governing their employment agreements and are unable to hire counsel to advise them of their rights.

The FTC's authority to address noncompetes through rule-making is unclear

FTC Commissioner Rebecca Slaughter stated her strong support for the FTC to undertake a rule-making endeavor to provide a national standard for regulating the use of noncompete agreements. Other speakers debated the FTC's rule-making authority in this area. FTC Commissioner Noah Phillips in particular expressed concern that an FTC rule regulating unfair methods of competition may implicate a fundamental question of constitutional separation of powers regarding Congress' ability to delegate legislative powers to administrative agencies.[5]

Alternatives to a ban on noncompetes may be appropriate

Potential alternatives to a national standard banning employee noncompetes were also discussed. One possibility is limiting the use of noncompete agreements – such as requiring employers to issue written notice, providing employees with the right to consult counsel, limiting the geographic scope of an agreement, and imposing a maximum duration that an agreement is enforceable. Another alternative is to have the FTC issue a policy statement regarding the use of employee noncompetes, thereby avoiding the procedural hurdles inherent in the rule-making process.

Next steps

Most of the panelists appeared to believe that a per se ban on noncompete agreements would be difficult for the FTC to justify. The economists on the panel were mostly in agreement that more research is necessary to determine whether the potential anti-competitive effects of noncompete agreements (e.g., stagnating wages, lack of mobility in the labor market, and limiting employees' bargaining power) outweigh any potential benefits (e.g., incentivizing employers to invest in training, protecting trade secrets, and preserving the freedom to contract). It was also suggested that the FTC analyze the disparate effects on workers and employers that result from the variations of noncompete laws across states.

The FTC is now seeking public comment on a number of questions, including:

- What additional economic research should be undertaken to evaluate the net effect of noncompete agreements? Should additional economic research on the empirical effects of noncompete agreements focus on a subset of the employee population? If so, which subset?
- What impact do noncompete clauses have on labor market participants?
- What are the business justifications for noncompete clauses?

---

[4] Studies show that noncompete agreements allow a medical practice to protect its patient relationships, one of its most valuable assets. If a doctor leaves a practice where a noncompete agreement is in place, she is more likely to refer her patients within the practice, resulting in increased earnings for the remaining physicians in the practice.

[5] Federal Trade Commission, Prepared Remarks of Commissioner Noah Joshua Phillips (9 January 2020) available at https://www.ftc.gov/system/files/documents/public_statements/1561697/phillips_-_remarks_at_ftc_nca_workshop_1-9-20.pdf.

- Do employers enforce employee noncompete agreements? How routine is such enforcement?
- Are there situations in which noncompete clauses constitute an unfair method of competition (UMC) or an unfair or deceptive act or practice (UDAP)? How prevalent are these situations?
- Should the FTC consider rule-making to address the potential harms of noncompete clauses, applying either UMC or UDAP principles?
  - What should be the scope and terms of such a rule?
  - Is state law insufficient for addressing harms associated with noncompete clauses? Is federal law insufficient?
  - What is the statutory authority for the commission to promulgate such a rule?
- Should the FTC consider using other tools besides rule-making to address the potential harms of noncompete clauses, such as law enforcement, advocacy, or consumer/industry guidance? [6]

The deadline for submitting public comments is 10 February 2020.

[6] FTC, Non-Competes in the Workplace: Examining Antitrust and Consumer Protection Issues (9 January 2020) available at https://www.ftc.gov/news-events/events-calendar/non-competes-workplace-examining-antitrust-consumer-protection-issues.

Contacts

Chuck Loughlin
Partner, Washington, D.C.
T +1 202 637 5661
chuck.loughlin@hoganlovells.com