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FTC bans noncompete clauses and the legal battle begins. What does it mean?

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Earlier this week, the U.S. Federal Trade Commission (FTC) **voted to ban** for-profit U.S. employers from including noncompete clauses in employment contracts, a move that could affect tens of millions of U.S. workers. The rule bans new noncompete clauses for all workers and makes existing noncompete agreements unenforceable except for those covering senior executives—those workers earning more than \$151,164 annually who are in "policy-making positions" and represent fewer than 1% of workers.

The FTC's decision was the result of a 3-to-2 vote among its five commissioners. The two dissenting commissioners said they believe the rule won't survive legal challenges. Indeed, the U.S. Chamber of Commerce sued the FTC on April 24 for what it views as an overreach by the commission. Meanwhile, other business groups have spoken out against the ruling, saying noncompete clauses are necessary to protect a company's intellectual property.

Why it matters

The controversial ruling has far-reaching implications for U.S. businesses and the estimated 30 million employees impacted. The FTC estimates the new rule will lead to new business formation growing by 2.7% per year, resulting in more than 8,500 new businesses each year.

In addition, the FTC says the rule is expected to:

- increase earnings for the average U.S. worker by an additional \$524 per year
- lower health care costs by up to \$194 billion over the next decade
- lead to an additional 17,000 to 29,000 more patents each year over the next decade

Meanwhile, the ban would apply nationwide, creating a federal regulation and overriding state laws regarding noncompete agreements. Currently Washington, D.C. and three states—California, North Dakota and Oklahoma—have all but banned noncompete agreements, while others—Colorado, Maryland, Oregon and Rhode Island—allow them but with restrictions.

What they say

President Biden says:

“The FTC is cracking down on ‘non-compete agreements,’ contracts that employers use to prevent their workers from changing jobs, even if that job will pay a few dollars more, or provide better working conditions. Workers ought to have the right to choose who they want to work for.”

Lina M. Khan, FTC chair, says:

“Noncompete clauses keep wages low, suppress new ideas, and rob the American economy of dynamism, including from new startups that will be created once noncompete clauses are banned. The FTC’s final rule to ban noncompetes will ensure Americans have the freedom to pursue a new job, start a new business, or bring a new idea to market.”

Suzanne P. Clark, U.S. Chamber of Commerce president & CEO, says:

“The Federal Trade Commission’s decision ... is not only unlawful but also a blatant power grab that will undermine American businesses’ ability to remain competitive. The FTC has never been granted the constitutional and statutory authority to write its own competition rules. This decision sets a dangerous precedent.”

What we say

“This new ruling by the FTC turns up the volume on some of the already pressing issues with organizations around retention, succession planning, learning and development, and knowledge sharing. It continues to shift the traditional power dynamic from employers to employees—a shift that has been highlighted over the past several years given the high demand and low supply of talent in the marketplace. Meanwhile, organizations will most likely see an elevated risk of intellectual property loss and increased labor costs. Ultimately, if this rule becomes reality, organizations will need to refocus their efforts to engage, train and retain their top talent.”

The bottom line

This situation is fluid, and the ruling is already being challenged. While we can’t know how long the issue will be argued in the courts, it’s likely that lawsuits will delay final decision on the new rule well past the planned August 2024 effective date. The current U.S. presidential election also could impact the ultimate court decision. If the rule ultimately does go into effect, the shift of power back to the individual employee will put added pressure on organizations to focus on employee experience, leadership development and management effectiveness, as talent retention will be key to success.

Protiviti Director Johnny Martinez contributed to this review.

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