

No More Non-Competes?

FEBRUARY 9, 2023

Direct sellers should take note of recent Federal Trade Commission enforcement actions and a proposed FTC rule which could fundamentally change the legal landscape for non-compete clauses. Under the FTC's new approach, companies would not be permitted to enforce non-compete clauses against their workers. And yes, that includes independent contractors.

The FTC in a press release last month announced that it reached consent agreements with three companies—a security company and two glass-container manufacturers—barring them from enforcing non-compete clauses in employment contracts.^[1] The next day, the FTC further announced that it is proposing a new rule which would consider most non-compete clauses to be “[u]nfair methods of competition” in violation of Section 5 of the FTC Act.^[2] The consent agreements and proposed rule are not yet final, and the FTC has posted notice soliciting public comment on each.^[3]

As noted by a dissenting statement by Commissioner Christine S. Wilson, the consent agreements depart from the analysis courts use to determine whether a non-compete clause can be enforced: “Courts have long analyzed the temporal length, subject matter, and geographic scope of non-compete agreements to determine whether those agreements are unreasonable; when non-compete agreements are not found to be unreasonable, courts repeatedly have held that they do not violate the antitrust laws.”^[4] In the newly announced consent agreements, however, the FTC declined to assess the “duration or scope of the non-compete clauses.”^[5] Instead, the FTC “seems to treat the non-compete clauses as per se unlawful under Section 5 of the FTC Act”—a bridge further than any federal court has thus far gone.^[6]

The FTC's proposed “Non-Compete Clause Rule” would formalize the FTC's approach in the consent agreements as a regulation barring enforcement of non-compete clauses. The proposed regulation, 16 C.F.R. § 910, states that:

It is an unfair method of competition for an employer to enter into or attempt to enter into a non-compete clause with a worker; maintain with a worker a non-compete clause; or represent to a worker that the worker is subject to a non-compete clause where the employer has no good faith basis to believe that the worker is subject to an enforceable non-compete clause.

Proposed 16 C.F.R. § 910.2(a). The proposed regulation would require employers to rescind existing non-compete clauses and issue notice to current and former workers that those clauses will not be enforced. § 910(b). These requirements mirror the relief ordered in the three proposed consent agreements. *Compare id.*, with 88 Fed. Reg. 2618-02.

The proposed rule also makes clear that the term “worker” includes “independent contractors.” § 910.1(f).^[7] This aspect of the rule impacts direct sellers, which heavily rely on independent distributors that are often subject to non-compete clauses. Non-compete clauses protect direct sellers by ensuring that a distributor doesn’t misuse confidential company information when transitioning to a new company. Barring non-compete clauses would remove a tool that direct sellers use to build out and manage their distributors.

There are two pieces of good news though for direct sellers. *First*, the FTC’s proposed rule would not affect the enforcement of non-solicitation clauses or confidentiality/non-disclosure agreements unless such agreements are disguised non-compete clauses. Those types of restrictive employment covenants arguably are even more important to direct sellers because they prevent a distributor from misusing confidential information and from engaging in downline and customer raiding upon exit.

Second, as noted above, the consent agreements and proposed regulation are not yet final. The public can comment on the consent agreements through February 16, 2023, and the proposed regulation through March 10, 2023.^[8] Even once the public comment period closes, any FTC rule purporting to bar or restrict non-compete clauses would in all likelihood face extensive litigation prior to enforcement. Indeed, the U.S. Chamber of Commerce has already positioned itself to challenge the rule in court, publicly calling it “blatantly unlawful” and stating its confidence that “this unlawful action will not stand.”^[9]

The FTC’s proposed rule raises two major legal questions at the outset. *First*, does the FTC’s statutory authority to “make rules and regulations for the propose of carrying out the provisions of the FTC Act” permit it to redefine non-compete clauses as “[u]nfair methods of competition”? 15 U.S.C. §§ 45(a); 46(g). Under the major questions doctrine—a prudential rule of statutory interpretation that the Supreme Court expressly adopted in *West Virginia v. EPA*—the answer may very well be “no”: the FTC’s attempt to bar non-compete clauses would certainly have “vast economic and political” consequences if successful, and one would be hard pressed to find a “clear statement” in the FTC Act granting the FTC that authority.^[10] *Second*, even if the FTC has that authority, could an FTC anti-non-compete rule preempt state laws permitting non-compete clauses in defined circumstances? See Proposed 16 C.F.R. § 910.4 (purporting to supersede state laws inconsistent with § 910). That question in particular stands to delay enforcement by years because regulatory preemption of state law requires courts to consider, *inter alia*, whether the regulation actually conflicts, after attempted reconciliation, with the state law in question. Enforcement is far from imminent, giving companies time to prepare and adjust as necessary.

The FTC’s proposed consent agreements and anti-non-compete-clause regulation pose challenges for businesses—especially direct sales companies—that rely on non-compete clauses to protect their interests. See Winston’s related article in its [Competition Corner Blog](#) for more detail on the proposed rule and practical advice to prepare for its implementation.^[11] And of course, contact your Winston attorney if you have questions about the FTC’s new direction on non-compete clauses or if you would like assistance submitting a comment by the February 16 and March 10, 2023, deadlines.

^[7] Federal Trade Commission, *FTC Cracks Down on Companies that Impose Harmful Noncompete Restrictions on Thousands of Workers*, 2023 WL 34347 (Jan. 4, 2023); Glass Container Non-Compete Restrictions; Analysis of Agreements Containing Consent Orders to Aid Public Comment, 88 Fed. Reg. 2618-02 (Jan. 17, 2023).

^[8] 16 C.F.R. § 910: *Non-Compete Clause Rulemaking*, Federal Trade Commission (Jan. 5, 2023); see also 15 U.S.C. § 45.

^[9] Non-compete Clause Rule (NPRM), Regulations.Gov (Jan. 8, 2023), <https://www.regulations.gov/docket/FTC-2023-0007/document>; *Glass Container Non-Compete Restrictions; Analysis of Agreements Containing Consent Orders to Aid Public Comment*, Regulations.gov (Jan. 16, 2023), <https://www.regulations.gov/document/FTC-2023-0011-0001>.

^[10] 88 Fed. Reg. at 2623.

^[9] *Id.*

^[10] *Id.* (citing cases); see also, e.g., *Brock Servs., LLC v. Rogillo*, 936 F.3d 290, 296–97 (5th Cir. 2019) (analyzing the geographic scope of a non-compete clause under Louisiana law); *Clark v. Lauren Young Tire Ctr. Profit Sharing Trust*, 816 F.2d 480 (9th Cir. 1987) (commenting that a non-compete clause with “no temporal or geography limitations[] is arguably too broad on its face”); *Energy Recovery, Inc. v. Hauge*, 745 F.3d 1353, 1357–58 (Fed. Cir. 2014) (holding that employee did not violate non-complete restriction in part due to the limited “two-year duration”).

^[11] “Worker means a natural person who works, whether paid or unpaid, for an employer. The term includes, without limitation, an employee, individual classified as an independent contractor, extern, intern, volunteer, apprentice, or sole proprietor who provides a service to a client or customer.”

^[12] Non-compete Clause Rule (NPRM), Relgations.gov (Jan. 8, 2023), <https://www.regulations.gov/docket/FTC-2023-0007/document>; *Glass Container Non-Compete Restrictions; Analysis of Agreements Containing Consent Orders to Aid Public Comment*, Regulatoins.gov (Jan. 16, 2023), <https://www.regulations.gov/document/FTC-2023-0011-0001>.

^[13] *The FTC’s Noncompete Rulemaking Is Blatantly Unlawful*, U.S. Chamber of Commerce (Jan. 5, 2023), <https://www.uschamber.com/finance/antitrust/the-ftcs-noncompete-rulemaking-is-blatantly-unlawful>.

^[14] *West Virginia v. EPA*, 142 S. Ct. 2587, 2605, 2609 (2022). In that case, the Court explained that the term “major questions doctrine . . . took hold because it refers to an identifiable body of law that has developed over a series of significant cases all addressing a particular and recurring problem: agencies asserting highly consequential power beyond what Congress could reasonably be understood to have granted.” *Id.* at 2609.

^[15] Neely B. Agin, et al., *FTC Proposes Rule Prohibiting Most Non-Compete Clauses for “Workers,”* Winston & Strawn LLP: Competition Corner (Jan. 6, 2023), <https://www.winston.com/en/competition-corner/ftc-proposes-rule-prohibiting-most-non-compete-clauses-for-workers.html>.

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[John Sanders, Jr.](#)

[Katrina Eash](#)

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