What Does President Biden's Order on Noncompetes Mean for Employers?

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Employers should review their noncompete agreements and other restrictive covenants in light of a new executive order that aims to curb the use of these contracts in the workplace. The federal government has yet to issue any new rules, but employers should prepare for potential changes.

President Joe Biden recently signed an executive order (https://www.whitehouse.gov/briefing-room/statements-releases/2021/07/09/fact-sheet-executive-order-on-promoting-competition-in-the-american-economy/) that encourages the Federal Trade Commission (FTC) to ban or limit noncompete agreements. The order is meant to promote competition and economic growth by making it easier for workers to change jobs, among other objectives.

Employers generally use noncompetes to protect their proprietary information by preventing employees from working for competitors in a specific geographic area for a limited amount of time. But such agreements, particularly with low-wage earners in the retail and restaurant industries, have been scrutinized in recent years.

Carson Sullivan, an attorney with Paul Hastings in Washington, D.C., said there's a lot of debate about what the executive order means for noncompetes. "We really can't tell how broad the ban will be," she said, though she noted that the order focused on "unfair" use of noncompetes and other agreements that limit employee mobility.

"Most likely, the FTC will look to how various states have addressed the issue," noted Scott Mirsky, an attorney with Paley Rothman in Bethesda, Md. Some states, such as California, ban noncompete agreements outright, while other states, including Virginia, prohibit noncompete agreements with low-wage workers.

"Since the thrust of the executive order seems to protect the ability of lower-wage workers to obtain higher wages and better work conditions, a ban on noncompete agreements with low-wage workers may be the best approach for the FTC," Mirsky said.

What to Expect

"The [FTC] is going to take a long, hard look at noncompetes, and there is considerable momentum behind curtailing their use," said John Siegal, an attorney with BakerHostetler in New York City. "We expect the FTC will conduct a public inquiry process reviewing all of the legal, human resources and economic competitiveness issues around noncompetes, leading to a rulemaking process."

Anything the FTC does in this area will likely draw a legal challenge, he noted. "But the seriousness of such a challenge and the grounds will depend on how extensive the FTC reaches into contractual relationships between employers and employees."

Siegal said some changes may be relatively less controversial, such as requiring that employers provide noncompetes prior an employee's start date. "An outright ban on noncompetes, however, would draw considerable opposition from a wide array of industries and employers."

Don Schroeder, an attorney with Foley & Lardner in Boston, doesn't think a wholesale ban on noncompetes is likely, but he does think employers can realistically expect the government to narrow the employment categories for which such agreements can be used.

Jon Nadler, an attorney with Eckert Seamans Cherin & Mellott in Philadelphia, noted, "Regardless of the eventual outcome of the FTC rulemaking process, the fact that the president is highlighting the issue is likely to spur additional restrictions through legislation at the state level, which have been increasing steadily in recent years."

Michael Wexler, an attorney with Seyfarth in Chicago, expects legal challenges if the FTC attempts to make rules that will affect state autonomy or protections for business intellectual capital. "Because no rules have yet been promulgated, there is nothing a business should do other than make sure agreements and policies currently in place are up-to-date and comply with the law," he said.

Remember to Check State Law

As employers await direction from the federal government, they should note that the enforceability of noncompete agreements is generally evaluated under state laws. And those laws vary significantly.

"It's really important for employers to make sure they are aware of the applicable state laws," Schroeder said.

California, North Dakota and Oklahoma have banned noncompete agreements in most circumstances, and a new law in Washington, D.C., will also ban (https://www.jdsupra.com/legalnews/washington-d-c-prepares-to-implement-1766755/) the use of such agreements, with some exceptions.

Nearly a dozen other states prohibit noncompetes with low-wage earners (https://www.npr.org/2021/07/09/1014366577/biden-moves-to-restrict-non-compete-agreements-saying-theyre-bad-for-workers) or hourly workers. Massachusetts bans noncompetes (https://www.mass.gov/info-details/massachusetts-law-about-noncompetition-agreements) for certain professionals, such as nurses, physicians, social workers and employees in the broadcasting industry.

Additionally, in some states, an otherwise valid agreement may not be enforceable if the employee was laid off.

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Even where noncompetes are banned, employers may be able to use other so-called restrictive covenants that protect trade secrets and confidential information.

A nonsolicitation agreement, for example, may prohibit former employees from soliciting a company's clients after their employment ends. Employers in states such as California, however, should note that limits apply to these agreements, too.

Many states disfavor restrictive covenants but will allow their use if:

- There is a legitimate business interest that needs to be protected (such as trade secrets or customer lists).

- The agreement is narrowly tailored to protect that interest.

Employers also may consider using nondisclosure or confidentiality agreements to protect their trade secrets and proprietary information.

Tips for Employers

Employers should take this opportunity to review their processes for protecting confidential information and trade secrets, Sullivan said. There are many legitimate reasons why businesses choose to use restrictive covenants, she explained, and they should identify what their agreements restrict and which groups of employees are covered. Broader agreements may need to be revised.

To stay ahead of the curve, Nadler said, employers should reassess whether noncompete agreements are needed or whether legitimate concerns about protecting confidential information for certain employees can be addressed through other means, such as nonsolicitation agreements, which are more likely to survive scrutiny.

Siegal urged employers to keep up with changes. "The prospect of federal action on noncompetes makes it exponentially more important for employers to do what we've always advised them to do: Make sure you're using noncompetes in a targeted and narrowly tailored way to protect truly legitimate trade secrets and customer goodwill."